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January 21, 2011

Mayor Jerry Sanders
Council President Tony Young
Council President Pro Tem Kevin Faulconer
Councilmember Sherri Lightner
Councilmember Todd Gloria
Councilmember Carl DeMaio
Councilmember Lorie Zapf
Councilmember Marti Emerald
Councilmember David Alvarez
City of San Diego
202 C Street
San Diego, CA 92101

Re: Joint Proposal By MEA and AFSCME Local 127 Re Purchase of Service Credit Issues; Confidential Settlement Proposal Under California Evidence Code § 1152

Dear Mayor and Councilmembers:

As you know, SDCERS has designed a "correction" process and a set of "options" related to "window period" purchase of service credit contracts which reflect SDCERS' understanding of its obligations in the wake of the Fourth District Court of Appeal's decision in *City of San Diego v. SDCERS*. As you also know, based on SDCERS' presentation to the Council on November 29, 2010, it remains for the City, as plan sponsor:

(1) to clarify which plan participants were "retirees" as of November 20, 2007, when the City filed its Writ Petition;

(2) to determine whether it is in the City's best interest to direct SDCERS to exclude any plan participants from the "correction process;" and/or,

(3) to determine whether it is in the City's best interest to direct SDCERS to add an option which would be available to any active employee/plan participant who is willing to sign a release of all legal claims.

This letter outlines the actions which MEA and Local 127 believe the City should take for the reasons explained.

1. Objectives To Be Achieved

The point of this letter is to identify an outcome which (1) lessens, if not eliminates, the likelihood of meritorious legal claims being filed and thereby (2) achieve a more certain fiscal outcome for the City and its pension plan. Our proposal is also intended to resolve the fundamental concern addressed by the courts regarding the "old" versus "new" pricing of service credits being purchased during the "window period," and to be fair to employees and retirees who did not know that any legal defect lurked in the contracts they signed and on which they relied in making career and financial planning decisions.

Indeed, it cannot be denied that the City's own representatives on the SDCERS Board approved the adoption of a "window period" along with Mayoral appointees Dick Vortmann and Diann Shipione. And employees themselves may have rejected the invitation to enter into a "window period" contract *if* the City Council or City Attorney had at least informed them that the City disagreed with the SDCERS Board's decision to make the "old" purchase rates available during a "window period." Yet, just the opposite occurred – the City itself promoted the purchase of service credits during the "window period," and the City Council, with the advice of the City Attorney, made a conscious decision to accept the unfunded liabilities associated with these "window period" contracts while using this circumstance to gain leverage in settling the *Gleason* Class Action litigation in 2004.

By acting *now* to eliminate or reduce the number of potential damage claims arising from SDCERS' proposed "correction" process, the City has the opportunity to secure actual gains for the pension system while assuring that these gains are not later diminished or eliminated altogether by litigation expenses and/or damage awards.

2. A Compromise To Settle Colorable Legal Claims Does Not Involve An Illegal "Gift of Public Funds"

At the outset, it is important to be clear that the City *can* lawfully take action to limit or reduce the adverse effects of the Court's decision where these effects will otherwise give rise to colorable claims for damages by individual retirees or active employees.

To re-acquaint you with the factual and legal issues which expose SDCERS and the City to a variety of legal outcomes – or to refresh your recollection regarding them – we have attached a copy of a letter dated August 11, 2010, which was authored by attorney Ann M. Smith and addressed to SDCERS' PSC Ad Hoc Committee. (Tab A)

Without belaboring or repeating these points here, suffice to say that the Court of Appeal's decision gives rise to a number of legal, financial, fiduciary, and administrative complications which remain unresolved by the decision. When the SDCERS' "correction" process, as currently designed, is implemented, affected employees and retirees will have potential individual claims against SDCERS *and*, both independently and through the City's obligation to indemnify SDCERS Board members, against the City. In fact, as a result of our own well-attended meetings, we can assure you

that very compelling factual scenarios abound which will lead to a host of individual damage claims and/or to a potential class action involving several discrete sub-classes. I and others who addressed you on November 29, 2010, described some of these issues and the likely litigation scenarios to follow.[1] Others conveyed in the most heartfelt and earnest terms the distress and upset which this proposed "correction" process has caused to those who have service retired, signed irrevocable DROP contracts, or made other career or financial decisions in reasonable reliance on *contracts* they believed were lawful, final and binding.

It is well-established that funds expended to settle a colorable legal claim are expended for a public purpose, and therefore are not an unconstitutional gift of public funds. Section 6 of article XVI of the California Constitution prohibits the state and its subdivisions from making gifts of public money to an individual or corporation. In determining whether an appropriation of public funds is to be considered a gift, the primary question is whether the funds are to be used for a public or private purpose; if they are to be used for a public purpose, they are not a gift within the meaning of the constitutional prohibition. *Sturgeon v. County of Los Angeles* (2008) 167 Cal.App.4th 630, 637-38 (internal quotations omitted). Money spent to settle a colorable legal claim is spent for a public purpose, and is thus not an unconstitutional gift. "The settlement of a good faith dispute . . . . is an appropriate use of public funds and not a gift because the relinquishment of a colorable legal claim in return for settlement funds is good consideration and establishes a valid public purpose." *Jordan v. California Dep't of Motor Vehicles* (2002) 100 Cal.App.4th 431, 450 (citing *Orange County v. Irvine Co.* (1983) 139 Cal.App.3d 195, 200).

3. MEA's and Local 127's Proposals

While MEA and Local 127 recognize that the "window period" purchase of service credit contracts implicated here are contracts signed by individual plan participants, MEA and Local 127 are, nevertheless, interested advocates regarding the outcome for these individuals. These contracts arose under the negotiated Purchase of Service Credit Program which is a provision of the City's pension plan and a term and condition of employment. The currently proposed "correction" process threatens the rights and economic well-being of current or former represented employees such that MEA and Local 127 are both motivated and committed to assuring a fair and proper outcome. With this goal in mind, we urge the City Council to take the following actions:

a. Clarify That Those Who Were in DROP When the City Filed its Writ Petition Were "Retired"

282 plan participants had already signed irrevocable DROP contracts *before* the City filed its Writ Petition on November 20, 2007. SDCERS *and the City* were signatories on these DROP contracts. These plan participants had "retired" under the plan because their eligible service credits were finalized, their pension benefit accruals ceased, and – as the DROP contract expressly states,

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[1] Because Councilmembers Alvarez and Zapf had not yet been sworn into office and thus were not present for this Council session, we respectfully urge you to listen to the videotape of the entire session to hear these presentations.

their pension allowances were not thereafter subject to change. Since the City *excluded* "retirees" from the relief it sought by its Writ Petition, this relief necessarily excluded those plan participants who were "retired" because they were already in DROP.

