Office of
The City Attorney
City of San Diego

MEMORANDUM
MS 59

(619) 236-6220

DATE: September 18, 2015

TO: Honorable Mayor and City Councilmembers

FROM: City Attorney

SUBJECT: Interest Payments to the San Diego City Employees' Retirement System Associated with Underpaid Contributions or Overpaid Benefits

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INTRODUCTION

The San Diego City Council (Council), through its San Diego Charter (Charter) Review Committee, has asked for legal analysis related to the authority of the City of San Diego (City) to pay interest to the San Diego City Employees' Retirement System (Retirement System or SDCERS), on behalf of active employees, who unknowingly underpay their employee contributions to SDCERS, and on behalf of retired employees, who unknowingly receive overpaid benefits. The interest is charged by SDCERS in association with the underpayments or overpayments.

The SDCERS Board of Administration (Board) has submitted a proposal to the Council's Charter Review Committee. *See* Attachment 1. The Board is requesting placement of a proposed Charter amendment on a future ballot to allow the City to pay the interest and other amounts associated with errors by SDCERS staff members. The Charter Review Committee has asked whether the City can pay this interest, without the proposed Charter amendment.

QUESTIONS PRESENTED

1. Based on current law, can the City pay interest to SDCERS on behalf of active employees, who must make up underpaid employee contributions?

2. Based on current law, can the City pay interest to SDCERS on behalf of retired employees, who must repay overpaid benefits?

SHORT ANSWERS

1. No, unless the Charter is amended, as suggested by the Board, at Attachment 1. Charter section 141.2, which was added by voters approving Proposition B in 2012, states, in part: "The City shall not pay, cap the employee contribution rate, or otherwise compensate for any portion of a contribution to the Retirement System by a City Officer or employee." If an employee underpays a required contribution, then no interest is earned on that contribution. When the underpayment is discovered, the Retirement System fund must be made whole, which means both the underpaid contribution and the associated interest must be paid into the fund. The interest is associated with the employee contribution, and cannot be paid by the City because of the prohibition set forth in Charter section 141.2. Voter approval of the Board's proposal at Attachment 1 would be necessary to enable the Council to consider paying interest on behalf of employees who must make up contributions.

2. Yes, but the Council must first determine that there is a public purpose served by the payment of interest on behalf of retired employees who are overpaid benefits and must repay the Retirement System, with interest. There is no language in the Charter prohibiting the payment of interest; however, the Council must find that the payment of interest on behalf of retired employees serves a public purpose, and is not a gift of public funds, in violation of Charter section 93.

BACKGROUND

The Charter provides that the Council may, by ordinance, establish a defined benefit pension plan (DB Plan or Plan) for certain eligible employees. San Diego Charter § 141. Through the adoption of a series of ordinances, the Council has established the DB Plan, which includes the conditions of eligibility for and benefits of the Plan. *See* San Diego Charter § 141; San Diego Municipal Code (SDMC) §§ 24.0100 – 24.1905. The Council's ordinances must comply with the Charter, which, at article IX, sets forth the parameters of the DB Plan. *See* San Diego Charter, art. IX, §§ 140-151. The City's DB plan is set forth in the Charter and the ordinances adopted by the Council.

The City sponsors the DB Plan, and has specific obligations under it, including making an annual required contribution. SDMC § 24.0801. *See generally* San Diego Charter §§ 140-151. The Board administers the DB Plan and invests the DB Plan funds. San Diego Charter § 144. The costs and expenses of administering the Retirement System come from the DB Plan fund, which is composed of employee contributions, City contributions, and interest earned on the contributions. SDMC §§ 24.0906, 24.1501, 24.1502. *See also* San Diego Charter § 145. Pursuant to its duties, the Board may establish rules and regulations it deems proper, within the parameters of the Charter. San Diego Charter § 144.

The Board has established an Underpayments Policy and an Overpayments Policy, consistent with Internal Revenue Service (IRS) regulations and procedures. *See* Attachment 2. The Underpayments Policy addresses situations where a City employee has underpaid contributions to the DB Plan. The Overpayments Policy addresses situations where SDCERS overpays a

retired City employee. The City has never voluntarily paid interest on behalf of employees. However, prior to adoption of the Underpayments and Overpayments Policies, the Board recovered funds due to errors through the Unfunded Actuarial Liability (UAL).[1]

SDCERS has advised that it can no longer correct the underpaid contributions or overpaid benefits by charging the City through the amortized UAL. *See* Attachment 1. Therefore, SDCERS presently collects the full underpaid contribution or overpaid benefit, plus interest at the DB Plan's earnings rate, from the active or retired member, not from the City.

SDCERS is proposing that a Charter amendment be presented to voters, providing enabling language for the Council, if it desires, to enact an ordinance, authorizing City payment to SDCERS of any portion of an overpayment of benefits to or underpayment of contributions by members and the associated interest, when the overpayment or underpayment is caused by the fault or negligence of SDCERS employees. In the July 13, 2015 letter to the Charter Review Committee Consultant, SDCERS Chief Executive Officer Mark Hovey writes: "The SDCERS Board of Administration would like for the City to consider playing a role in resolving such underpayments/overpayments." Attachment 1.

DISCUSSION

I. SDCERS HAS A LEGAL DUTY TO CORRECT ITS ERRORS AND MAKE THE RETIREMENT SYSTEM "WHOLE" WHEN THERE ARE OVERPAID BENEFITS TO RETIRED EMPLOYEES OR UNDERPAID CONTRIBUTIONS BY ACTIVE EMPLOYEES.

The questions presented here relate to situations where SDCERS commits an error, resulting in an active member, who is a City employee, underpaying his or her contribution, or a retired employee receiving an overpaid benefit. In his July 13, 2015 letter, Mr. Hovey explains: "SDCERS works diligently to make zero mistakes, and while we successfully and accurately process hundreds of thousands of transactions each year, our staff members are not perfect. When the mistakes have been made, the error is usually the results [sic] of a step or process not done correctly by an SDCERS staff member, rather than due to an error made by the member, or the City." Attachment 1.

The Board has the duty to administer the Retirement System within the parameters of the Charter, ordinances adopted by the Council, and applicable federal and state laws, including the Internal Revenue Code and article XVI, section 17(a) of the California Constitution, which sets forth the fiduciary duties of public retirement systems in California. *See City of San Diego v. San Diego City Employees' Retirement System*, 186 Cal. App. 4th 69, 72 (2010) (holding that SDCERS actions to charge the City for underfunded pension service credits purchased by City

[1] In 2008, the Board amended the Underpayments and Overpayments Policies to require the City, as Plan sponsor, to pay the difference between an interest rate of two percent charged to members and the actuarial assumed rate in effect when the underpayment or overpayment is resolved. The City objected to the 2009 amendments because the City is not legally required to pay employee's contributions or to pay interest on overpaid benefits. In 2009, SDCERS revised its policies to recover the entire interest amount from the active or retired members.

employees was "contrary to law" and SDCERS "exceeded its authority to administer the pension system's assets"). SDCERS does not have "plenary authority to evade the law." *Id.* at 78-79. Therefore, SDCERS must correct its errors. *In re Retirement Cases*, 110 Cal. App. 4th 426, 450-51 (2003). Further, employees do not have a right to erroneous or improper benefits. *Id.*

The Board adopted its Underpayments and Overpayments Policies to ensure compliance with IRS correction procedures, which require that the Retirement System be made whole when there is an error resulting in underpaid contributions or overpaid benefits. *See* IRS Revenue Procedure 2008-50, § 6.06(3), and Appendix B, § 2.04(1). Under IRS regulations, the error must be corrected; SDCERS must collect the underpaid contribution or the overpaid benefit and "appropriate interest" from the active or retired employee, or from the City or another person. Revenue Procedure 2008-50, § 6.06(3), and Appendix B. *See* Attachments 1, 3. Mr. Hovey explains that SDCERS collects interest from the Retirement System member, at a rate equal to the SDCERS assumed rate of investment return, which is currently 7.25 percent, when an active member underpays a contribution or when a retired member is overpaid a benefit. The City's ability to offset the funds owed the Retirement System when there is an error is limited by the Charter.

II. THE CHARTER PROHIBITS THE CITY FROM PAYING ANY PORTION OF AN EMPLOYEE'S CONTRIBUTION TO THE RETIREMENT SYSTEM, WHICH INCLUDES INTEREST ON UNDERPAID CONTRIBUTIONS.

