

Office of Audit Services



Public Agency Review

Fallbrook Public Utility District

CalPERS ID: 2373193306
Job Number: FR15-001

October 2016



California Public Employees' Retirement System
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October 20, 2016

CalPERS ID: 2373193306
Job Number: FR15-001

Marcie Eilers, Administrative Services Manager
Fallbrook Public Utility District
PO BOX 2290
Fallbrook, CA 92088-2290

Dear Ms. Eilers:

Enclosed is our final report on the results of the public agency review completed for the Fallbrook Public Utility District (Agency). Your written response, included as an appendix to the report, indicates agreement with the issue noted in the report.

In accordance with our resolution policy, we have referred the issues identified in the report to the appropriate divisions at CalPERS. Please work with these divisions to address the recommendations specified in our report. It was our pleasure to work with your Agency. We appreciate the time and assistance of you and your staff during this review.

Sincerely,

Original signed by Beliz Chappuie

BELIZ CHAPPUIE, Chief
Office of Audit Services

Enclosure

cc: Board of Directors, Fallbrook Public Utility District
Brian Brady, General Manager, Fallbrook Public Utility District
Paula Clark, Accounting Supervisor, Fallbrook Public Utility District
Risk and Audit Committee Members, CalPERS
Matthew G. Jacobs, General Counsel, CalPERS
Anthony Suine, Chief, BNSD, CalPERS
Renee Ostrander, Chief, EAMD, CalPERS
Carene Carolan, Chief, MAMD, CalPERS

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RESULTS IN BRIEF

The California Public Employees' Retirement System (CalPERS) Office of Audit Services (OAS) previously issued a compliance review of the Agency in August 2015. The objective of the review was to determine whether the Fallbrook Public Utility District (Agency) complied with applicable sections of the California Government Code (Government Code), California Code of Regulations (CCR), and its contract with the California Public Employees' Retirement System (CalPERS). However, the review excluded a determination as to whether an individual was enrolled and reported by the Agency and its affiliate complied with the Government Code. The Office of Audit Services (OAS) performed a subsequent review and noted the following finding. Details are noted in the Results section beginning on page two of this report.

- The Agency reported compensation for an individual who performed services as an employee of an affiliated entity.

OAS recommends the Agency comply with applicable sections of the California Government Code, CCR and its contract with CalPERS. We also recommend the Agency work with the appropriate CalPERS divisions to resolve issues identified in this report.

SCOPE

OAS performed and issued a compliance report on the Agency's payroll reporting and enrollment reporting procedures in August 2015. During the course of performing this review, OAS identified a potential common-law employee enrollment and reporting issue in connection with the individual that provided services for the affiliated entity, Rainbow Municipal Water District (RMWD). As a result, OAS performed a follow-up membership enrollment review to further analyze this issue.

This follow-up review is limited to the examination of records pertaining to the employee/employer relationship of sampled employees working for the Agency. The review objectives and a summary of the procedures performed are listed in Appendix B.

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OFFICE OF AUDIT SERVICES REVIEW RESULTS

1: An employee of an affiliated entity was incorrectly reported to CalPERS.

Condition:

The Agency incorrectly reported compensation earnable for the Agency's General Manager. The individual was hired as the Agency's full time General Manager on July 19, 2011. On April 5, 2013, the Agency entered into a Joint Exercise of Powers Agreement (JPA) with Rainbow Municipal Water District (RMWD) to share the General Manager's services on a 50 percent basis. RMWD is a separate and distinct entity from the Agency with a separate Board of Directors. Both entities contract with CalPERS for retirement benefits. RMWD's organizational chart showed that the General Manager began working for RMWD on April 6, 2013. The General Manager was incorrectly reported as a full-time employee of the Agency from April 6, 2013 to April 5 2014, rather than half time, or 50 percent basis.

OAS found that the Agency and RMWD entered into agreements for the purpose of managing the combined resources of the Agency and RMWD in order to test the possibility of consolidating the Agency and RMWD. The agreements identified that the agencies would share staff as well as the physical plant/infrastructure to obtain cost-effective means for providing services to ratepayers. As a result, the two entities came together through a JPA and an Employee Leasing Agreement with the intention of sharing employees. The JPA's effective date was April 5, 2013 to April 5, 2014, and the General Manager was hired by RMWD on April 6, 2013 to perform services as the General Manager. The dissolution of the JPA ended the Employee Leasing Agreement and thus the agreement to share the Agency's staff.