Accordingly, the City Council should simply clarify that SDCERS must not include in the "correction process" any plan participant who had already retired on or before November 20, 2007, by virtue of his/her having signed an irrevocable DROP contract on or before that date.

b. Exclude Those Who Entered DROP After the City Filed Its Writ Petition Because the City Signed Off on Their DROP Contracts

187 plan participants signed irrevocable DROP contracts *after* the City filed its writ petition on November 20, 2007. They should be excluded from the "correction" process based on two distinct grounds relevant to an appropriate risk/benefit analysis.

First, the City failed to provide any notice to its employees that a legal challenge was underway which might affect "window period" purchase of service credit contracts. Without such notice, employees reasonably relied on the finality of these contracts and the service credits they had purchased at the price set by the SDCERS Board. Since the City had, in fact, encouraged these "window period" purchases throughout the workplace, employees had no means to know that the City was attacking the validity of these contracts years after the fact.

Moreover, the City *waived* its right to challenge these employees' purchased service credits when the *City signed off* on these irrevocable DROP contracts. The City's independent action in waiving any alleged defects in the service credits being used to calculate these employees' final pension allowances is not excused by the Court of Appeal's decision. Had the City informed the DROP applicant that the City was reserving its right to challenge service credits being used in the calculation of his/her pension allowance, the applicant may have decided to forego or delay entry into DROP until the matter was resolved.

Finally, the City will ultimately be liable (directly or indirectly) for SDCERS' failure to disclose to employees who were preparing to enter DROP after November 20, 2007, that there was a material risk their "window period" service credits might be lost or reduced as a result of contentions the City was making in ongoing litigation.

Accordingly, the City should authorize SDCERS to exclude these plan participants from the "correction" process because any benefit from including them is outweighed by a substantial risk that their meritorious legal claims will succeed and impose a greater cost burden on the City by increasing the pension plan's unfunded liability.

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c. Exclude Those Who Service Retired After the City Filed Its Writ Petition Because Neither SDCERS Nor the City Disclosed To Them That the Service Credits On Which They Relied When Retiring Were Subject to Loss or Reduction Due to Pending Litigation

53 plan participants service retired *after* the City filed its writ petition on November 20, 2007. The City, of course, saw the logic in excluding retirees from the relief it sought by its Writ Petition because they had retired in reliance on any "window period" service credits.

Yet, those who retired *after* the Writ Petition was filed – just as was true for those who retired *before* that date – reasonably relied on these "window period" service credits and had no forewarning or notice from SDCERS *or the City* that they were at any risk of losing or having their service credits reduced due to pending litigation.

Had SDCERS or the City informed these employees of such a risk, most, if not all, would have delayed their retirement until the matter was resolved. Having made a good faith decision to retire based on the pensions they had earned – which they reasonably believed to be guaranteed for the remainder of their life of expectancy – they forfeited the right to work longer and thereby accrue additional service credits. The City has not offered to rescind these employees' retirements and restore them to the positions they were in prior to retirement. Most, if not all, now live on a fixed income; they do not receive Social Security benefits for their City service. The damage claims of these retirees if the proposed "correction" process proceeds against them will be among the most compelling and sympathetic.

Accordingly, the City should authorize SDCERS to exclude these plan participants from the "correction" process because any benefit from including them is outweighed by a substantial risk that their meritorious legal claims will succeed and impose a greater cost burden on the City by increasing the pension plan's unfunded liability.

d. Direct SDCERS To Add A Compromise or Settlement Option For Active Employees Designed To Make the Plan "Whole" Without Punitive Interest Charges Being Added

1,536 active employee/plan participants now face limited "correction" options – each of which has adverse consequences depending on the employee's circumstances. However, there is *no option* which permits the employee to preserve the contract he/she signed in good faith during the "window period" by paying the difference between the "old rates" charged and the "new rates" which the City argued, and the Court agreed, should have been charged for any contracts after August 15, 2003. Allowing an employee to pay *now* what the City argues should have been paid *then* – but *no more than that* – would put the City, the plan, and the innocent employees in the position they would have been in if the "window period" had not been adopted.

Currently, the "correction" option which SDCERS intends to offer affected plan participants – who want to preserve the "window period" purchase of service credit contracts they signed – only

permits them to "true up" the cost of these contracts by paying the difference between the "old rates" and the "new rates" with 8% interest added for the multi-year period involved. These interest charges are not only burdensome, they are punitive in their effect because these employees would not have paid any interest if the "new rates" had simply been charged in the first place. And the only reason they didn't do so at that time is because the SDCERS Board adopted a "window period" to which the City agreed.

Putting it another way, the fundamental argument which the City made and the Court accepted was that the SDCERS Board's decision to offer a "window period" was a violation of the San Diego Municipal Code (albeit with the City's agreement at the time). Had this alleged violation not occurred, no "window period" would have been adopted and all service credits purchased *after* August 15, 2003, would have been priced at the "new rates." By permitting employees to pay *now* what they would have paid *then* is a fair result which is consistent with the Court's ruling. Adding 8% interest to the bill is unfair because it is SDCERS' and the City's fault – not employees' fault – that "window period" was made available to them in the first place.

If the City, as plan sponsor, directs SDCERS to *add* this "true-up-without-interest" option to the "correction" options SDCERS otherwise intends to make available, the City will be presenting employees with *another option* which may, in fact, reduce the likelihood and/or number of potential costly individual legal claims. In fact, to assure that the City would be more likely to achieve this outcome, we propose that the City direct SDCERS to make this "true-up-without-interest" option available to those employees who *voluntarily* sign a release of all claims in exchange.

By offering employees this "trade-off," the City will make it more likely that the plan's unfunded liability associated with these "window period" purchase of service contracts will be reduced without the offsetting disadvantage of litigation expenses and potential costly damage awards. By accepting this "trade-off," an affected plan participant must pay additional hard-earned money for service credits he/she reasonably believed had been bought and paid for already, yet, by doing so, he/she can take some small comfort in knowing that the uncertainty surrounding this issue has been removed and that the punitive burden of interest charges has been avoided. Of course, as with the other options already identified by SDCERS, it would be the plan participant's decision whether to select this option and sign the release. Needless to say, neither MEA nor Local 127 has the power to guarantee that *any* plan participant would do so. But the compromise with regard to interest charges will be a significant inducement.

Accordingly, the City should authorize SDCERS to *add* this "true-up-without-interest" option to the options SDCERS has already identified, and to make this particular option available only to those plan participants who sign a release of claims form acceptable to the City.

