

CITIZENS' ECONOMY AND EFFICIENCY COMMISSION



OF LOS ANGELES COUNTY

September 8, 1993

Honorable Edmund D. Edelman
Los Angeles County Board of Supervisors
500 West Temple Street
821 Hahn Hall of Administration
Los Angeles, CA 90012

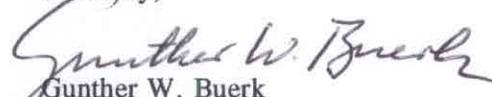
Dear Chairman Edelman:

In response to the Board's action of November 17, 1992, requesting the Economy and Efficiency Commission to retain independent counsel "to advise the Board of Supervisors on its legal options with respect to the deferred compensation issue". The Commission has received the requested legal opinion. The Pension Task Force of our Commission has reviewed the opinion to insure that the assignment as stated in the Board motion was completely addressed, but has not made any changes to this opinion or directed the independent counsel to make any changes in his opinion.

Following direction, the independent counsel, Frank Smith, has provided a professional and complete opinion on the legal aspects of the issue requested in the Board motion. As such the Commission is forwarding this opinion to your Board for consideration.

It is important to note that neither the Pension Task Force nor the Economy and Efficiency Commission has reached any conclusions or recommendation regarding this issue and by transmitting the attached opinion, the Commission is not indicating agreement or disagreement with any conclusions or implication of the independent counsel's opinion.

Sincerely,


Gunther W. Buerk
Chair

c:Each Supervisor
Each Commissioner
Harry Hufford, CAO
Sally Reed, CAO Designate
DeWitt Clinton, County Counsel
Charles Conrad, LACERA
Bruce Staniforth

l:opinion.cvr

Chair

Gunther W. Buerk

Vice-Chair

Betty Trotter

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Efrem Zimbalist, III

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Bruce J. Staniforth

Assistant to the Director

Peter C. White

MORGAN, LEWIS & BOCKIUS

PHILADELPHIA
LOS ANGELES
MIAMI
LONDON
FRANKFURT

COUNSELORS AT LAW
801 SOUTH GRAND AVENUE
TWENTY-SECOND FLOOR
LOS ANGELES, CALIFORNIA 90017-4615
TELEPHONE: (213) 612-2500
FAX: (213) 612-2554

WASHINGTON
NEW YORK
HARRISBURG
SAN DIEGO
BRUSSELS
TOKYO

FRANK H. SMITH
DIAL DIRECT (213) 612-1016

August 17, 1993

Economy and Efficiency Commission
163 Hall of Administration
500 West Temple Street
Los Angeles, California 90012

Re: Deferred Compensation

Dear Commissioners:

The Board of Supervisors has requested that the undersigned, as independent legal counsel retained by the Economy and Efficiency Commission, advise it further with respect to its legal options regarding the impact that certain deferred compensation payments have on the affected employees' pensions. This opinion has been prepared in response to that request.

Background and Prior Legal Opinion

Pursuant to agreements with the County, some County officers and department heads elected to delay receipt of up to 10% of one year's salary to be paid without interest at a time chosen by the individual participating in the arrangement. In addition, certain employees who had previously been scheduled for an average 6% merit raise, effective September 1, 1991, were given the option by the County of receiving an average 3% merit salary increase effective as of such date or a 6% raise to be delayed to at least September 1, 1992. These deferral arrangements were incorporated in written agreements between the County and each of the affected employees. Each of these agreements contained the following language:

"County warrants that all amounts deferred pursuant to this Agreement shall constitute compensation earnable within the meaning of Government Code Section 31461 at the time the funds are paid to Employee."

Thus, as part of the overall contractual arrangement, the County committed itself to have the deferred compensation treated as pensionable compensation at the time such amounts were to be received for purposes of determining that employee's retirement benefits.

The treatment of deferred compensation as pensionable compensation and when it should be so treated was one of the

MORGAN, LEWIS & BOCKIUS

Economy and Efficiency Commission

August 17, 1993

Page 2

subjects covered under a previous legal opinion prepared by the undersigned (herein referred to as the "Prior Legal Opinion"). The Prior Legal Opinion concluded that the deferred compensation resulting from the agreements is compensation earnable within the meaning of Government Code Section 31461, but should be considered to be compensation earnable at the time of deferral, not at the time of receipt. Fiduciary counsel for the Board of Retirement subsequently agreed with this conclusion in an opinion prepared for the Board of Retirement on this and other issues involving pensionable compensation. Opinion of September 10, 1992, p. 70-71. Presumably, County Counsel is now in agreement with this conclusion as well.