OAS reviewed the employment status of the Agency's General Manager to determine whether the individual was an employee of one or both entities from April 6, 2013 to April 5, 2014. Also to determine whether the General Manager's compensation earnable was accurately reported to CalPERS. The Agency explained that during this period the General Manager worked fifty percent of the time for the Agency, and the other fifty percent for RMWD. However, the Agency reported the General Manager on a full-time basis.

In order to make the determination, OAS reviewed the General Manager's Employment Agreement, an Employment Leasing Agreement, the JPA agreement, and an employment relationship questionnaire. Using this information, OAS performed a common-law employment test to identify the services performed under each entity, and which entity controlled the manner and means in which the services were performed. OAS identified the following common facts:

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General Manager's duties and compensation under the Agency from April 6, 2013 to April 5, 2014

- Performed General Manager services on a half-time, or 50 percent basis.
- The Agency was reimbursed at one-half of the individual's monthly compensation (including salary and benefits) from RMWD.
- The General Manager position was listed on the Agency's organizational chart.
- The job description stated that the individual would serve at the will and pleasure of the Agency's Board of Directors.
- The Agency does not have first call on the individual's time. Individual's services are shared with RMWD.
- The right to control the manner and means of how the General Manager does his work is shared between the Agency and RMWD.
- The General Manager is required to attend Agency meetings.
- Services are performed at the Agency office.
- Work is directed, supervised or reviewed by the Agency's Board of Directors.
- General Manager uses the office, office equipment, stationery, e-mail, and business cards of the Agency.
- The General Manager was delegated the authority by the Agency's Board to plan, organize and control Agency programs, services, and resources in accordance with short- and long-term goals, policy statements and directives; administer and carry out policies established by the Board; monitor program results to ensure that they effectively support the Agency's goals and objectives; recommend construction contracts, leases and other legal agreements to the Board for approval; and present for the Board's consideration major goals and policy alternatives and recommendations for the Agency.
- The General Manager was also delegated the authority by the Agency's Board to analyze monthly financial statements, engineering reports, labor distribution report, water sales report and other operating reports; develop water and sewer rate and fee schedules for Board consideration; review agreements negotiated by staff; and perform highly significant and specialized responsibilities in connection with inter-jurisdictional, legal, engineering and other administrative problems.
- The General Manager was also delegated the authority to monitor and oversee Agency's human resources programs related to employment, classification and compensation, employer-employee relations, employee benefits, safety, recognition, performance evaluation and discipline.

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General Manager's duties and compensation under RMWD from April 6, 2013 to April 5, 2014

- Performed General Manager services on a half-time, or 50 percent basis.
- RMWD reimbursed the Agency for payment to the individual at one-half of the individual's monthly compensation (including salary and benefits).
- The individual was listed by name on the RMWD organizational chart as General Manager with a hire date of April 6, 2013.
- The job description stated that the individual would serve at the will and pleasure of RMWD Board.
- RMWD does not have first call on the individual's time. Individual's services are shared with the Agency.
- The right to control the manner and means of how the General Manager does his work is shared between RMWD and the Agency.
- General Manager is required to attend RMWD meetings.
- Services are performed at RMWD's office.
- Work is directed, supervised or reviewed by RMWD's Board of Directors (RMWD Board).
- General Manager uses the office, office equipment, stationery, e-mail account, and business cards of RMWD.
- The General Manager was delegated the authority by the RMWD Board to direct the development and implementation of Board policies, rules, and regulations; monitor program results to ensure that they effectively support the RMWD's goals and objectives; and approve special studies, reports, and documents for submission to the Board with recommendations for policy determination for RMWD.
- The General Manager was delegated the authority by the RMWD Board to determine RMWD's annual budget and monitor expenditures; expend RMWD funds for non-emergency items specifically enumerated in the budget; determine when an emergency occurs and expend RMWD funds to meet the emergency; and meet with managers to ensure efficient and cost-effective operations.
- The General Manager was delegated the authority to establish RMWD positions and job descriptions; set compensation levels, and direct the activities of all RMWD employees; and retain and dismiss consultants for projects approved by the RMWD Board.