4. Conclusion

We believe that the proposals we have outlined in this letter fulfill the objectives we identified above and are within the City's power to adopt. Moreover, if adopted, the City will thereby protect the City's best interests while achieving a fair outcome for the retirees and employees who have become the victims of circumstances for which they are not responsible.

In deference to the time-line SDCERS has described for implementing the proposed "correction" process, we welcome any opportunity to discuss this proposal with you on an expedited basis.

Dated: January 21, 2011

TOSDAL, SMITH, STEINER & WAX

By: Ann M. Smith

Ann M. Smith
Attorneys for SAN DIEGO MUNICIPAL EMPLOYEES ASSOCIATION

Dated: January 21, 2011

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Encl.: Ltr 8/11/10 from Ann M. Smith to SDCERS/PSC Ad Hoc Committee

cc: Jan I. Goldsmith, City Attorney
Jay Goldstone, Chief Operating Officer
Scott Chadwick, Human Resources Director
Andrea Tevlin, Independent Budget Analyst
Mark Hovey, SDCERS CEO
Elaine Reagan, SDCERS General Counsel
Mike Zucchet, MEA General Manager
Joan Raymond, President, AFSCME Local 127

TAB A

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August 11, 2010

Mr. Alan J. Arrollado
Mr. Raymond G. Ellis
Mr. David A. Hall
PSC Ad Hoc Committee Members
c/o Elaine Reagan, General Counsel
401 West A Street, 4th Floor
San Diego, CA 92101

Re: Legal and Ethical Obstacles to Any Proposed PSC "Corrections" Adversely Affecting Employees and Retirees

Dear Messrs. Arrollado, Ellis, Hall:

I write on behalf of those MEA-represented active and retired employees who are threatened with adverse action related to certain purchase of service contracts ("PSCs") as a consequence of the SDCERS Board's operational decisions (and votes) on August 15, 2003, and again on November 16, 2007, which have led to the published opinion filed on June 7, 2010, by the Fourth District Court of Appeal ("4th DCA") in *City of San Diego v. SDCERS*, D054688 (Super. Ct. No. 37-2007-00081912-CU-WM-CTL).

The 4th DCA concluded that SDCERS may not recover any underfunding associated with certain PSC contracts through the Unfunded Accrued Liability ("UAL") portion of its annual bill to the City because (1) the SDCERS Board's decision on August 15, 2003, to allow additional service credits to be purchased at the *old* rates during a 60-day "window period" was *unlawful*, and (2) the SDCERS Board's decision and vote on November 16, 2007, to charge the City for the funding shortfall – which triggered the City's timely writ petition – was also *unlawful*.

As to the Board's vote on November 16, 2007, "to charge the City for the underfunding," the court noted that SDCERS' own fiduciary counsel (Harvey L. Leiderman of Reed Smith LLP) had publicly stated that the Board's alternative was to "charge the employees" (instead of the City) by "voiding contracts, collecting arrears payments, offering rewritten contracts, spreading out additional payments or reducing benefit levels." The fact

that Mr. Leiderman's advice was clearly wrong (based on well-established legal and equitable principles, as well as the **undisputed outcome of past litigation and rulings which were clearly binding on the City and SDCERS**) – and likely constituted legal malpractice (as described below in detail) – went unmentioned in the 4th DCA's decision.

With Board Members Sullivan, Meyers, Lamberth and Thompson having recused themselves, the remainder of the Board followed Mr. Leiderman's advice and, in doing so, they – and he – ignored my express plea to take *no further action* for the reasons detailed in an 18-page Memorandum which I distributed to the Board on *October 19, 2007,* and, thereafter, buttressed in my follow-up e-mail communications.

Thus, regrettably, it was these *two Board actions* which have led directly to the heartache and threatened economic hardship to which certain plan participants are being subjected despite the unequivocal fact that they are innocent victims. During your first public hearing on this issue on August 6, 2010, you began to hear their personal stories and their undeniable anguish, disbelief, fear and confusion over the unwelcome news you have delivered to them in your recent communications. As one speaker correctly noted, neither the Union Tribune nor any other media outlet was present to hear these stories – another sign of the bias which informs all "news-making" in the City of San Diego.

In my presentation to you, I attempted to sum up the depth of this anguish based on the fact that employees and retirees have consistently viewed SDCERS, in its role as a *fiduciary*, to be a *trusted* protector of their legitimate interests in a City, and at a time, when they have been repeatedly victimized by hostile public opinion and by highly political decision-making which affects their employment in every respect from morale to take-home pay. They relied in good faith on the finality and enforceability of the *contracts* which SDCERS invited and prepared; they signed and performed these contracts to their detriment; they made irreversible career, financial, family and retirement decisions without ever doubting that SDCERS' (and the City's) promises to them were likewise *irreversible*.

It must also be emphasized that, in most cases, those employees who made a decision to apply to purchase service credits during the "window period" in 2003, did so as a result of the deliberate efforts and publicity generated by both SDCERS *and the City*. After the SDCERS Board's vote on August 15, 2003, SDCERS staff sent a notification to all City employees alerting them that PSC purchase applications received by SDCERS prior to November 1, 2003, would be priced under the *old* rates. The "PSC request form" which SDCERS provided to employees "reassured" them that SDCERS was in compliance with the laws governing this PSC purchase opportunity; the form stated: "The San Diego Municipal Code and Retirement Board Rules govern the PSC benefit; therefore, SDCERS must adhere to all regulations and rules pertaining to each PSC."

And the City's authorized managerial agents *promoted* this PSC "opportunity" in meetings held throughout the workplace. Thus, not only did the *City* approve the "window period" by and through its representatives on the SDCERS Board who voted in favor of it, but also the *City*, through its authorized managerial agents, induced employees to rely on the lawfulness of this PSC opportunity in making their critical decisions to use their savings, other assets, or even a portion of each paycheck, to purchase service credits at the price SDCERS set – a price which they neither influenced nor negotiated. Finally, if the City had disagreed with SDCERS' interpretation of the Charter, Municipal Code and/or its fiduciary duty when establishing the "window period" on August 15, 2003, the City could have and should have – but did not – bring a timely legal challenge to the Board's action (by writ of mandate). Instead, the City took *no action* to challenge SDCERS' right to offer, and employees' right to accept, irrevocable contracts to purchase service credits at the non-negotiable price SDCERS set.

THE "CORRECTION" OPTIONS

Based on SDCERS' communications to date to the potentially affected plan participants, it appears that SDCERS has concluded – albeit tentatively – that, if SDCERS may not permissibly include the unfunded liability associated with the service credit contracts arising from the "window period" in its calculation of the City's annual UAL payment, then the only viable solution to make the trust fund "whole" is to collect the underfunding from affected plan participants. **This is wrong**.