As a charter city, the City must act within the limitations and restrictions set forth in the Charter. *City of Grass Valley v. Walkinshaw*, 34 Cal. 2d 595, 598 (1949). *See also Domar Electric, Inc. v. City of Los Angeles*, 9 Cal. 4th 161, 170 (1994). The Charter is the City's constitution, and the City, acting through its officers and employees, must comply with it. *Miller v. City of Sacramento*, 66 Cal. App. 3d 863, 867 (1977) ("A city charter is like a state constitution but on a local level; it is a limitation of, not a grant of power."). *See also City & County of San Francisco v. Patterson*, 202 Cal. App. 3d 95, 102 (1988) (the charter is to the city what the state constitution is to the state). The Council cannot act in conflict with the Charter. "Any act that is violative of or not in compliance with the charter is void." *Domar Electric, Inc.*, 9 Cal. 4th at 171.

As established by the Charter, the DB Plan is a contributory plan, meaning the City contributes funds jointly with the employees who will receive benefits when they retire. San Diego Charter § 143. All money contributed to or earned by SDCERS must be placed in a special trust fund to be held and used only for the purpose of carrying out the provisions of the Charter related to the DB Plan. San Diego Charter § 145. The trust fund is composed of employee contributions, City contributions, and investments earnings. *Id.* The Board invests the City's and employees' contributions and credits interest to the contribution accounts of active employees and the City at a rate determined by the Board. SDMC § 24.0904.

The Charter provides that employees must contribute according to actuarial tables adopted by the SDCERS Board. San Diego Charter § 143. Employees make regular contributions based on their age at their birthday closest to the date when they join SDCERS. SDMC §§ 24.0201(a),

24.0301(a).[2] Employee contribution rates are established by the Board, based on advice of the Retirement System's actuary "according to the age at the time of entry into the Retirement System." SDMC §§ 24.0202, 24.0302. The Board also establishes maximum and minimum rates of contribution. SDMC §§ 24.0203, 24.0303. Employees' contributions are deducted from their biweekly paychecks and transferred to SDCERS for crediting to the individual employee's account. SDMC §§ 24.0204, 24.0304. The employees' contributions are credited with interest, at a rate determined by the Board. SDMC §§ 24.0902, 24.0904.

The City must contribute annually "an amount substantially equal to that required of the employee for a normal retirement allowance, as certified by the Actuary . . . but shall not contribute in excess of that amount, except in the case of financial liabilities accruing under any new retirement plan or revised retirement plan because of past service of the employee." San Diego Charter § 141.2. *See also* San Diego Charter § 143. In calculating annual contributions for the City and City employees, the Board must divide equally between the City and City employees "all costs except those costs explicitly and exclusively reserved to the City." San Diego Charter § 141.2. This section also states: "The City shall not pay, cap the employee contribution rate, or otherwise compensate for any portion of a contribution to the Retirement System by a City Officer or employee." *Id.* Charter section 141.2 was added by City voters, who approved Proposition B, in June 2012.

If employees are regularly contributing to SDCERS through payroll deductions, their contributions are invested by SDCERS in a timely manner and their retirement accounts are regularly credited with the interest, which is drawn from investment earnings. SDMC § 24.0904. However, if SDCERS staff make a mistake in entering an employee's birthdate or other clerical error that results in the employee underpaying the required normal contribution, then the employee must, when the error is discovered, make up the contribution and associated interest, under the Underpayments Policy.

Given the limitations set forth in the Charter, it is clear that employees must make up their underpaid contributions and the City cannot offset them. However, the question of whether the City can pay the interest associated with an underpayment turns on whether the interest is included in the prohibition against the City offsetting employee contributions, as set forth in Charter section 141.2.

Construction of a written law is a legal issue for a court to determine. *Woo v. Superior Court*, 83 Cal. App. 4th 967, 974 (2000). A court reviews a measure adopted by voters, like Proposition B, in the same manner as it interprets statutes. *Howard Jarvis Taxpayers Ass'n v. County of Orange*, 110 Cal. App. 4th 1375, 1381 (2003). *See also City of San Diego v. Shapiro*, 228 Cal. App. 4th 756, 790 (2014). The voters' intent in approving a measure is a court's "paramount concern." *Woo*, 83 Cal. App. 4th at 975. In interpreting a charter provision, a court

[2] It is this Office's understanding that a number of the errors SDCERS makes are related to incorrect data entry or reporting of birth year, which can change the contribution rate.

will look first to the words of the adopted provision. *Id.* "We construe the words from the perspective of the voters, attributing the usual, ordinary, and commonsense meaning to them; we do not interpret them in a technical sense or as terms of art." *Howard Jarvis Ass'n,* 110 Cal. App. 4th at 1381.

If the language is clear and unambiguous, there is no need for further interpretation: "[w]e presume that the voters intended the meaning apparent on the face of the measure, and our inquiry ends." *Woo,* 83 Cal. App. 4th at 975.

As the California Supreme Court (Supreme Court) recently explained, a reviewing court will look first to the plain meaning of the relevant language, "affording the words of the provision their ordinary and usual meaning and viewing them in their statutory context." *Poole v. Orange County Fire Authority*, 61 Cal. 4th 1378, 1384 (2015). The plain meaning controls if there is no ambiguity. *Id.* at 1385 (citing *People v. Cornett*, 53 Cal. 4th 1261, 1265 (2012)).

The Supreme Court explained that the task of a reviewing court is "to select the construction that comports most closely with the Legislature's apparent intent, with a view to promoting rather than defeating the statutes' general purpose, and to avoid a construction that would lead to unreasonable, impractical, or arbitrary results." *Copley Press, Inc. v. Superior Court*, 39 Cal. 4th 1272, 1291 (2006).

But, if the words of a statute or charter provision are not clear, then a court will look to the overall context of the provision and extrinsic evidence if necessary. "We do not interpret statutes (or charter provisions) in isolation. Rather, we must construe every statute with reference to the entire scheme of law of which it is part so that the whole may be harmonized and retain effectiveness." *Mason v. Retirement Bd.*, 111 Cal. App. 4th 1221, 1229 (2003) (citations and internal quotation marks omitted).

"The information and arguments contained in the official ballot pamphlet may indicate the voters' understanding of the measure and their intent in passing it." *Woo*, 83 Cal. App. 4th at 976. "The historical context in which the provision was adopted also is relevant." *Id.* at 976-77.

Applying these rules of interpretation to the current issues, the term "contribution" is not defined in Charter section 141.2. It is unclear what is meant or included in a "contribution." The word "contribution" is generally defined as "[s]omething that one gives or does in order to help an endeavor be successful." *Black's Law Dictionary* 402 (10th ed. 2014). Another definition is "[a]n amount of money one gives in order to help pay for something." *Id.* A third definition is a "regular payment one makes to one's employer or to the government to help pay for one's future benefits such as social security, a pension, etc." *Id.*

The plain meaning of contribution does not resolve what is included in the offsetting prohibition under Charter section 141.2. Therefore, a court will look to the overall provision in context, and the voters' intent.

The ballot question for Proposition B asked, in part: "Should the Charter be amended to: . . . require substantially equal pension contributions from the City and employees . . . ?" Ballot Pamp., Primary Elec. (June 5, 2012).[3] The ballot summary stated that the measure would "[r]equire the City to contribute annually to the defined benefit pension plan an amount substantially equal to that required of the employee for a normal retirement allowance, but not contribute in excess of that amount." *Id.* The argument in favor of Proposition B stated, "YES on Proposition B guarantees that government employees pay a fair share of their pension costs, and it ends the practice of City taxpayers subsidizing the employees' share of pension costs." *Id.* Thus, the voters intended to eliminate any ability of the City to pay for or offset any of an employee's required contribution.

Further, when Proposition B was adopted, the DB Plan treated, as it still does, the biweekly contributions paid by employees and the interest credited to the employees' accounts on investment earnings as interrelated. "Normal Contributions" are defined by Council ordinance as "contributions by a Member at the normal rates of contribution." SDMC § 24.0103.[4] "Accumulated Normal Contributions" are defined by ordinance as "all normal contributions standing to the credit of a Member's individual account and interest thereon." *Id.*

Further, if an employee leaves City service prior to retirement, the employee may withdraw all accumulated contributions, plus compound interest. SDMC §§ 24.0206, 24.0306. Employees' retirement allowances consist of two elements: a service retirement annuity, which is the actuarial equivalent of the member's accumulated normal contributions, meaning actual contributions plus interest, and a creditable service pension, which is derived from the City's contributions. SDMC §§ 24.0402, 24.0403.

It could be argued that the interest associated with an underpaid employee contribution is separate from the contribution and not covered by Charter section 141.2. However, applying the well-established rules of construction described here, it is this Office's view that a reviewing court would find payment of interest associated with an underpaid employee contribution by the City as a violation of Charter section 141.2, because the City would be offsetting a required employee contribution.