As indicated in the Prior Legal Opinion, however, it is only the Board of Retirement that can bind the retirement system to such matters as the proper interpretation of compensation earnable. However, as also concluded in the Prior Legal Opinion, the County, by virtue of the written agreements, had nonetheless clearly committed itself to a position to treat the deferred compensation as pensionable compensation when received (at least if that results in a greater pension than if taken into account at the time of deferral) and, as a result, has generally estopped itself from repudiating that position at this time. As indicated above, the Board of Supervisors has requested at this time that we further elaborate on the legal obligations of the County and the corresponding rights of the recipients of the deferred compensation in view of this set of facts.

Legal Opinion

In our opinion, the County is generally obligated to make any additional payments necessary to the recipients of the deferred compensation in order to make up for any shortfall in their pensions due to the fact that the retirement system will not consider the deferred compensation to be pensionable when received. This can either be done by direct payment by the County or through reimbursement of the retirement system.

The language used in the deferred compensation agreements on this question could not have been clearer. Furthermore, the employees clearly gave legal consideration for the County's representations in that they deferred salary otherwise receivable, in some cases on an interest-free basis. Thus, under a simple contract analysis, the County has legally bound itself to its representation with respect to the treatment of the deferred compensation as pensionable compensation.

It should also be noted that the County Counsel in its legal review of this issue has never raised a question concerning the County's legal capacity to enter into a deferred compensation

MORGAN, LEWIS & BOCKIUS

Economy and Efficiency Commission

August 17, 1993

Page 3

arrangement of this type (i.e., to provide a supplemental pension following retirement where such supplemental pension is not funded by employee contributions) under the laws governing the County's general legal powers. See e.g., Attachment III to the Chief Administrative Office's Memorandum to the Board of November 13, 1992, p. 6.^{1/}

Thus, the sole question that remains is whether the County can repudiate the obligation it assumed by the representations contained in the written deferred compensation agreements on the basis that such representations were made due to a misinterpretation of the law governing the County's retirement system. In our opinion, the County cannot do so because of two related but somewhat distinct well-developed doctrines - (i) vesting in public pensions and (ii) estoppel.

As discussed in the Prior Legal Opinion (pgs. 24-33), the courts in California have held that a vested contractual right to pension benefits accrues upon a public employee's acceptance of employment and that such a pension right may not be destroyed once vested without impairing a contractual obligation of the employing public entity. Kern v. City of Long Beach, 29 Cal.2d 848 (1947). The deferred compensation agreements, through their express representations regarding the treatment of the deferred compensation for pension purposes, directly relate to the determination of the amount of the employees' pensions. Under the long line of cases following Kern, the employees have achieved a vested interest in that amount of their pensions. Furthermore, as discussed in the Prior Legal Opinions (p. 32) in a somewhat different context, while there is no judicial authority on the question, it is likely that a court would find that an employee is vested in a pension benefit resulting from

^{1/} Specific authority to enter into certain deferred compensation arrangements is conferred for example by Section 53212 et. seq. of the Government Code under which the deferred compensation arrangement is based on salary reduction payments by the participating employees. Presumably, the County's authority to enter into a non-contributory supplemental deferred compensation arrangement is sustainable under its general powers. If not, it is possible that the pension obligation could be challenged as being outside of the County's power. In these circumstances, the doctrine of estoppel cannot be applied to enlarge such powers. Merco Construction Engineers, Inc. v. Los Angeles Unified School District, 274 Cal.App.2nd 154 (1969); Shoban v. Board of Trustees, 276 Cal.App.2nd 534 (1969). However, the obligation may still be upheld under a vesting analysis (Prior Legal Opinion, page 32).

MORGAN, LEWIS & BOCKIUS

Economy and Efficiency Commission

August 17, 1993

Page 4

this kind of representation even if it was erroneous as long as the representation created a reasonable expectation on the part of the employee with respect to the amount of the pension.

There is much more judicial authority on the question of the application of the doctrine of estoppel to situations similar to this. It is well settled in California that estoppel can lie against a governmental entity where justice and right require it and where the elements of estoppel are met. Driscoll v. City of Los Angeles, 67 Cal.2d 297 (1967). These elements that must be present in order to apply the doctrine of estoppel are: (1) the party to be estopped must be apprised of the facts; (2) the party to be estopped must intend that its conduct shall be acted upon or must so act that the party asserting the estoppel had a right to believe it was so intended; (3) the other party must be ignorant of the true state of facts; and (4) the other party must rely upon the conduct to his injury. Id. at 305.