1. As Indemnitor of the SDCERS Board, The City Itself Is Liable To Affected Plan Participants For Their Economic and Non-Economic *Damages* Resulting From the SDCERS Board's Unlawful Ministerial Decision on August 15, 2003

While SDCERS may not charge the City *directly* for the PSC underfunding at issue here by adding it to the City's annual UAL cost, **the City – *not employees or retirees* – nevertheless remains *indirectly* liable to make SDCERS "whole" for this underfunding** as follows:

(A) The City's legal argument before the Superior Court and the Court of Appeal was, in essence, that the SDCERS Board acted *unlawfully* on August 15, 2003, in establishing a "window period" for additional PSCs contracts to be executed at the *old rates*. The City persuaded the courts that this Board decision – though motivated by a desire to fulfill its fiduciary duty to plan participants – was not a proper exercise of discretion deserving of judicial deference but was, instead, an unlawful ministerial or operational decision in direct violation of the plan documents as set forth in the City Charter and in the Municipal Code. While SDCERS argued to the contrary in defending the Board's action, the City's view prevailed. Accordingly, it follows from the City's argument that the SDCERS

Board breached its fiduciary duty to plan participants by allowing (indeed inducing) contracts to be signed, relied upon, and performed, when the Board (and its advisors) knew or, in the exercise of reasonable care, should have known that the plan document did or arguably could be interpreted to prohibit these transactions – thus, potentially subjecting plan participants to subsequent adverse action (as is now threatened). Nor did SDCERS disclose to employees *before* they signed and relied on the finality and enforceability of these "window period" PSCs that there was any risk these contracts might be found to violate the City Charter or the San Diego Municipal Code.

(B) At the time of its operational decision to establish a "window period" on August 15, 2003, the SDCERS Board had thirteen Members in office and in attendance at the meeting when they **voted twelve to one** in favor of implementing the new rates developed by the system's actuary for purchased service credits *and* in favor of allowing a "window period" for purchases to be accomplished at the *old rates*. The twelve Board Members who voted in favor of this "window period" included three appointed Members **Dick Vortmann, Diane Shipione, and Franklin Pierce; City Manager-designee Cathy Lexin, City Treasurer Mary Vattimo, City Auditor-designee Terry Webster**, and all six Members elected by Retirees (1), General Members (3), Fire Safety Members (1) and Police Safety Members (1). The only "no" vote was cast by appointee Ray Garnica.

(C) At the time the SDCERS Board took action to establish the PSC "window period" on August 15, 2003, Resolution R-297335 was in effect which the City Council had adopted on November 18, 2002, in recognition of the fact that Board Members "may, from time to time be subjected to claims and suits for actions taken in their capacity as such;" and that "there is a need to protect and encourage individuals who volunteer their time and their talent to serve in the public interest." By this broad indemnification Resolution – which included indemnification for punitive or exemplary damages under certain conditions – the City agreed that it:

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

(D) By Resolution R-301414, adopted on May 10, 2006, the City Council repealed its Indemnification Resolution R-297335, "for any acts or omissions by Board Members occurring *after April 18, 2006*. The repealing Resolution states on its face that notice of this repeal was given on April 20, 2006, to the SDCERS Board Members in office at that time.

(E) While Resolution R-301414 effectively ended the broad and automatic obligations established by Resolution R-297335, it did *not* end the City's obligation to defend and indemnify SDCERS Board Members for acts and omissions after April 18, 2006. Resolution R-301414 simply stated that "any determination of whether to provide a defense and indemnification would be governed by the provisions of Government Code sections 825 and 995."

(F) On July 25, 2007, the 4th DCA upheld the Superior Court's enforcement of Resolution R-297335 by ordering the City to pay both (1) the costs and attorneys fees incurred by Board Members in defending against the civil litigation filed against them by San Diego City Attorney Mike Aguirre, and (2) the costs and attorneys' fees they incurred in suing the City to enforce the obligations of Resolution R-297335. *Torres, et al. v. City of San Diego* (2007) 154 Cal.App.4th 214.

Accordingly, if SDCERS takes adverse action against employees or retirees on the PSCs at issue here, the following cascading events are surely to follow as night follows day:

- Such adverse action will give rise to meritorious damage claims against the SDCERS Board Members whose acts or omissions on August 15, 2003, constituted a breach of fiduciary duty;

- These Board Members will, in turn, look to the City to defend *and indemnify* them;

- The City will be obligated to do so based on binding appellate authority in *Torres, et al. v. City of San Diego* (2007) 154 Cal.App.4th 214;

- These Board Members will likely be forced to concede that their decision on August 15, 2003, *was a breach of fiduciary duty* based on the successful argument the City already made and the Court of Appeal accepted in *City of San Diego v. SDCERS*, D054688 (Super. Ct. No. 37-2007-00081912-CU-WM-CTL);

- Damage awards would likely follow in the amount of each employee's and retiree's harm – which would include both economic and non-economic damages since the measure of damages for a breach of fiduciary duty is the traditional tort recovery per Civil Code section 3333 – i.e., "the amount which will compensate for all the detriment proximately caused thereby, whether it could have been anticipated or not." (See also Civil Jury Instruction 4101; *Michelson v. Hamada* (1994) 29 Cal.App.4th 1566, 1582.)

- As indemnitor, the City, not SDCERS, will be required to indemnify these Board Members for these damages awards.

Accordingly, by pursuing the aggressive arguments it did and by procuring a determination that the Board's 8/15/03 operational decision was *unlawful,* the City itself has essentially *proven* that a breach of fiduciary duty occurred – a breach for which the City is the express indemnitor.[1]

While the City undoubtedly expected that employees/retirees would bear the brunt of its litigation strategy, the opposite is true because the *City itself must pay for all of the harm caused to plan participants by the SDCERS Board's acts or omissions on August 15, 2003.* In calculating the likely amount of these damages, SDCERS may reasonably assume that the *minimum* amount of the economic harm to employees and retirees would be the full value of the "underfunded" purchase price of the PSC contracts at issue; yet, if SDCERS proceeds with adverse action against employees and retirees, the economic damages will undoubtedly be greater than this amount because each individual employee's and retiree's particular circumstances and hardships must be taken into account when measuring damages. Moreover, if SDCERS proceeds, each employee's and retiree's non-economic damages in the form of emotional and mental distress, fear, anxiety, worry, and anger (as previewed by the individual stories presented on August 6, 2010) must be added to the total damage calculation *for which the City is ultimately liable.*

Thus, the City's seeming "victory" in this litigation is a hollow one. In its gleeful rush to judgment in this case (initiated by former City Attorney Mike Aguirre without City Council's authorization and pursued without careful scrutiny by City Attorney Goldsmith), the City has failed to assess and appreciate the risk it ultimately faced if it succeeded – whereby it would become obligated to pay *in tort damages* an amount which is equal to or greater than the amount SDCERS had added to the UAL for these "window period" PSCs. The result is that the City's annual budget will be further strained because a judgment for tort damages would be permissibly spread over a maximum of ten (10) years (under certain conditions) rather than amortized over twenty years as this portion of the UAL would be.