The conclusion that a court would likely find that employee contributions, within the meaning of Charter section 141.2, includes interest associated with the contributions is consistent with the holding in the *Barrett v. Stanislaus County Employees Retirement Ass'n*, 189 Cal. App. 3d 1593 (1987). The *Barrett* case involved a dispute over the proper classification of 21 employees in the Stanislaus County sheriff's department. *Id.* at 1597. The employees were classified as miscellaneous members of the Stanislaus County Employees Retirement Association; however, they argued that they should be classified as safety members because they were engaged in

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[3] http://www.sandiego.gov/city-clerk/pdf/pamphlet121221.pdf

[4] A "Member" is "any person employed by the City who actively participates in and contributes to the Retirement System, and who will be entitled, when eligible, to receive benefits from the System." SDMC § 24.0103.

active law enforcement duties as work program staff at the county honor farm. *Id.* The trial court granted the employees' peremptory writ of mandate and directed the retirement system board to reclassify the employees as safety members. *Id.* at 1598. The appellate court affirmed the trial court's decision. *Id.* at 1599.

The retirement system then filed a return to the peremptory writ of mandate, arguing in part that

> an eligible member should not receive credit as a safety member for prior service as a Work Program Supervisor unless the member contributes the additional contributions, including contributions of interest, which the member would have made if he had been treated as a safety member from his initial date of service in that position.

Id. at 1599. The employees contended, in part, that the retirement system had no statutory or common law power to demand arrears contributions for members who were misclassified through no fault of their own and the retirement board was not entitled to any interest on the contributions. *Id.* at 1600.

The trial court agreed with the employees, finding that the retirement system had no legal authority, power, or ability under the County Employees Retirement Law of 1937 (1937 Act) to request arrears contributions of principal and interest in cases where the retirement system erroneously misclassified employees. *Id.* at 1600-01. The trial court also concluded that it would be unfair and inequitable to require the plaintiff employees to make repayments to the retirement system, which was primarily responsible for the alleged arrearage through its own actions. *Id.* at 1601. The appellate court reversed the trial court, and concluded that the retirement system could obtain the arrears contributions and interest. *Id.* at 1600, 1608, 1613-14. The court explained:

> In the instant case, the defendants retroactively reclassified plaintiffs as safety members but have conditioned their higher pension benefits on the deposit of their share of arrears contributions plus applicable interest. Plaintiffs have been deprived of nothing for which they bargained. Rather, they have merely been required, by defendants, to pay their quid pro quo. They will receive the higher pension benefits retroactively but are required, as are all other safety members, to pay retirement contributions commensurate with the formula contributions paid by all other safety members during the entire course of their employment.

Id. at 1608.

In that case, the court of appeal analyzed the 1937 Act, which establishes retirement benefits for county employees throughout California and has a contributory system, funded by both employee contributions and employer contributions, with no requirement that the employer pay the employee's share, which is similar to this City's Retirement System. The *Barrett* court stated:

"A public officer may only collect and retain such compensation as is specifically provided by law and any money paid by a governmental agency without authority of law may be recovered from such officer." *Barrett*, 189 Cal. App. 3d at 1602 (citing *County of San Diego v. Milotz*, 46 Cal. 2d 761, 767 (1956)).

The *Barrett* court explained that, as a general rule, "pension legislation should be liberally construed, resolving all ambiguities in favor of the [member]." *Id.* at 1608. "However, this rule of liberal construction is applied for the purpose of effectuating the *obvious legislative intent* and should not blindly be followed so as to eradicate the clear language and purpose of the statute and allow eligibility for those for whom it was obviously not intended." *Id.* at 1608-09. After concluding that the work program employees in the sheriff's department were eligible for safety member retirement status, the court of appeal further concluded that the reclassified employees must make up the arrears contributions.

> A review of the entire statutory scheme reveals a retirement system based on contributions by both employer and employee. Thus, imposition of an arrears contributions obligation on plaintiffs would place them in the position they would have been had they been properly classified from the date of their employment. Plaintiffs contend such an obligation would result in a "drastic financial impact" because they would have to pay up to 20 years of contributions including interest over a relatively brief period of time. Plaintiffs infer they will have to bear the entire burden of arrears contributions. However, in light of the statutory scheme, the County of Stanislaus would also be required to contribute its share of retroactive contributions to fund the plaintiffs' retirement as safety members.

Id. at 1609.

The court of appeal also found that the payment of interest by the employees for the lost investment earnings was appropriate.

For investment purposes, retirement funds under the 1937 Act are invested as a whole; the contributions of a county and the members are not invested separately. *Id.* at 1611. When a member retires, he or she is entitled to a retirement allowance based on an annuity, which is the actuarial equivalent of the member's accumulated contributions at the time of retirement, meaning the principle contributed and interest credited to the member's account, and a pension, which is composed of the county contributions. *Id.* at 1611-12. "Upon the retirement of a member, a county must match the interest which has been credited upon the member's contributions as well as the contributions themselves." *Id.*

The court agreed with the retirement system that the interest earned on employee contributions was part of the employee contribution. "A review of the entire statutory scheme reveals a retirement system based upon contributions by both employer and employee and the crediting of

interest on contributions by both employer and employee. . . . Thus, both employer and employee will be required to contribute interest." *Id.* at 1612. The court concluded that the retirement system could properly require the employees to pay regular interest on their arrears contributions to obtain their retirement benefits. *Id.*

Likewise, here, an employee who underpays a contribution must make up the contribution and interest on the contribution to obtain benefits. The City cannot offset the payment because of the language in Charter section 141.2, which states: "The City shall not pay, cap the employee contribution rate, or otherwise compensate for any portion of a contribution to the Retirement System by a City Officer or employee." San Diego Charter § 141.2.

Based on the letter submitted by Mr. Hovey, the Board also interprets Charter section 141.2 as a limitation on the City's ability to pay to SDCERS any portion of an underpayment or overpayment and the associated interest. That is why the Board is requesting that the City consider placing an amendment to Charter section 141.2 on the 2016 ballot to provide enabling language for the proposed ordinance, allowing for the City to pay interest on behalf of members. The Board is proposing to amend Charter section 141.2 to add the following language:

> Nothing contained in this Section or in Section 143 shall preclude the City from agreeing to pay to the Retirement System any portion of an overpayment of benefits or underpayment of contributions, and any interest associated with an overpayment or underpayment as assessed by the Board of Administration, where the overpayment or underpayment was proximately caused by the fault or negligence of a City employee acting in the course and scope of his or her employment. The Council of the City is hereby authorized and fully empowered to enact any and all ordinances necessary to carry into effect the provisions of this section and any and all ordinances so enacted shall have equal force and effect with this Article and shall be construed to be part hereof as fully as it drawn herein. Any ordinance enacted pursuant to this section shall not be considered an ordinance affecting or enhancing the benefits of any active or retired Member of the System and shall not be subject to the voting requirements set forth in Section 143.1.

Attachment 1.

A Charter amendment, if approved by voters, would provide enabling authority for the Council to adopt an ordinance to allow the City to pay interest, which is presently prohibited by Charter section 141.2. Conversely, without an amendment to Charter section 141.2, the City is without authority to pay any interest to SDCERS on behalf of active employees.

III. IF THE COUNCIL DESIRES TO INDEMNIFY, OR COMPENSATE, EMPLOYEES WHO ARE ARGUABLY HARMED BY THE ERRORS OF SDCERS, IT MUST ACT WITHIN THE PARAMETERS OF THE CHARTER.

Under the California Government Claims Act, specifically California Government Code section 815.2,[5] a public entity, like the City, may be held vicariously liable for the negligence of its employees acting in the scope of their employment. Employees are defined as officers, employees, or servants, but not agents or independent contractors. Cal. Gov't Code § 810.2.[6] This vicarious liability "flows from the responsibility of such an entity for the acts of its employees under the principle of respondeat superior." *San Diego City Firefighters, Local 145 v. Board of Administration*, 206 Cal. App. 4th 594, 611 (2012). The City cannot be liable for employees not under its control. Further, there is immunity for discretionary acts or omissions. Cal. Gov't Code § 820.2.[7]

The Council recognizes SDCERS as a City department: "City Retirement." SDMC § 22.1801. But SDCERS is also recognized as a separate legal entity under the provisions of article XVI, section 17, of the California Constitution, with specific fiduciary duties, separate and apart from those of the City, as a municipal corporation and the Plan sponsor.[8] *See* SDMC § 24.0901. *See also Lexin v. Superior Court*, 47 Cal. 4th 1050, 1063 (2010) ("Although established by the City, the [SDCERS] Board is a separate entity."); *City of San Diego v. Haas*, 207 Cal. App. 4th 472, 480 (2012)(SDCERS is separate legal entity).

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[5] California Government Code section 815.2 states:

(a) A public entity is liable for injury proximately caused by an act or omission of an employee of the public entity within the scope of his employment if the act or omission would, apart from this section, have given rise to a cause of action against that employee or his personal representative.