Applying the California common-law employment test, the most important factor in determining whether an individual performs services for another as employee is the right of the principal to control the manner and means of job performance and the desired result, whether or not this right is exercised. Where there is independent evidence that the principal has the right to control the manner and means of performing the service in question, CalPERS will determine that an employer-employee relationship exists between the employee and the principal.

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Other factors to be taken into consideration under the common-law employment test are as follows:

- Whether or not the one performing services is engaged in a distinct occupation or business;
- The kind of occupation, with reference to whether, in the locality, the work is usually done under the direction of a principal or by a specialist without supervision;
- The skill required in the particular occupation;
- Whether the principal or the individual performing the services supplies the instrumentalities, tools, and the place of work for the person doing the work;
- The length of time for which the services are to be performed;
- The method of payment, whether by the time or by the job;
- Whether or not the work is a part of the regular business of the principal;
- Whether or not the parties believe they are creating the relationship of employer-employee.

By applying common-law factors, OAS determined that the direction and control over the General Manager was fifty percent with the Agency. Therefore, the compensation reported for the General Manager should be limited to services performed under the Agency's direction and control. As such, this individual should be enrolled and reported to CalPERS by the Agency only for the time worked as an employee of the Agency for the period April 6, 2013 to April 5, 2014.

Government Code Section 20460 provides in relevant part that any public agency may participate in and make all or part of its employee's members of this system by contract. Government Code Section 20022 defines a contracting agency as any public agency that has elected to have all or any part of its employees become members of this system and that has contracted with the Board for that purpose.

Government Code 20028 defines an employee as any person in the employ of any contracting agency. Management and control of CalPERS is vested in the CalPERS Board as provided in Government Code Section 20120. Each member and each person retired is subject to the PERL and the rules adopted by the Board pursuant to Government Code Section 20122. Government Code Section 20125 provides that the Board shall determine who are employees and is the sole judge of the conditions under which persons may be admitted to and continue to receive benefits under this system. Government Code Section 20283 provides in pertinent part that any employer that fails to enroll an employee into membership when he or she becomes eligible, or within 90 days thereof, when the employer knows or can reasonably be expected to have known of that eligibility shall be required to pay all arrear costs for member contributions and administrative costs of five hundred dollars per member as a reimbursement to this system's current year budget.

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For the purposes of the PERL and for programs administered by the Board, the standard used for determining whether an individual is the employee of another entity is the California common law employment test as set forth in the California Supreme Court case titled *Tieberg v. Unemployment Ins. App. Bd.*, (1970) 2 Cal. 3d 943, which was cited with approval in *Metropolitan Water Dist. v. Superior Court (Cargill)*, (2004) 32 Cal. 4th 491, and which was adopted by the Board in two precedential decisions, *In the Matter of Lee Neidengard*, Precedential Decision No. 05-01, effective April 22, 2005, and *In the Matter of Galt Services Authority*, Precedential Decision No. 08-01, effective October 22, 2008.

Recommendation:

The Agency should ensure that compensation reported to CalPERS is limited to the remuneration paid out of the funds controlled by the Agency in payment for a member's services performed for the Agency.

The Agency should work with CalPERS Employer Account Management Division (EAMD) to identify and make adjustments, if necessary, to any impacted active and retired member accounts pursuant to Government Code Section 20160.

Criteria:

Government Codes: § 20022, § 20028, § 20030, § 20056, § 20065, § 20120, § 20121, § 20122, § 20125, § 20160, § 20281, § 20283, § 20460, § 20630, § 20636

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CONCLUSION

OAS limited this review to the areas specified in the scope section of this report and in the objectives outlined in Appendix A. OAS limited the test of transactions to employee samples selected from the Agency's payroll records. Sample testing procedures provide reasonable, but not absolute, assurance that these transactions complied with the California Government Code except as noted.

The findings and conclusions outlined in this report are based on information made available or otherwise obtained at the time this report was prepared. This report does not constitute a final determination in regard to the findings noted within the report. The appropriate CalPERS divisions will notify the Agency of the final determinations on the report findings and provide appeal rights, if applicable, at that time. All appeals must be made to the appropriate CalPERS division by filing a written appeal with CalPERS, in Sacramento, within 30 days of the date of the mailing of the determination letter, in accordance with Government Code Section 20134 and Sections 555-555.4, Title 2, of California Code of Regulations.