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[1] This result is also consistent with the legal doctrine of vicarious liability whereby a principal (i.e., the City as pension plan sponsor) is liable for the negligence of its agent (i.e., SDCERS as pension plan administrator). And, as a practical matter, all expenses incurred by SDCERS to defend itself against legal claims and/or to pay damage claims against it are ultimately borne entirely by the City in any event.

2. The City, SDCERS, and/or Its Former Fiduciary Counsel Must Make The Plan "Whole" for Any Window Period PSC Underfunding – Not Employees Or Retirees – Due to the Board's Ill-Advised And Careless Operational Decision on November 16, 2007, Which Put Plan Participants Directly In Harm's Way

When the SDCERS' fiduciary counsel Harvey Leiderman of Reed Smith LLP made a Power Point presentation to the Board on "Pricing of Additional Service Credit Purchases" on October 19, 2007, he noted that the City Attorney had "threatened litigation" and that he, as SDCERS' fiduciary counsel, had "commenced his legal analysis" in March 2007, leading to three closed sessions of the Board in July, August and September 2007, "to address pricing issues," with the affected Board Members having recused themselves (Mark Sullivan, Franklin Lamberth, Steven Meyer and John Thomson).

Mr. Leiderman suggested that the Board could take any one of *six* potential actions related to *all* PSC contracts; *five* of those actions were adverse to plan participants who had signed and performed PSC contracts – i.e., "voiding contracts, collecting arrears payments, offering rewritten contracts, spreading out additional payments or reducing benefit levels." Only *one* of the *six* proposed actions maintained the status quo – i.e., "continuing to collect the shortfall through the amortization of the system's unfunded liability."

Although Mr. Leiderman's Power Point presentation itemized "issues for consideration" which included queries suggestive of legal or equitable barriers to the Board's actually taking any of the *five* adverse actions, he did *not* qualify the Board's alleged *discretion* to do so in any respect – leaving the impression, as the Court of Appeal noted, that there would have been no legal or equitable barriers to the Board's having voted to take any one of those *five* actions instead of the one it did.[2] He described the Board's fiduciary duties in considering the appropriate action to take as (1) the duty to preserve and protect the fund; to pay benefits that are promised and earned and collect sufficient contributions to support the benefits; (2) the duty to correct errors when appropriate and not perpetuate erroneous interpretations of the plan; (3) the duty to act fairly and equitably to members and their beneficiaries; and (4) a subordinate duty to minimize employer contributions, consistent with fiduciary duties.

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[2] For example, Mr. Leiderman's Power Point asked: "Did members reasonably rely on the PSC pricing? Could members be returned to their pre-purchase positions? Could members be rehired to their old positions? Is it practical for the Board to collect arrears payments? May the Board adjust any PSC contracts, and if so, how? Is there a likelihood of litigation arising, and if so, at what cost?"

Although Mr. Leiderman's Power Point presentation on October 19, 2007, noted that the goal of the planned public sessions on October 19 and November 16, 2007, was to "(1) offer a forum to all stakeholders, (2) gather additional relevant evidence and data, (3) obtain useful perspective on the issues under consideration and potential actions, and (4) assure the public that the Board (was) acting fairly, openly, responsibly and prudently," my very detailed presentation analyzing *why* it was imperative that the Board take ***no further action*** went unheeded. (See attached 18-page Memorandum dated 10/19/07 entitled "Purchased Service Credits: What Should SDCERS Do?")

Although Mr. Leiderman's Power Point presentation had identified as an "issue for consideration" whether "the Board should file a declaratory relief action to get direction from the courts," I spelled out in painstaking detail that **SDCERS had already done so on July 26, 2005** (*SDCERS v. City of San Diego*, GIC 851286; consolidated with *SDCERS v. Aguirre, et al.* GIC 841845), using plan assets, **and had procured an Order from the Court** on SDCERS' Motion for Summary Judgment/Adjudication (which the City opposed) **"that SDCERS may properly and legally pay all City Retirement Benefits, including, but not limited to, the *Contested Benefits*."** SDCERS' declaratory relief complaint itself **defined** what these *Contested Benefits* were by reference to former City Attorney Mike Aguirre's Memorandum dated June 17, 2005, directed to City Auditor and Comptroller John Torell, and copied to SDCERS' Retirement Administrator and General Counsel, demanding that certain "illegal" retirement benefits not be paid; the list included, among others:

> **"Any retirement benefit based on a Purchase of Service Credit that was purchased by a member at a rate that was not actuarially neutral."**

In seeking a declaration from the Court "that SDCERS may properly and legally pay all City Retirement Benefits, including, but not limited to, *the Contested Benefits*," SDCERS explained in its Complaint why its action was appropriate and necessary as follows:

> ¶ 24: Pursuant to its duties under the California Constitution and the Charter, the Board has a fiduciary duty to seek a judicial determination of the legality of retirement benefits to its members upon reasonable notice that the legality of such benefits is disputed. Therefore, the Board has filed this declaratory relief action for the express purpose of discharging its fiduciary duty to all of its members and their beneficiaries to determine the legality of the **Contested Benefits**.[3]

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[3] This is apparently the concept which Mr. Leiderman had in mind when he presented the issues to the Board on October 19, 2007; though he did not inform the Board that SDCERS had already procured a declaration related to these PSCs.

Thus, when the Court granted SDCERS' motion on October 16, 2006, SDCERS had the final ruling it sought "for the express purpose of discharging its fiduciary duty to all of its members and their beneficiaries." That ruling clearly and unequivocally confirmed **"that SDCERS may properly and legally pay all City Retirement Benefits, including, but not limited to, the *Contested Benefits*."** In addition to this definitive ruling, as I detailed in my 18-page Memorandum, other litigation-related events *before* and *following* this ruling had established an ironclad roadblock against the City's misguided efforts to force the undoing of the PSC *contracts* which SDCERS had prepared and on which employees had relied in planning their work and personal *lives*.