(b) Except as otherwise provided by statute, a public entity is not liable for an injury resulting from an act or omission of an employee of the public entity where the employee is immune from liability.

[6] To prevail on a negligence claim, a plaintiff must prove that the public entity owed a legal duty to the plaintiff, breached the duty, and the breach was the proximate or legal cause of the injuries. *Wilson v. County of San Diego*, 91 Cal. App. 4th 974, 979 (2001). The duty must be statutory in nature and obligatory or mandatory, not merely discretionary or permissive. *Id.* at 980.

[7] California Government Code section 820.2 states: "Except as otherwise provided by statute, a public employee is not liable for an injury resulting from his act or omission where the act or omission was the result of the exercise of the discretion vested in him, whether or not such discretion be abused." *See also Nasrawi v. Buck Consultants LLC*, 231 Cal. App. 4th 328, 342 (2014)(immunity for policymaking but not for execution of ministerial tasks).

[8] The Board has "exclusive control" and fiduciary responsibility for administration and investment of the DB Plan funds, as set forth in the Charter section 144 and in article XVI, section 17 of the California Constitution. *See also* SDMC § 24.0901. The Constitution distinguishes between the board of a public retirement system and "the elected legislative body of a jurisdiction which employs participants in a public employees' pension or retirement system." Cal. Const. art. XVI, §17.

SDCERS employees act under the control of the chief executive officer, who is appointed by the Board and serves under the Board. *See* San Diego Charter § 144 (stating the Board may appoint employees as may be necessary). The Board has "exclusive control of the administration and investment" of the retirement fund. *Id.* And the Board has discretion to delegate appropriate responsibilities to staff. *See* SDCERS Board Charter.[9]

Neither the Mayor nor the Council has supervision or control over the SDCERS staff. [10] The City, as a municipal corporation, could only be held vicariously liable for the negligence of SDCERS employees as a joint employer or special employer. But without control over SDCERS staff, a joint or special employment relationship fails to exist. The Supreme Court recently explained: "It is settled that the right to control job performance is the primary factor in determining any employment relationship, including special employment." *State ex rel. Dept. of California Highway Patrol v. Superior Court*, 60 Cal. 4th 1002, 1012 (2015). *See also Jones v. County of Los Angeles*, 99 Cal. App. 4th 1039, 1047 (2002) (county not joint employer of court employees even though paychecks are drawn from county and benefits are similar because the court, not the county, had the right to control the duties the employee performed).

Further, the Council cannot agree to indemnify or compensate City employees allegedly harmed by errors of SDCERS staff, if the agreement violates the Charter, as explained earlier. Claims for equitable relief also will not stand if they are contrary to the express provisions of the Charter. "[N]either the doctrine of estoppel nor any other equitable principle may be invoked against a governmental body where it would operate to defeat the effective operation of a policy adopted to protect the public." *San Diego City Firefighters, Local 145*, 206 Cal. App. 4th at 610.

In the *Barrett* case, the court of appeal rejected the employees' argument that equitable considerations barred the defendant retirement system from demanding arrears contributions, which included principal and interest. *Barrett,* 189 Cal. App. 3d at 1608. The court stated:

> A fundamental maxim of jurisprudence is that equity must follow the law. Equity is bound by rules of law; it is not above the law and cannot controvert the law. Equity penetrates beyond the form to the substance of the controversy, but is nonetheless bound by the prescriptions and requirements of the law. While equitable relief is flexible and expanding, its power cannot be intruded in matters that are plain and fully covered by positive statute. A court of equity will not lend its aid to accomplish by indirect action what the law or its clearly defined policy forbids to be done directly.

Id. at 1608 (citations omitted).

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[9] https://www.sdcers.org/Sdcers-Documents/Board_CPRR_final_050815.aspx

[10] Staff appointments to SDCERS are made under the provisions of article VIII of the Charter, meaning the City's Civil Service Rules must be followed. San Diego Charter § 144. If a classified employee at SDCERS is terminated for cause, the employee has appeal rights to the Civil Service Commission. San Diego Charter § 115. But this does not mean that the employee is under the supervision and control of City officers or employees.

As explained above, as a matter of law, the Charter prohibits the City's payment of employee contributions, which include interest assessed on underpaid contributions. A court is unlikely to find the City liable for these interest payments based on either legal or equitable grounds.[11]

IV. THE CHARTER DOES NOT PROHIBIT PAYMENT OF INTEREST ON BEHALF OF RETIREES WHO ARE OVERPAID BENEFITS, BUT THE COUNCIL MUST FIND THAT THERE IS A PUBLIC PURPOSE FOR THE PAYMENT.

There is no provision in the Charter expressly prohibiting the City from paying assessed interest on an overpaid benefit to retired employees, who must repay the benefit. However, the Charter prohibits the giving of "credit . . . to or in the aid of any individual, association or corporation." San Diego Charter § 93. This provision is consistent with the prohibition in article XVI, section 6 of the California Constitution on the gift of public funds. Generally, there must be a public purpose established by the legislative body to justify the use of public resources in a specified manner. *See Tevis v. City & County of San Francisco*, 43 Cal. 2d 190, 197 (1954) (charter provision defining gift of public funds prevails over constitutional provision); *City & County of San Francisco v. Patterson*, 202 Cal. App. 3d 95, 103-104 (1988). The expenditure of funds to settle a good faith dispute is an appropriate use of public funds; however, the compromise of an invalid claim serves no public purpose. *Page v. Mira Costa Comm. College Dist.*, 180 Cal. App. 4th 471, 495 (2009).

To pay interest on behalf of retired employees who receive overpaid benefits, the Council must determine that there is a public purpose served. If other avenues to obtain repayment of the overpaid benefit and interest have been exhausted, there may be a public purpose served by the City making the Retirement System whole and viable. However, this is for the Council to determine.

CONCLUSION

The Charter prohibits the City from paying interest on behalf of employees who underpay their contributions to SDCERS. If the Council desires to provide an option for employees who unknowingly underpay their contributions and then are faced with the contribution and interest payment later, then the Council must consider placement of a Charter amendment on the ballot, as recommended by SDCERS.

While the City cannot pay contributions, including principal and interest, on behalf of City employees because of the prohibition set forth in the Charter, the City can request that SDCERS resolve errors expeditiously so that errors do not compound. Further, Mr. Hovey suggests that there may be other solutions, such as the purchase of insurance to cover the errors of SDCERS employees.

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[11] This memorandum does not discuss whether individual City employees could state a cause of action against SDCERS for errors committed by SDCERS employees.

There is no express prohibition on the payment of interest on behalf of retired employees who receive overpaid benefits, except that the City must determine that there is a public purpose for the payment, in accordance with Charter section 93. This Office will provide further analysis on any issues set forth in this memorandum, at the request of the Mayor or Council.

JAN I. GOLDSMITH, City Attorney

By *\/s/ Joan F. Dawson*
Joan F. Dawson
Deputy City Attorney

JFD:jdf:ccm
MS-2015-15
Doc. No.: 1111436
Attachments (3)

ATTACHMENT 1

SDCERS
San Diego City Employees' Retirement System

Mark A. Hovey
Chief Executive Officer

July 13, 2015

Mr. Steven Hadley
Charter Review Committee Consultant
for Council President Sherri Lightner
City Administration Building
202 C Street
San Diego, CA 92101

Dear Mr. Hadley:

On January 30, 2015, I provided the enclosed letter to Scott Chadwick providing SDCERS' suggestions for revisions to City Charter Article IX. The Charter Review Committee graciously allowed the SDCERS Board of Administration ("SDCERS Board") additional time to review and provide additional suggestions. The SDCERS Board has now completed its review.

SDCERS has received requests from both the San Diego Unified Port District ("UPD") and the San Diego County Regional Airport Authority ("Airport") to provide Charter language allowing UPD and Airport employees the opportunity to run for the elected seats on the SDCERS Board. The SDCERS Board concurs with this request.

Enclosed are SDCERS' proposed updates and modifications to Article IX of the City Charter. In addition to the suggestions made in my January 30, 2015 letter, the SDCERS Board has requested the following revisions:

- Amend Charter Section 141 to provide that nothing contained in Section 141 or Section 143 of the Charter will preclude the City of San Diego from agreeing to pay to SDCERS any portion of an overpayment or underpayment, and associated interested assessed by the Board, where the overpayment or underpayment was proximately caused by the fault or negligence of a City employee acting in the course and scope of his or her employment. The Council would be empowered to enact any and all ordinances necessary to put this provision into effect. Any ordinances enacted pursuant to this amendment would not be subject to a Charter Section 143.1 vote of the membership or the electorate.
- Amend Charter Section 144 to include in the eligibility requirements for appointment to the Board 15 years of legal experience related to the practice of law in any of the fields listed (i.e., pension administration, pension actuarial practice, investment management, real estate, banking or accounting).