The courts have readily applied estoppel when an employee's pension benefits are at stake. For example, in Baillargeon v. Department of Water and Power, 69 Cal.App.3rd 670 (1970), the court held that a governmental entity was bound by a statement regarding benefits set forth in a retirement plan booklet even though it was inconsistent with the plan itself.

Likewise, in Crumpler v. Board of Administration, 32 Cal.App.3rd 567 (1973), the governmental employer was estopped from reducing public employees' pensions by retroactively classifying them as "miscellaneous members" rather than "safety members." In discussing the application of the estoppel doctrine to pension rights, the court stated: "Good faith conduct of a public officer or employee does not excuse inaccurate information negligently given. [Cites.] In a matter as important to the welfare of a public employee as his pension rights, the employing public agency 'bears a more stringent duty' to desist from giving misleading advice. [Cite]" Id. at 582.^{2/}

^{2/} The courts have not been as quick to apply an estoppel approach in non-pension benefit cases. E.g., Longshore v. County of Ventura, 25 Cal.3rd 14 (1979). In addition, in several early cases involving an estoppel against a governmental entity that was asserting a statute of limitations (Driscoll v. City of Los Angeles, 67 Cal.2d 297 (1967); Aldler v. City of Pasadena, 57 Cal.2d 609 (1962); Henry v. City of Los Angeles, 201 Cal.App.2d 299 (1962)), the courts distinguished between a fundamental pension claim and one not deemed to be of such magnitude, allowing estoppel in the one but not the other. However, it is noted (continued...)

Estoppel has not been applied against a public entity where the result would nullify a strong rule or policy adopted for the benefit of the public or to contravene directly any statutory or constitutional limitations. E.g., Transamerica Occidental Life Insurance Co. v. State Board of Equalization, 232 Cal.App.3rd 1048 (1991) (collection of taxes); State v. Superior Court of Placer County, 29 Cal.3rd 240 (1981) (government asserting public trust in lands). Addressing this issue in the context of pension rights, the Crumpler court stated that "[w]e discern no harmful effect upon any specific public policy or interest which would result from invoking estoppel in the instant case where pension rights of a public employee are involved." Id. at 584. Likewise, in Baillargeon against an argument that the application of the estoppel doctrine would have a negative impact on the general public's interest in an actuarially sound pension system for its employees, the court stated: "This argument has little merit since there is little likelihood that plaintiff's recovery against defendants would jeopardize The Plan from any actuarial standpoint. In addition, it would not be beneficial to anyone for public employees to be misled - intentionally or otherwise - by an informational booklet issued to them." Id. at 680.

Thus, the facts in this situation would seem to clearly estop the County from repudiating the obligation undertaken in its written agreements should it choose to attempt to do so. The County, through its representatives, was aware of the nature of the representation being made and intended that the representation as to the treatment of the deferred compensation be one of the items of consideration given in exchange for the employee's agreement to defer the compensation. Furthermore, to the extent that employees participating in the arrangement were ignorant of the proper treatment of deferred compensation under the statutory provisions governing the retirement system (see Prior Legal Opinion at p. 34-35), they were entitled to rely on the representation. Finally, it is clear that employees relied on the County's representation to their detriment in that they elected to defer the receipt of compensation that otherwise would have been immediately payable.

^{2/}(...continued)

that the subsequently decided Baillargeon and Crumpler cases involve supplemental and incremental benefits and, as noted above, both apply the estoppel doctrine. It is unlikely that a court would make a fundamental/non-fundamental distinction in a non-statute of limitations case involving facts such as those presented here where the County made a direct representation that the deferred compensation would be treated as pensionable compensation when received.

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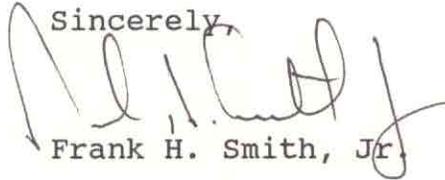
Economy and Efficiency Commission

August 17, 1993

Page 6

In conclusion, it is our opinion that it is highly likely that the courts would bind the County to the express written representations that it made in the deferred compensation agreements as to the treatment of the deferred compensation for pension purposes.

Sincerely,

A handwritten signature in cursive script, appearing to read "F. H. Smith, Jr.", written in dark ink.

Frank H. Smith, Jr.