Accordingly, the SDCERS Board's public meetings on PSC contracts in October and November 2007, were entirely unnecessary. SDCERS' fiduciary counsel was inexcusably unaware – or misunderstood – what had already occurred and been achieved during costly prior litigation, including the declaratory relief SDCERS itself had already sought and achieved.

As a result, Mr. Leiderman guided the Board down a path which subjected hundreds of plan participants to unnecessary stress, anxiety and anguish (see tapes of meetings on October 19, 2007, and November 16, 2007). Even though the Board *intended* to act in a manner which did *not* alter SDCERS' contractual liability to plan participants based on their signed PSC contracts but, instead, to preserve the *status quo* by including the unfunded liability associated with all PSC contracts in the UAL, the Board was advised to *take action* – albeit an unnecessary one – which ultimately undermined SDCERS' *contracts* with plan participants.

Thus, as reported in the Board's Summary, on November 16, 2007, after a closed session from 9:30 a.m. to 10:26 a.m., "the Board returned to open session at 10:50 a.m., and Board President Thomas Hebrank announced that in closed session the Board had determined, by a unanimous vote of 8 to 0, to allow the existing purchased service contracts to remain as formulated and to *continue* to amortize the shortfall through the existing unfunded actuarial liability." Because the Board conducted its discussions on this issue in a *closed* session on November 16, 2007, it is not known whether Board members understood the *effect* of *taking a vote* as opposed to *taking no further action* as I had urged on October 19, 2007, when presenting my 18-page Memorandum.

Moreover, I also do not know whether Mr. Leiderman had considered the potential effect of *taking this action* as opposed to *taking no further action.* While I do not claim to know today what Mr. Leiderman's thought process or motivations may have been in this regard – and I am not asserting that he acted deliberately rather than negligently in handling this issue – I am informed by a reliable source (which would undoubtedly be confirmed during any litigation-related discovery process) that Mr. Leiderman's first telephone call after

his professional services were terminated by SDCERS soon after the November 16, 2007, Board meeting, was to Executive Assistant City Attorney Don McGrath who was City Attorney Mike Aguirre's second-in-command in the effort to reduce employees' and retirees' vested pension benefits and one of the attorneys of record on the City's writ petition.

Although the Board's decision on November 16, 2007, was to maintain the *status quo* by (1) not attempting to alter its contractual obligations with plan participants, and (2) continuing to include PSC underfunding in the plan's UAL as had been its practice, this unanimous vote on November 16, 2007, gave rise to the City's timely writ of mandate (filed four days later without City Council approval) challenging the Board's ministerial action to "charge the City for this shortfall" as unlawful. Moreover, the City argued, and the courts agreed, that the Board's action did not involve a basic policy decision such that judicial deference was warranted; its action was, instead, an unlawful ministerial decision in direct violation of the City Charter and San Diego Municipal Code.

Thus, despite the ironclad record of prior litigation barring a legal challenge to these PSCs – and despite other available defenses to any attempt to unwind or "rewrite" these contracts (i.e., *res judicata*, the statute of limitations, and detrimental reliance, among others), the SDCERS Board's *action* deprived plan participants of these legitimate legal and equitable defenses and exposed them to the harm **which SDCERS itself is now threatening to take against them.**

Accordingly, if SDCERS proceeds with adverse action against employees and retirees on these PSC contracts, these employees and retirees will, in turn, have a meritorious claim against the SDCERS Board for its action on November 16, 2007, which, under all the circumstances, constituted a breach of fiduciary duty entitling them to a tort measure of damages as explained above in relation to the Board's action on August 15, 2003. The Board may, in turn, have a viable claim for malpractice against Mr. Leiderman and Reed Smith LLP as a result of the advice which induced their action constituting a breach of fiduciary duty.

I do not know whether SDCERS had a policy of insurance in effect on November 16, 2007, which would provide a defense and indemnification of Board Members for any such claims if employees and retirees file them. Nor do I know what malpractice insurance Reed Smith LLP had in effect during the relevant period which might be available to cover the damages arising from the Board's negligent ministerial action November 16, 2007. However, I do know that both potential insurance sources must be looked to as a proper and viable means of making the SDCERS trust fund "whole" for any losses associated with the PSC contracts at issue in this case – *instead of looking to employees and retirees to do so.*

Finally, apart from any potential insurance coverage which may be available to the SDCERS Board and/or to Harvey Leiderman/Reed Smith LLP to defend and indemnify them

against the damage claims which will inevitably arise if SDCERS takes adverse action against employees and retirees, the **City itself will also remain as an indemnitor** of the individual Board Members who participated in the decision on November 16, 2007.

Even though the broad indemnity Resolution R-297335 had been repealed by the City Council on May 10, 2006, "for any acts or omissions by Board Members occurring *after April 18, 2006*, the City Council's new Resolution R-301414 affirmed that "any determination of whether to provide a defense and indemnification (for acts or omissions after April 18, 2006) would be governed by the provisions of Government Code sections 825 and 995." These code sections require a public entity to defend an employee or former employee who is sued in his or her official or individual capacity on account of an act or omission in the scope of his or her employment, and to pay any resulting judgment, compromise or settlement. And section 117 of the City Charter provides that members of the city's Boards and Commissions are deemed to be unclassified employees of the City. Accordingly, sections 825 and 995 apply to SDCERS Board members who are not otherwise employed by the City.

Thus, the City remains the indemnitor of the Board's actions *after* April 18, 2006, including but not limited to its action taken on November 16, 2007. To the extent that SDCERS pursues adverse actions against plan participants on PSC contracts which SDCERS induced them to sign and on which these plan participants thereafter relied when making life-altering decisions, these adverse actions will be a direct consequence of the Board's breach of its fiduciary duty when it took an unnecessary, gratuitous and negligent ministerial action on November 16, 2007, thereby putting at risk PSCs on which plan participants had detrimentally relied. As noted above, those plan participants who are adversely affected, will have meritorious claims for a tort measure of damages against these SDCERS' Board members who, in turn, will have an absolute right to seek both a defense and indemnification from the City of San Diego.

3. SDCERS May Not Unilaterally "Void" or "Re-Write" These PSCs and Any Legal Action Seeking to Modify These Contracts Will Require Individualized Proof of "Cost Neutrality" And Will Trigger Individual Defenses And Cross-Claims

SDCERS' communications to employees and retirees to date suggest that SDCERS may and will unilaterally "undo" or "re-write" the affected PSCs because the 4th DCA's decision leaves it no other alternative. **This is wrong**.[4]

[4] Nor may SDCERS side-step its fiduciary duties under the circumstances by proposing a rescission/correction plan to the IRS in any *ex parte* VCP proceeding which undermines the state law rights of plan participants or deprives them of their state law remedies.