- Amend Charter Section 144 to allow general, safety and retired members of Contracting Public Agencies to run for election and vote in elections for the elected positions on the SDCERS Board of Administration.

SDCERS is suggesting that the Charter be amended to allow the City to enact an ordinance, at its discretion, allowing the City to pay SDCERS for any portion of an overpayment of benefits to or underpayment of contributions from members and associated interest where the overpayment or underpayment was caused by the fault or negligence of a City employee. SDCERS' employees are City employees.

SDCERS works directly with its members to resolve any active member underpayments to the pension system, or retired member benefit overpayments (both collectively referred to as "overpayments"). Due to IRS requirements, SDCERS also collects interest from the members on the overpayment, at a rate equal to the SDCERS assumed rate of return (currently 7.25%). The SDCERS Board of Administration would like for the City to consider playing a role in resolving such underpayments/overpayments.

To provide perspective on this issue, SDCERS works diligently to make zero mistakes, and while we successfully and accurately process hundreds of thousands of transactions each year, our staff members are not perfect. When the mistakes have been made, the error is usually the results of a step or process not done correctly by an SDCERS staff member, rather than due to an error made by the member, or the City.

IRS rules require that in the event of an overpayment, SDCERS resolve the overpayment by collecting the full principal amount, with interest at the plan's earnings rate, to make the system "whole." Consistent tax advice from SDCERS outside counsel advises that we have been following the IRS corrections process accurately since SDCERS received its IRS Determination Letter of plan compliance back in 2008.

Members frequently comment to SDCERS that if the mistake was not due to their (i.e., the member's) error, why are they doubly "penalized" by assessing interest on the amount. Indeed, SDCERS implemented a policy in 2008 to comply with IRS overpayment requirements and decided to charge the member a lower interest rate . . . 2% . . . and have the balance of the interest due be covered by the City. Following correspondence between SDCERS and the City Attorney's office, who clearly conveyed that the City and taxpayers could not be held responsible for resolving overpayments to the member, SDCERS revised its policy in 2009 to recover the entire interest amount from the member and has consistently done so since then.

It has been suggested SDCERS procure insurance to cover such errors, rather than have the member repay the error in full. However, insurers have stated deductibles would be involved that exceed the cost of the overpayment, and even if the overpayments were to exceed the deductible, the insurance company retains subrogation rates to pursue a counter claim against the City. In short, insurance might transfer a portion of the burden off the member, but that burden would be placed back on the City, regardless.

It has also been suggested SDCERS simply fix the overpayment issue prospectively, and historical overpayment amounts be left in the City's Unfunded Actuarial Liability (UAL).

Unfortunately, the IRS explicitly does not allow the plan sponsor to cover overpayments via an amortized UAL phased into the City's annual pension payments. Instead, the City, per IRS rules, must immediately cover any portion of the overpayment not made by the member.

As noted above, the SDCERS Board believes the IRS effectively ties its hands and that full recoupment of the overpayment, with interest, is required from the member. However, the Board also believes that given the underlying cause of the error has traditionally been made by SDCERS, an agent of the City in this case, that it may be prudent for the City to acknowledge the impossibly high standard of perfection placed on its employees and agree to shoulder a portion of the overpayment.

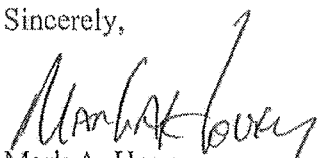
It's difficult to assess the amount of money involved in prospective overpayment corrections to be done by SDCERS (i.e., it is not possible to predict future overpayment errors). However, SDCERS does report annually on the number and amount of overpayments collected from members. In FY 2013, that amount was $701,171, which included $611,501 associated with the PSC Litigation lawsuit the City won against SDCERS. In FY 2014, SDCERS collected $150,788 in member overpayments. There are approximately 300 potential member overpayment issues that SDCERS is researching now, and we expect to resolve those by December 31, 2015; this relatively large number of open matters was primarily driven by the complete data conversion audit when SDCERS covered to its new pension system in May 2014. Going forward, we expect overpayments to be limited in number and not material.

As previously advised, SDCERS believes the majority of the remaining proposed Charter modifications are required to achieve consistency with the Board's fiduciary duties as well as consistency between provisions in other Articles of the Charter. SDCERS is also proposing that the City amend the Charter to allow Police Recruits to join SDCERS upon entering the Police Academy. Not only does SDCERS believe that this was the actual intent of the proposers of Proposition B, but that it will also assist the City in its retention of new police officers.

The SDCERS Board of Administration respectively requests the City review applicable City Charter language to allow for flexibility in resolving member overpayments with the City.

SDCERS would be happy to appear before the Charter Review Committee if requested. Thank you for your consideration.

Sincerely,



Mark A. Hovey
Chief Executive Officer

MAH/er

Enclosure: SDCERS' Proposed Revisions to the City Charter

cc: SDCERS Board of Administration
Elaine Reagan, SDCERS Deputy CEO – Compliance & Legal Operations
Hon. Council President Sherri S. Lightner
Hon. Mayor Kevin Faulconer
Scott Chadwick, Chief Operating Officer
Hon. Jan Goldsmith, City Attorney
Paul Cooper, Asst. City Attorney
Sharon Spivak, Deputy City Attorney
Roxanne Story Parks, Deputy City Attorney

SDCERS

2015 CITY CHARTER REVIEW
SDCERS' PROPOSED REVISIONS TO THE CITY CHARTER
CITY CHARTER ARTICLE IX

Section 140: Establishment of Separate Retirement Pension Systems; Definitions

As of the election at which this Section becomes operative, the electorate of the City of San Diego has found and declared that the fiscal best interests of the City are served by reforming the retirement system authorized by this Charter to be established for City employees.

"Defined Benefit Pension Plan" or "Defined Benefit Pension System" is a system or plan to provide a specified allowance to a city retiree or a retiree's spouse after retirement that is based on a set formula based on factors such as age, years of service, and elements of compensation as established in this Article.

The Defined Benefit Pension Plan in place prior to said election, established by the City Council pursuant to Sections 141 through 149 of this Charter, may remain in place until, for any reason, there remain no participants in the Defined Benefit Plan. The City Council may by ordinance utilize any lawful means for terminating the Defined Benefit Plan. Any closure of the Defined Benefit Plan shall be designed and implemented to protect the employees' vested rights in the Defined Benefit Plan, generate cost savings for taxpayers, and ensure compliance with applicable laws and regulations, including tax regulations.

At such time as there remain no participants in the Defined Benefit Pension Plan, the City shall take such actions as are necessary and appropriate to promptly wind down and terminate the Defined Benefit Pension Plan.

Notwithstanding the foregoing, and except as expressly provided in this Article IX, all Officers and employees, with the exception of sworn police officers and police recruits participating in the City's Police Academy, who are initially hired or assume office on or after the effective date of this Section shall participate only in such Defined Contribution Plans as authorized by Sections 150 and 151 of this Charter.

The provisions of Sections 141 through 149 shall apply only to the Defined Benefit Plan, and those City employees eligible to participate in the Defined Benefit Plan. The provisions of Sections 150 and 151 shall apply only to the Defined Contribution Plan, and those City employees eligible to participate in the Defined Contribution Plan, except as expressly stated.

Notwithstanding the foregoing, and except as provided in this Article IX, the City Council is hereby authorized and empowered by ordinance to enroll sworn police officers hired after the effective date of this section in either the Defined Benefit Plan or the Defined Contribution Plan. This section shall be implemented in a manner consistent with the requirements of applicable labor relations laws.

(Addition voted 06-05-2012; effective 07-20-2012.)

+-Section 141: City Employees' Retirement System

The Council of the City is hereby authorized and empowered by ordinance to establish a retirement system and to provide for death benefits for compensated public officers and employees, other than those policemen and firemen who were members of a pension system on June 30, 1946. No employee shall be retired before reaching the age of sixty-two years and before completing ten years of service for which payment has been made, except such employees may be given the option to retire at the age of fifty-five years after twenty years of service for which payment has been made with a proportionately reduced allowance. Policemen, firemen and full time lifeguards, however, who have had ten years of service for which payment has been made may be retired at the age of fifty-five years, except such policemen, firemen and full time lifeguards may be given the option to retire at the age of fifty years after twenty years of service for which payment has been made with a proportionately reduced allowance.

The Council may also in said ordinance provide:

(a) For the retirement with benefits of an employee who has become physically or mentally disabled by reason of bodily injuries received in or by reason of sickness caused by the discharge of duty or as a result thereof to such an extent as to render necessary retirement from active service.