Respectfully submitted,

Original signed by Beliz Chappuie

BELIZ CHAPPUIE, CPA, MBA
Division Chief, Office of Audit Services

Staff: Cheryl Dietz, CPA, Assistant Division Chief
Alan Feblowitz, CFE, Senior Manager
Chris Wall, MBA, Senior Manager
Aileen Wong, MBA, Lead Auditor

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APPENDIX A

OBJECTIVES

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OBJECTIVES

The objectives of this review were to determine whether the Agency complied with:

- Applicable sections of the Government Code (Sections 20000 et seq.), PEPRA, and Title 2 of the CCR.
- Reporting and enrollment procedures prescribed in the Agency's retirement contract with CalPERS.

This review did not include an assessment as to whether the Agency is a "public agency," and expresses no opinion or finding with respect to whether the Agency is a public agency or whether its employees are employed by a public agency.

METHODOLOGY

To accomplish the review objectives, OAS interviewed key staff members to obtain an understanding of the Agency's personnel and payroll procedures, reviewed documents, and performed the following procedures.

- ✓ Reviewed:
 - Provisions of the contract and contract amendments between the Agency and CalPERS
 - Correspondence files maintained at CalPERS
 - Agency Board minutes and Agency Board resolutions
 - Agency written labor policies and agreements
 - Agency salary, wage and benefit agreements including applicable resolutions
 - Agency personnel records and employee hours worked records
 - Agency payroll information including Contribution Detail Transaction History reports
 - Other documents used to specify payrate, special compensation, and benefits for employees
 - Various other documents as necessary
- ✓ Reviewed Agency payroll records and compared the records to data reported to CalPERS to determine whether the Agency correctly reported compensation.
- ✓ Reviewed payrates reported to CalPERS and reconciled the payrates to Agency public salary records to determine whether base payrates reported were accurate, pursuant to publicly available pay schedules that identify the position title, payrate and time base for each position, and duly approved by the Agency's governing body in accordance with requirements of applicable public meetings laws.

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- ✓ Reviewed the Agency's affiliated entities to determine if the Agency shared employees with an affiliated entity and if the employees were CalPERS members and whether their earnings were reported by the Agency or by the affiliated entity.

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APPENDIX B

AGENCY'S WRITTEN RESPONSE



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October 7, 2016

VIA CERTIFIED MAIL AND E-MAIL BELIZ.CHAPPUIE@CALPERS.CA.GOV

Beliz Chappuie, Chief
Office of Audit Services
California Public Employees' Retirement System
P.O. Box 942707
Sacramento, CA 94229-2701

Re: Response by Fallbrook Public Utility District to September 6, 2016 Draft Audit Report

Dear Ms. Chappuie:

We submit the following on behalf of our client, Fallbrook Public Utility District ("District"). The District is in receipt of the Office of Audit Services' ("OAS") September 6, 2016 draft audit report ("Draft Report") related to the District's contract with the California Public Employees' Retirement System ("CalPERS"). Staff appreciates the efforts of OAS in performing its compliance review and the opportunity to comment on the Draft Report. Although our written response was initially due September 20, 2016, the District was graciously given an extension until October 7, 2016 to confer with legal counsel and provide this response. We thank you for granting us this additional time to prepare the District's response.

The Draft Report reflects a single finding regarding the agreement between the District and Rainbow MWD to share the services of a single General Manager ("Finding"). We understand the position taken by CalPERS and appreciate that the conclusion reached is reasonable in light of the facts that the determination was based on. As such, the District agrees with the Finding and will work with designated staff to make the necessary corrections. However, we request that due consideration be given to the fact that the agreement was of limited duration such that only half a year of service is implicated in this finding. We further request prompt resolution of this Finding since the GM at issue here may elect to retire in the very near future.



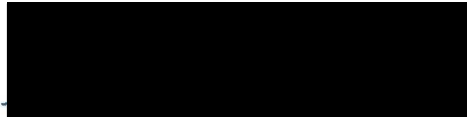
BEST BEST & KRIEGER
ATTORNEYS AT LAW

Belize Chappuie, Chief
October 7, 2016
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We thank you for the opportunity to submit this written response and look forward to working with OAS and CASD to ensure that the final recommendation and the implementation of said recommendation is appropriate.

Respectfully submitted,

Original signed by Isabel C. Safie



Isabel C. Safie
of BEST BEST & KRIEGER LLP

cc: Ace Rule (via e-mail)

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