As noted above, the Court of Appeal's ruling was quite narrow in concluding *only* that SDCERS may not "lawfully" include the "window period" PSC underfunding in the UAL to be paid by the City. Alternative means to make the trust fund "whole" as identified above were not considered by the Court nor were employees or retirees "heard" at all in the proceedings which led to this decision.

Well-established state law principles related to *contracts* and *vested* pension benefits prevent any such unilateral actions.[5] Instead, SDCERS may only *propose* a PSC "re-write" to each affected plan participant, together with a full disclosure of the economic consequences of the proposed "re-written" contract and the plan participant's rights in the matter, and, after such a full disclosure, invite the plan participant's *voluntary* agreement to rescind the prior PSC and accept SDCERS' proposed modification.

In the absence of such a *voluntary* contract modification, SDCERS' only recourse would be to take legal action against each individual employee or retiree (or other beneficiary whose rights derive from an employee or retiree), such that SDCERS would be required to prove, by a preponderance of the evidence, why a timely modification of this contract can or should occur under the law. In response, each employee or retiree will have the right and the opportunity to raise any and all defenses against SDCERS' claim based on law and equity; and, in addition, may cross-claim against the City based on the relevant facts in his or her case. **A sampling of the issues likely to be raised includes:**

(A) Legal Actions Against Retirees and Active DROP Members:

(1) Those employees who made decisions to *retire* or to sign *irrevocable DROP contracts* after the City's writ of mandate had been filed against SDCERS on November 20, 2007, were not given any warning or other form of written disclosure by SDCERS (or the City) that their prior PSCs were being challenged or might be subject to rescission/correction as a result of this litigation.

- Accordingly, their decisions to *retire* and/or to enter *DROP* after November 20, 2007, were not based on a knowing and intelligent waiver of their rights under the pension plan and/or of their rights to continued employment with the City.

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[5] After retirement, pension benefits vest *absolutely* and the power to modify contractual pension rights is non-existent. *Terry v. City of Berkeley* (1953) 41 Cal.2d 698, 702-703. Moreover, San Diego Municipal Code section 24.1404, subsection (b), establishes that "all amounts credited to a Member's DROP Participation Account are fully vested." This, of course, includes all monthly pension allowances credited to the DROP account based on the amount of the service retirement awarded by the Board.

▸ However, as plan administrator, SDCERS does not have the power, by itself, to make them "whole" for the harm which would flow from the rescission or modification of their PSCs because (1) SDCERS cannot rehire them into the positions from which they retired, and/or (2) SDCERS cannot agree to rescind their irrevocable DROP contracts because the City is also a signatory to these contracts.

▸ The detrimental reliance and irreparable harm these plan participants would suffer from any rescission or modification of their PSCs are **insurmountable obstacles/defenses** which SDCERS cannot overcome in any court of law or equity, and, in the proper exercise of its fiduciary duty, SDCERS should take no further action against them.

(2) SDCERS may not unilaterally change the amount of any retiree's or active DROP member's retirement allowance; this amount became final and binding upon **SDCERS and the member** at the time the Board approved the employee's retirement and/or change in status to "active DROP."

▸ If SDCERS now claims that any retiree or active DROP member owes additional contributions to SDCERS – *and* SDCERS makes an informed determination as a fiduciary that it is in the best interest of the plan to pursue a legal claim against a retiree or active DROP member to recover these additional contributions, SDCERS will be obligated to prove this claim to the satisfaction of a court of law or equity and, in doing so, to overcome all defenses raised by the retiree or active DROP member before procuring a money judgment against the retiree or active DROP member. These defenses will include, but not be limited to:

- the bar of the statute of limitations,
- the equitable doctrine of laches,
- the Board's breach of fiduciary duty,
- the doctrines of promissory and equitable estoppel,
- the bar of a fully-performed contract,
- the vested rights doctrine under the state and federal constitutions).

▸ As noted above, in any such legal action which SDCERS initiates, any retiree or active DROP member will also be entitled to file a cross-claim against the City for the City's direct culpability in approving the "window period" in August 2003, and for thereafter inducing the retiree or active DROP member to rely to his/her detriment on the finality and enforceability of these PSCs – as well as for the City's vicarious liability for the negligence of its plan administrator.

- Pursuant to San Diego Municipal Code section 24.1008, even if SDCERS procures a money judgment against a retiree or active DROP member, SDCERS will become a simple judgment creditor and will have *no right* to subject the retiree's or active DROP member's retirement allowance to execution, garnishment, attachment or any other process of any court except to the extent permitted by California Code of Civil Procedure section 704.110 (limited to judgments for child, family or spousal support).

(B) Legal Actions Against Active Employees:

(1) For the same reasons described above, SDCERS may ***not*** unilaterally rescind or alter the irrevocable "window period" PSCs which became final and binding upon each plan participant who remains an active employee of the City. Many of these contracts have been fully performed by the employees who fully paid for the purchase *years ago* – at the non-negotiable price SDCERS set – in justifiable reliance on the finality and enforceability of these contracts. With the City's express approval of this "window period," these employees drew upon limited assets or otherwise found the means to raise the funds needed to complete these purchases and the purchased service was added to their "creditable service" balances. Other employees have paid and continue to pay for their PSCs by pre-tax and post-tax payroll deductions – thus *diminishing* their bi-weekly take-home pay available to support themselves and their families – also in justifiable reliance on the finality and enforceability of these contracts.

(2) If SDCERS does not get an employee's *informed* and *voluntary* agreement to rescind or modify his/her prior "window period" PSC, SDCERS will be required to take legal action against each individual employee precisely in the manner described above with regard to retirees and active DROP members – and with the same defenses being available and the same potential cross-claim being asserted against the City.

(C) In Any Such Legal Actions, SDCERS Will Have the Burden to Prove What Specific Amount of "Underfunding" Occurred With Each PSC

The City's Purchase of Service Credit program under its pension plan is set forth in Division 13 of Article 4 ("CERS") of the San Diego Municipal Code. Division 13 establishes the types of service credit which may be purchased. For example, Section 24.1302 establishes a plan member's right to purchase service credit covering his/her probationary period if a *prescribed* amount is paid into the system; section 24.1306 establishes a member's right, upon re-employment with the City, "to repay any refunded contributions with interest at the actuarial interest rate under terms and conditions prescribed by the Board."