(b) Death benefits for dependents of employees who are killed in the line of duty or who die as a result of injuries suffered in the performance of duty.

(c) Retirement with benefits of an employee who, after ten years of service for which payment has been made, has become disabled to the extent of not being capable of performing assigned duties, or who is separated from City service without fault or delinquency.

(d) For health insurance benefits for retired employees.

Notwithstanding anything to the contrary in this section, the Charter or the Municipal Code, reciprocal service granted under the Uniform Reciprocal Provisions pursuant to the Reciprocity Contract between SDCERS and CalPERS shall be included as service for purposes of establishing eligibility for retirement benefits.

] *(Editor's note: Supplement No. 655)*
(Amendment voted 03-13-1945; effective 04-09-1945.)
(Amendment voted 04-19-1949; effective 05-20-1949.)
(Amendment voted 03-13-1951; effective 03-26-1951.)
(Amendment voted 06-08-1954; effective 01-10-1955.)
(Amendment voted 11-06-1990; effective 02-19-1991.)
(Amendment voted 11-08-1994; effective 01-30-1995.)
(Amendment voted 11-05-1996; effective 02-10-1997.)

Section 141.1: Reform of ~~Sworn~~ Police Officer Defined Benefit Pension Plan

Notwithstanding any other provision of this Charter, or any ordinance or other action taken pursuant hereto, the maximum amount of retirement benefit payable to a sworn police officer or police recruit participating in the City's Police Academy, who is hired after the effective date of this section and who is a participant under the Defined Benefit Pension Plan, shall be an amount equivalent to 80% at age 55 of the average of the participant's highest consecutive 36 months of Base Compensation as defined by Section 70.1. The maximum set by this provision shall decrease by 3% (three percentage points) for each year that such participant retires before age 55.

(Addition voted 06-05-2012; effective 07-20-2012.)

Section 141.2: Full and Fair Employee Contributions for The Defined Benefit Pension Plan

For officers and employees who have the legal right to remain in the established Defined Benefit Pension Plan, the City shall contribute annually an amount substantially equal to that required of the employee for a normal retirement allowance, as certified by the Actuary established in Charter Section 142, but shall not contribute in excess of that amount, except in the case of financial liabilities accruing under any new retirement plan or revised retirement plan because of past service of the employee. The City shall not pay, cap the employee contribution rate, or otherwise compensate for any portion of a contribution to the Retirement System by a City Officer or employee.

To the fullest extent permissible by law, in calculating annual contributions for the City and City employees, the Retirement Board shall divide equally between those two parties all costs those costs explicitly and exclusively reserved to the City in this Section and Section 143. Contributions shall also be governed by Section 143 of this Article. In the event of a conflict between this Section and Section 143, this Section shall prevail. This section is not intended to interfere with vested defined rights of any retiree receiving benefits from the Defined Benefit Retirement System or of any employee enrolled in the Defined Benefit Retirement System as of the effective date of this section.

Nothing contained in this Section shall preclude the City from entering into a settlement of *City of San Diego v. San Diego City Employees' Retirement System* Case No. #37-2010-00091207-CU-WM-CTL_to define responsibilities of the City and employees for unfunded liabilities of the Retirement System even if the settlement includes terms that might otherwise conflict with the above restrictions, as long as the settlement is approved by the court as a good faith settlement and approved by a two-thirds vote of the City Council.

Nothing contained in this Section or in Section 143 shall preclude the City from agreeing to pay to the Retirement System any portion of an overpayment of benefits or underpayment of contributions, and any interest associated with an overpayment or underpayment as assessed by the Board of Administration, where the overpayment or underpayment was proximately caused by the fault or negligence of a City employee acting in the course and scope of his or her employment. The Council of the City is hereby authorized and fully empowered to enact any and all ordinances necessary to carry into effect the provisions of this section and any and all ordinances so enacted shall have equal force and effect with this Article and shall be construed to be a part hereof as fully as if drawn herein. Any ordinance enacted pursuant to this section shall not be considered an ordinance affecting or enhancing the benefits of any active or retired Member of the System and shall not be subject to the voting requirements set forth in Section 143.1.

(Addition voted 06-05-2012; effective 07-20-2012.)

Section 142.1: Employment of Attorneys (New)

The Board of Administration hereinafter provided, may appoint attorneys to advise and represent the Board, as may be necessary. Attorneys hired or retained by the Board shall have duties and responsibilities only to the Retirement System and its Board of Administration and shall not have a duty of loyalty or care to the City of San Diego. Except to the extent that the

Board retains outside counsel as consultants, such appointments shall be made under the provisions of Article VIII of this Charter.

Section 143: Contributions [No Change.]

Section 143.1: Approval of Retirement System Benefit [No Change]

Section 144: Board of Administration

Effective April 1, 2005, the system shall be managed by a newly constituted Board of Administration which shall consist of 13 members. Seven members shall constitute a quorum of the Board and the concurring vote of seven members shall be required for the Board to take any action. Prior to April 1, 2005, in anticipation of the effective date, and thereafter, members shall be selected to serve as follows:

(a) Seven (7) members shall be appointed by the Mayor and confirmed by the Council. No person who is a City employee, participant in the Retirement System, or City union representative may be eligible for appointment in this category. Such appointees shall have the professional qualifications of a college degree in finance, economics, law, business, or other relevant field of study or a relevant professional certification. In addition, such appointees shall have a minimum of fifteen (15) years' combined experience in pension administration, pension actuarial practice, investment management, real estate, banking, ~~or~~ accounting or the practice of law related to any of the preceding fields. Members of the Board serving in this category shall serve staggered terms of four (4) years each. Inaugural appointments occurring after the effective date of this section shall have four (4) members serving two (2) year terms and three (3) members serving three (3) year terms. The Board shall determine which open seats shall serve four (4) and three (3) years terms to achieve staggered terms of four (4) years for all subsequent appointments. ~~(inaugural appointments shall have three (3) members serving two year terms) and m~~Members in this category shall be limited to a maximum of eight (8) consecutive years in office and an interval of four (4) years must pass before such persons can be reappointed. Such appointees shall not have any other personal interests which would create a conflict of interest with the duties of a Board member and trustee.

(b) One (1) police safety member of the Retirement System elected by the active police safety members to serve a four (4) year term, except that the inaugural member elected in 2005 to fill the seat in this category shall serve a two (2) year term. For purposes of this section, police safety members eligible to serve and vote shall include any police safety members employed by a Contracting Public Agency as defined in Section 149 of this Article.

(c) One (1) fire safety member of the Retirement System elected by the active fire safety members to serve a four (4) year term. For purposes of this section, fire safety member eligible to serve and vote shall include any fire safety members employed by a Contracting Public Agency as defined in Section 149 of this Article.

(d) Two (2) general members of the Retirement System elected by active general members of the Retirement System to serve a four (4) year term. For purposes of this section, general members eligible to serve and vote shall include any general members employed by a Contracting Public Agency as defined in Section 149 of this Article.

(e) One (1) retired member of the Retirement System elected by the retired members of the Retirement System to serve a four (4) year term, except that the inaugural member elected in 2005 to fill the seat in this category shall serve a two (2) year term. For purposes of this section, retired members eligible to serve and vote shall include any retired members of a Contracting Public Agency as defined in Section 149 of this Article.

(f) One (1) City management employee in the administrative service appointed by the ~~City Manager~~ Mayor to serve at the pleasure of the ~~City Manager~~Mayor selected from the following: ~~City Manager~~Chief Operating Officer, City Treasurer, Deputy or Assistant ~~City Manager~~Chief Operating Officer, or person in a similar position who reports to the ~~City Manager~~Mayor

The Board of Administration may establish such rules and regulations as it may deem proper; shall elect one of its members president and appoint a secretary and may appoint such other employees as may be necessary. Such appointments, except the actuary, shall be made under the provisions of Article VIII of this Charter.

The Board of Administration shall be the sole authority and judge under such general ordinances as may be adopted by the Council as to the conditions under which persons may be admitted to benefits of any sort under the retirement system; shall have all powers and duties provided in the Declaration of Group Trust for the SDCERS Group Trust effective July 1, 2007 and any amendments thereto or successor trusts hereinafter adopted by Resolution of the City Council; ~~and~~ shall have exclusive control of the administration and investment of such fund or funds as may be established; ~~and~~ shall be permitted to invest in any bonds or securities which are authorized by General Law for savings banks; and, further, shall be permitted to invest in such additional classes or types of investments as deemed prudent by the Board consistent with its fiduciary duties. ~~are approved by resolution of the Council of the City of San Diego; provided, however, that individual investments within the classes or types approved by the Council must be approved by independent investment counsel; and, provided, further, the board may place such funds in the hands of the Funds Commission for investment. Provided, however, that the Auditor and Comptroller shall refuse to allow any warrant drawn for payment of a retirement allowance if, in the opinion of the Auditor and Comptroller, such retirement allowance has been granted in contravention of this Article or any ordinances passed under the authority granted herein.~~

(Amendment voted 03-13-1951; effective 03-26-1951.)
(Amendment voted 11-08-1960; effective 01-09-1961.)
(Amendment voted 11-04-1969; effective 01-29-1970.)
(Amendment voted 06-04-1974; effective 08-13-1974.)
(Amendment voted 11-2-2004; effective 04-01-2005)
(Effective 07-08-2008, the authority, power, and responsibilities conferred upon the Auditor and Comptroller by this Charter were transferred to the Chief Financial Officer. See section 39.)
Prior Language

Section 145: Retirement Fund

All moneys contributed by employees of the City or appropriated by the Council or received from any other source under the terms of this Article, shall be placed in a special fund ~~in the City Treasury~~ to be known as the City Employees' Retirement Fund, which said fund is hereby created. Such fund shall be a Trust Fund to be held and used only for the purpose of carrying out the provisions of this Article. No payments shall be made therefrom except upon

the order of the Board of Administration. This fund may be placed by the Board under the Funds Commission for investment; but shall not be merged with other funds of the City.

Sections 146 through 151 [No Change}

ATTACHMENT 2

OVERPAYMENTS POLICY

PURPOSE AND SCOPE

In order to preserve the financial integrity of the Retirement System and comply with the Board's fiduciary responsibilities and IRS rules and regulations governing overpayment of benefits, it is the Board's policy to investigate any overpayment promptly and diligently and to recover the overpayment unless circumstances exist that make it unreasonable or futile to do so. The purpose of this policy is to provide guidelines and a process for evaluation and collection of overpayments made to Members and Beneficiaries (collectively "Members," for purposes of this Policy).

POLICY

The CEO may delegate to staff any reporting or investigative responsibilities assigned to the CEO in this policy. Therefore, the term "CEO" as used in this policy refers to the CEO and his/her delegate. When an overpayment is identified, the following guidelines and procedures will be followed:

1. NOTIFICATION

   a. When an overpayment is identified, staff will notify the CEO, who will report any overpayments in excess of $10,000 to the Board at the next regularly scheduled Board meeting. The CEO will report back to the Board on the progress of the investigation and collection of the overpayment within 90 days.

   b. The CEO will provide an annual report to the Board setting forth the final resolution of any overpayments of $10,000 or less.

2. INVESTIGATION

   a. When an overpayment is identified, the CEO will conduct an investigation into the facts and circumstances surrounding the overpayment. Before an overpayment may be resolved for anything less than immediate full payment, the CEO must ascertain the financial situation of the member and the financial hardship, if any, of requiring immediate full payment of the amount owed.

   b. The CEO will establish internal procedures to investigate, collect and resolve overpayments.

3. COLLECTION

   a. Overpayments Exceeding $10,000 – Approval by the Board:

1) Resolution of an overpayment that exceeds $10,000 should be resolved for immediate full payment of the entire amount, plus interest, whenever feasible. For purposes of this Policy, full repayment may include an installment repayment plan for the full amount owed, including interest at the actuarially assumed rate. A resolution on these terms does not need Board approval.

2) Any resolution of an overpayment exceeding $10,000 that does not result in immediate full payment of the entire amount, plus interest, must be approved by the Board.

3) The Board will not approve any resolution that is inconsistent with IRS guidelines in place at the time the overpayment is discovered. The CEO will inform the Board of the current IRS guidelines for settling overpayments when the proposed resolution is presented to the Board for approval.

b. Overpayments of $10,000 or Less – Approval by the CEO:

1) Resolution of an overpayment of $10,000 or less should be resolved for immediate full payment of the entire amount, plus interest, whenever feasible. For purposes of this Policy, full repayment may include an installment repayment plan for the full amount owed, including interest at the actuarially assumed rate.

2) Subject to the procedures in this Policy and IRS guidelines in place at the time the overpayment is discovered, the CEO will have sole discretion to resolve any overpayment of $10,000 or less.

c. Factors to Consider When Resolving Overpayments: Before agreeing to accept something other than immediate full repayment, the Board or CEO will consider the following factors:

1) The amount of the overpayment;

2) The Member's financial position;

3) Whether requiring immediate full repayment will cause a financial hardship to the Member; and,

4) Whether the resolution complies with IRS guidelines for correction of plan errors.

5) Before agreeing to any resolution requiring SDCERS to refrain from collecting any overpayment from a Member that would require recovery from the plan sponsor, the Board or CEO will seek the plan sponsor's consent. The Board or CEO will not agree to

resolve an overpayment with a Member that would require recovery from the plan sponsor without the plan sponsor's consent.

d. Interest:

1) SDCERS will charge the Member interest only if the overpayment is not resolved within the same fiscal year when it occurred. "Resolved" for purposes of charging interest means the date when the Member either tenders to SDCERS the amount owed or signs and returns a payment plan to repay the Overpayment or a combination of the two.

2) Interest will be charged at the actuarially assumed rate in effect when the overpayment is Resolved.

3) Interest on repayment plan: If the Member chooses to repay the overpayment in installments over time, SDCERS will charge interest on the repayment plan at the actuarially assumed rate in effect on the date the Member signs the repayment plan.

e. Offset: The collection of a Retirement System overpayment does not constitute "execution, garnishment, attachment or any other process of any court" under Municipal Code Section 24.1008. The Retirement System may collect an overpayment as an offset from future benefits the System owes to the Member or, where legally permissible, the Member's beneficiaries, whether or not the Member consents to the offset.

4. DUE PROCESS

a. Before collecting an overpayment from the future benefits of a Member without consent, SDCERS will give notice to the affected party of its intent to do so and provide an opportunity for the affected party to request a hearing on the matter should the affected party dispute the fact that an overpayment has occurred or the amount of the overpayment.

b. No overpayment will be collected from the future benefits of a Member unless that person has been given 30 days notice of SDCERS' intent to do so. The notice will include an explanation as to the reason for the offset, the basis for calculation of the amount of the overpayment and an explanation of the Member's right to request a hearing on the matter. The notice will be mailed to the affected person's last known address and will include a proof of service. Service by regular mail will constitute sufficient notice.

c. The Member must request a hearing within 30 days of the mailing of the above notice. Failure to do so will constitute a waiver of the right to a hearing. If the Member requests a hearing within 30 days of the mailing of

the notice, staff will place the matter on the agenda for the Business and Governance Committee meeting.

d. Hearings will be held before the Business and Governance Committee for a recommended final decision by the Board. The Committee will hear all matters, including those arising from disputed facts, although the Committee may recommend referral to a hearing before an Adjudicator if the Committee deems that appropriate. The same procedural requirements for hearings set forth in Board Rule 7.50 through 7.170 will apply to hearings on overpayments before the Business and Governance Committee.

POLICY REVIEW AND HISTORY

5. The Board will review this Policy at least once every three years to ensure that it remains relevant and appropriate.

6. This Policy replaces prior Board Rule 7.50, was adopted by the Board of Administration on June 20, 2008 and amended on October 17, 2008, September 18, 2009 and January 22, 2010 and reviewed and amended on August 19, 2011, and amended on September 20, 2013.

UNDERPAYMENTS POLICY

In order to preserve the financial integrity of the Retirement System, and comply with the Board's fiduciary responsibilities and IRS rules and regulations governing Members' underpayments of contributions, it is the Board's policy to investigate any underpayment promptly and diligently and to recover the underpayment. The purpose of this policy is to provide guidelines and a process for evaluating and recovering underpayments of Member contributions. For purposes of this Policy, Member contributions include amounts paid for purchases of service under the applicable provisions of the Municipal Code and the Board Rules. This Policy does not apply to the correction of Affected PSC Contracts set forth in Board Rule 4.90.

POLICY

The CEO may delegate to a staff member any reporting or investigative responsibilities assigned to the CEO in this policy. Therefore, the term "CEO" as used in this policy refers to the CEO and his/her delegate. When an underpayment is identified, the following guidelines and procedures will be followed:

1. NOTIFICATION

   a. When an underpayment is identified, staff will notify the CEO, who will report any underpayments in excess of $10,000 to the Board at the next regularly scheduled Board meeting. The CEO will report back to the Board on the progress of the investigation and collection of the underpayment within 90 days.

   b. The CEO will provide an annual report to the Board setting forth the final resolution of any underpayments of $10,000 or less.