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Other sections of Division 13 establish additional types of service which may be purchased but offer no specificity regarding the cost to be charged. See, for example, section 24.1303 (previous City service); section 24.1304 (part-time or hourly service); section 24.1305 (purchase of service credit upon reinstatement); section 24.1308 (service by officer or employee not previously included within the field of membership); and section 24.1309 (military service). Although these sections do not specify what must be paid for the service being purchased, section 24.1310 provides the following "catch-all" provision:

> To purchase Creditable Service, a Member must elect to pay and thereafter pay, in accordance with such election before retirement, into the Retirement Fund **an amount, including interest, determined by the Board.** No Member will receive Creditable Service under this Division for any service for which payment has not been completed pursuant to this Division before the effective date of the Member's retirement.

However, two other sections under Division 13 offer greater specificity related to the cost for *certain* service credits:

- for a purchase of an approved leave of absence, section 24.1307 requires payment of an amount "determined by the Board to be the equivalent of the employee cost of that service" if the absence was less than one year; and requires payment of an amount "determined by the Board to be the equivalent of the employee and employer cost of that service" if the absence exceeds one year.

- for a "five-year" purchase option (commonly known as an "air-time" purchase), section 24.1312 requires payment of an "amount the Board determines to be the employee and employer cost of that Creditable Service."

Thus, while SDCERS has used both "flat rates" (1997 through 2008) and "age/service-based" rates (since 12/19/08) for pricing service credits when performing its ministerial duty under the plan, if SDCERS initiates legal action against any plan participant based on the theory that he or she did not pay the amount "required by the San Diego Municipal Code" – albeit he or she paid the amount the Board had determined to be the correct amount at the time the purchase price was established by contract – SDCERS will be required to prove the *actual cost which should have been paid at that time by that employee based on the actual requirements of the San Diego Municipal Code and all relevant actuarial considerations*. The "old" or "new" flat rates will be irrelevant in this process as they were adopted for the administrative convenience of SDCERS and did not necessarily reflect the actual cost for each employee executing a PSC. Indeed, this point is borne out by the numbers Cheiron presented to the Board on October 19, 2007, which showed, in pertinent part, that:

- as of the June 30, 2006, actuarial valuation, General Members who purchased service credits during the "window period" had "underpaid" (as a group) by a total of $22,049,867 [and some of these General Members retired *before* November 20, 2007, and are not impacted by the City's Writ Petition];

- as of the June 30, 2006, actuarial valuation, Safety Members who purchased service credits during the "window period" had "overpaid" (as a group) by a total of $1,047,024 [and some of these Safety Members retired *before* November 20, 2007, and are not impacted by the City's Writ Petition].[6]

As Cheiron emphasized to the Board on December 19, 2008, the "single rate for all members is not an approach widely used elsewhere, is unnecessarily simplistic and undercharges a few members at the expense of overcharging most members."

Accordingly, once each individual General or Safety Member's *actual* cost is determined by SDCERS as part of its required proof in any legal action to collect additional contributions from the employee (on the theory that SDCERS did not charge the amount "required by the San Diego Municipal Code"), it will become clear whether that individual employee paid too much (and is owed a refund by SDCERS) or paid too little and owes additional contributions to SDCERS – subject to the defenses and cross-claims otherwise available to defeat SDCERS' claim for such additional contributions as described above. In that context, among other potential issues, the impact of investment gains and losses over the life expectancy of each individual employee who purchased service credits must also be considered because Cheiron did not include investment gains in excess of the assumed interest rate when calculating the alleged "underfunding" as of the 6/30/06 valuation date – and the 4th DCA specifically observed that the underfunding at issue in the case before it "may have been avoided entirely if, for example, the retirement fund experienced better than expected investment returns."

4. What Should the PSC Ad Hoc Committee Do With the Information Presented in This Letter?

- **Post this letter on the SDCERS' website.**

First, in the interest of full disclosure to employees and retirees who received SDCERS' prior communications on this issue, it is imperative that the information contained

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[6] Cheiron also noted in its 8/14/07 letter to SDCERS that a portion of the unfunded liabilities associated with all PSCs were *not* part of the UAL as of June 30, 2006, because these amounts represented benefits in excess of IRS section 415 limitations and were, in any event, a direct obligation of the City.

in this letter be made available to them and it is incumbent upon SDCERS, acting in its fiduciary capacity, to make it available – even if SDCERS does not agree with its contents. Only in this manner will all retirees and employees be able to make a more informed judgment about how to protect their rights and defend their vested pension benefits without incurring the burdensome and prohibitive costs of seeking individual counsel.

Because SDCERS is using its website as the medium to disseminate information on this issue in a timely manner, and this website is funded by plan assets belonging to *all* plan participants, it would be most appropriate for this letter to be posted on the SDCERS website as an item of interest to members who are or may be impacted by the work being done by the PSC Ad Hoc Committee – together with any disclaimer that SDCERS does not endorse or agree with its contents (if this is the case).

- **Reconsider the list of "correction" options tentatively identified.**

Next, the PSC Ad Hoc Committee and, thereafter, the full Board, must make a full and complete evaluation of the issues raised in this letter before proceeding with any proposed "corrections" of the "window period" PSCs. As fiduciaries, SDCERS must not continue to subject plan participants to the anguish and worry they are currently experiencing as a result of SDCERS' recent communications when, in the exercise of due care, SDCERS has other lawful and proper means to make the trust fund "whole" for these underfunded PSCs without looking to retirees and employees to do so. Those means are outlined in detail in this letter and each must be evaluated and acted upon – or, if rejected, a sound rationale for the rejection (based on fact and law) must be offered to those affected. In view of the City's ultimate liability in the matter, it would be unconscionable for SDCERS to use trust fund assets to subject retirees and employees to adverse consequences and thereby transfer to them the obligation to cross-claim against the City and/or to counterclaim against SDCERS and the relevant Board Members in order to trigger the City's obligation to defend and indemnify those Board Members. Nor, frankly, is there any logical reason to subject these Board Members to such an ordeal.

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In short, SDCERS has the power and the duty to see that a thorough analysis is done and that decisions are made in keeping with its fiduciary duties and, thus, unencumbered by "political" considerations. On behalf of all affected employees and retirees, as well as MEA, I urge you to do just that and I look forward to additional opportunities to work with you in achieving this outcome.

Sincerely,

Ann M. Smith

cc: Mayor Jerry Sanders
COO Jay Goldstone
City Attorney Jan Goldsmith
Deputy City Attorney Walter Chung
MEA President Tony Ruiz
MEA General Manager Mike Zucchet
Firefighters Local 145 President Frank DeClercq
SDPOA President Brian Marvel
AFSCME Local 127 President Joan Raymond
DCAA Representative George Schaefer
San Diego Alliance of Unrepresented Employees (AUE)
Retired Employees Association
SDCERS Board Members (August 15, 2003)
SDCERS Board Members (November 16, 2007)