2. INVESTIGATION

   a. When an underpayment is identified, the CEO will immediately conduct an investigation into the facts and circumstances surrounding the underpayment. Before an underpayment may be resolved for anything less than immediate full payment, the CEO must ascertain the financial situation of the Member and the financial hardship, if any, of requiring immediate full payment of the amount owed.

   b. The CEO will establish internal procedures to investigate, collect and resolve underpayments.

3. COLLECTION

   a. Underpayments Exceeding $10,000 – Approval by the Board:

1) Resolution of an underpayment that exceeds $10,000 should be resolved for immediate full payment of the entire amount, plus interest, whenever feasible. For purposes of this Policy, full repayment may include an installment repayment plan for the full amount owed, including interest at the actuarially assumed rate. A resolution under these terms does not need Board approval.

2) Any resolution of an underpayment exceeding $10,000 that does not result in immediate full payment of the entire amount, plus interest, must be approved by the Board.

3) The Board will not approve any resolution that is inconsistent with IRS guidelines in place at the time the underpayment is discovered. The CEO will inform the Board of the current IRS guidelines for settling underpayments when the proposed resolution is presented to the Board for approval.

b. Underpayments of $10,000 or Less – Approval by the CEO:

1) Resolution of an underpayment of $10,000 or less should be resolved for immediate full payment of the entire amount, plus interest, whenever feasible. For purposes of this Policy, full repayment may include an installment repayment plan for the full amount owed, including interest at the actuarially assumed rate.

2) Subject to the procedures in this Policy and IRS guidelines in place at the time the underpayment is discovered, the CEO will have sole discretion to resolve any underpayment of $10,000 or less.

c. Factors to Consider When Resolving Underpayments: Before agreeing to accept something other than immediate full payment, the Board or CEO will consider the following factors:

1) The amount of the underpayment;

2) The Member's financial position;

3) Whether requiring immediate full repayment will cause a financial hardship to the Member; and,

4) Whether the resolution complies with IRS guidelines for correction of plan errors.

5) Before agreeing to any resolution requiring SDCERS to refrain from collecting any underpayment from a Member that would require recovery from the plan sponsor, the Board or CEO will seek the plan sponsor's consent. The Board or CEO will not agree to

resolve an underpayment with a Member that would require recovery from the plan sponsor without the plan sponsor's consent.

d. Interest:

1) SDCERS will charge the Member interest only if the underpayment is not resolved within the same fiscal year when it occurred. "Resolved" for purposes of charging interest means the date when the Member either tenders to SDCERS the amount owed or signs and returns a payment plan to repay the underpayment or a combination of the two.

2) Interest will be charged at the actuarially assumed rate in effect when the underpayment is resolved.

3) Interest on Repayment Plan: If the Member chooses to repay the underpayment in installments over time, SDCERS will charge interest on the repayment plan at the actuarially assumed rate in effect on the date the Member signs the repayment plan. Repayment Plans may only be made on a post-tax basis.

e. Procedure Where Full Amount Cannot Be Collected:

1) In any case where an underpayment arising from a purchase of service credit cannot be collected in full from the Member, the Member's service credit will be reduced on a pro rata basis or the Member may elect to rescind his or her after tax purchase of service contract and receive a refund of the funds paid for the purchase plus interest.

f. Offset: The collection of a Retirement System underpayment does not constitute "execution, garnishment, attachment or any other process of any court" under Municipal Code Section 24.1008. If the underpayment cannot be collected through any of the above means, the Retirement System may collect an underpayment as an offset from any future benefits the System owes to the Member or, where legally permissible, the Member's beneficiaries, whether or not the Member consents to the offset.

4. DUE PROCESS

a. Before collecting an underpayment from the future benefits of a Member without consent, SDCERS will give notice to the affected party of its intent to do so and provide an opportunity for the affected party to request a hearing on the matter should the affected party dispute the fact that an underpayment has occurred or the amount of the underpayment.

b. No underpayment will be collected from the future benefits of a Member unless that person has been given 30 days notice of SDCERS' intent to do

so. The notice will include an explanation as to the reason for the offset, the basis for calculation of the amount of the underpayment and an explanation of the Member's right to request a hearing on the matter. The notice will be mailed to the affected person's last known address and will include a proof of service. Service by regular mail will constitute sufficient notice.

c. The Member must request a hearing within 30 days of the mailing of the above notice. Failure to do so will constitute a waiver of the right to a hearing. If the Member requests a hearing within 30 days of the mailing of the notice, staff will place the matter on the agenda for the Business and Governance Committee meeting.

d. Hearings will be held before the Business and Governance Committee for a recommended final decision by the Board. The Committee will hear all matters, including those arising from disputed facts, although the Committee may recommend referral to a hearing before an Adjudicator if the Committee deems that appropriate. The same procedural requirements for hearings set forth in Board Rule 7.50 through 7.170 will apply to hearings on underpayments before the Business and Governance Committee.

POLICY REVIEW AND HISTORY

5. The Board will review this Policy at least once every three years to ensure that it remains relevant and appropriate.

6. This Policy was adopted by the Board of Administration on June 20, 2008 and amended on October 17, 2008, September 18, 2009 and January 22, 2010 and reviewed and amended on August 19, 2011, and amended on September 20, 2013.

ATTACHMENT 3

SDCERS
San Diego City Employees' Retirement System

SAN DIEGO CITY EMPLOYEES' RETIREMENT SYSTEM
STAFF REPORT
LEGAL DIVISION

DATE: July 27, 2011

TO: BUSINESS AND GOVERNANCE COMMITTEE

FROM: Elaine W. Reagan, General Counsel, Legal

SUBJECT: Staff Recommendation to Adopt Revised Overpayments and Underpayments Policies

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RECOMMENDATION:

Adopt Revised Overpayments and Underpayments Policies

SUMMARY:

Staff is in the process of its triennial review of all Board Charters, Policies, Resolutions and Rules. The Overpayments and Underpayments Policies were adopted by the Board on June 20, 2008 and last amended on January 22, 2010. The Overpayments Policy applies when SDCERS overpays a benefit to a Member or Beneficiary. The Underpayments Policy applies when a Member underpays contributions, including underpayment of contributions for purchase of service.

The Business and Governance Committee reviewed the Policies at its April 2011 meeting as part of the triennial review. At that time, staff recommended that where the Overpayment or Underpayment was not caused by the Member, that the policies be revised to change the interest rate applied to collections from 2% to the non-corporate rate established by the IRS for tax underpayments ("IRS rate") as the interest, which is currently set at 4%. The Committee continued the item and asked staff to discuss this proposed revision with the Plan sponsors. As a result of feedback received from the plan sponsors, staff is no longer recommending that SDCERS use the IRS rate.

Staff is recommending the following substantive revisions to the policies:

- Change the interest rate applied to collections of overpayments and underpayments from 2% to the actuarial assumed rate in effect when the matter is resolved.
- Delete the provision requiring SDCERS to collect from the plan sponsor the difference between the interest rate actually charged the member and the actuarial assumed interest rate.

Currently, the policies require that SDCERS collect interest on overpayments and underpayments at the actuarially assumed interest rate, with 2% interest from the Member and the remainder from the plan sponsor. The policies also require that SDCERS collect the plan sponsor portion of interest immediately. This policy was based on the guidelines for collection of Overpayments provided by the IRS for self-correction of plan errors. The IRS guidelines state:

> *Return of Overpayment Correction Method.* Overpayments as a result of amounts being paid in excess of the limits of §415(b)[1] may be corrected using the return of Overpayment correction method set forth in this paragraph . . . . The Employer takes reasonable steps to have the Overpayment (with appropriate interest) returned by the recipient to the plan . . . . To the extent the amount returned by the recipient is less than the Overpayment, adjusted for earnings at the plan's earnings rate, then the Employer or another person contributes the difference to the plan. (Rev. Proc. 2008-50, Appendix B, section 2.04(1)(a)(i), emphasis added.)

See also, Rev. Proc. 2008-50, §6.06(3).

The guidelines require that interest be collected at the plan's earnings rate (the actuarial assumed rate). There is no provision in the plan documents of the City, Port or Airport that would allow SDCERS to require the plan sponsors to pay this interest without their consent. Because the plan sponsors have not agreed to voluntarily pay any portion of this interest, SDCERS must collect the entire amount from the Member.

Therefore, staff is recommending that the policies be revised to provide that the Member will pay interest on overpayments and underpayments at the actuarial assumed rate so that SDCERS will be in compliance with IRS guidelines.

The remaining revisions are non-substantive, cosmetic changes.

[1] The guidelines also provide if a plan has a different but analogous failure to one set forth in Appendix B, then the analogous correction method is generally available to correct any failure. [Rev. Proc. 2008-50, Section 6.01(2).) Collection of an overpayment of a benefit or underpayment of contributions is analogous to an overpayment of benefits under 415(n) and is thus the appropriate correction method to use in these policies.