

Robert E. Talton

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House of Representatives

RECEIVED

AUG 02 2004

OPINION COMMITTEE

July 29, 2004

RQ-0251-GA

The Honorable Greg Abbott
Texas Attorney General
P.O. Box 12548
Austin, Texas 78711-2548

FILE # ML-43860-04
I.D. # 43860

Dear General Abbott:

In March of this year, I received an e-mail from a constituent questioning the legality of an addendum to a contract of employment for a local superintendent of schools. Such contract seems to provide that the employee could convert accumulated vacation time to salary to be used as creditable compensation under the Texas Teacher Retirement System. By this letter, I request an opinion as to whether this portion of the contract is a violation of Government Code §822.201(c)(3) or any other section of the Government Code.

Enclosed please find a copy of the contract addendum and an opinion offered by a school district attorney.

Thank you for your attention to this matter.

Sincerely,

A handwritten signature in cursive script that reads "Robert E. Talton".

Robert E. Talton
State Representative

RET:ch
Enclosure



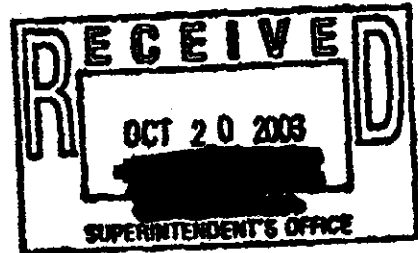
[REDACTED]

[REDACTED]

[REDACTED]

Board Certified Labor and Employment Law
Texas Board of Legal Specialization

October 17, 2003



Via Facsimile and Regular Mail
Ms. Becky Smith
Associate General Counsel
Texas Teacher Retirement System
1000 Red River Street
Austin, Texas 78701-2698

Re: 2003 Addendum to Employment Contract of [REDACTED]

Dear Becky:

As you know, this Firm represents the [REDACTED] Independent School District. Thank you for giving us the opportunity to address certain issues that have been raised with the Texas Teacher Retirement System regarding the 2003 Addendum to the Employment Contract of its Superintendent, [REDACTED], and, more specifically, the conversion of certain benefits to salary, as set forth in the Addendum, a copy of which is attached hereto.

Prior to addressing the legal issues involved, I would like to briefly comment on other aspects of the TRS role in this process. I recognize that TRS' interest in [REDACTED] 2003 Addendum was generated by a letter from a [REDACTED] citizen who was apparently complaining of the conversion of unused vacation leave and deferred compensation to salary, as provided in paragraphs V.(d) and V.(e) of the Addendum. While you have not identified the citizen to me, nor have you shared the letter with me, I must surmise that it is the same citizen, with the same opinions and allegations that have been published in numerous letters to the editor in the local newspaper and in correspondence to the [REDACTED] Board and school administrators. I also recognize, as you and I have discussed, that it would be inappropriate for TRS to address specific aspects of [REDACTED] employment, or his potential retirement benefits with third parties, such as this citizen, especially when his retirement is entirely hypothetical at this time. Any response that TRS makes to this citizen's letter to it must, therefore, be general in nature.

[REDACTED]

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Nevertheless, TRS should still recognize that this response will be relied upon and applied (or misapplied) to [REDACTED] situation, as well as, perhaps, the situations of other, similarly situated superintendents. This is, I suspect, a difficult balance to strike, and your assistance in this regard is appreciated.

Along these lines, I think it is first necessary to emphasize what this matter is *not* about. In letters to the editor and elsewhere, it has been alleged that [REDACTED] the [REDACTED] Board and the undersigned counsel for the School District had engaged in a conspiracy to defraud the TRS, through the conversion of benefits to salary in the 2003 Addendum. In making such an unfounded allegation, reliance has been erroneously placed on the penal provisions of Tex. Gov't Code § 821.101, "Conversion of Funds; Fraud," the lay interpretation of which seems to be that "conversion" of non-creditable compensation (*i.e.*, benefits) to creditable compensation (*i.e.*, salary) must be the type of "conversion" prohibited by this section of the TRS laws. As lawyers, we know that "conversion" in the criminal context is an entirely different matter, and that in this instance, the statute is referring to the theft of TRS contributions. At the local level, the shrillness of this controversy would be reduced substantially by clarifying that this is not about any criminal or other illegal act, or any wrongful conduct for that matter; it is simply about whether, upon retirement, certain compensation may or may not be considered creditable for purposes of computation of retirement benefits of the member involved.* Any statement to this effect from the TRS would be extremely helpful.

In discussing the gravamen of this matter with you, it appears that there is no disagreement with the conversion of deferred compensation to salary and, thus, creditable compensation, since the deferred compensation was for future years and had not yet been earned. Where questions have arisen, however, is with respect to the conversion of unused vacation days, and that is where I will now focus my attention.

Prior to the 2003 Addendum, [REDACTED] contract provided that he could accumulate no more than ten (10) vacation days per year, up to a maximum of forty (40) accumulated days, and that, upon mutual termination of his contract, he would be paid for such accumulated vacation days at his then current daily rate. Pursuant to paragraph V.(a) of the 2003 Addendum, the parties agreed to reduce and eliminate this benefit by increasing [REDACTED] salary by \$20,000.00 per year over the next two years and

* There is also more than a little irony in the citizen's suggestion that [REDACTED] the [REDACTED] Board and its counsel sought to "defraud" anyone. If anything, the 2003 Addendum is the epitome of disclosure, stating in detail what benefits were being converted to salary and how. We would likely not be in this controversy if such amounts had simply been placed in salary in the Addendum and nothing more was stated.

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placing limitations on his ability to cash out unused leave. Specifically, he could cash out accumulated vacation days only if his contract were mutually terminated prior to July 1, 2004, and he would be able to cash out only up to a maximum of twenty (20) days. Significantly, by agreeing to these terms, ██████████ placed his accumulated vacation days at risk (first twenty (20) days in 2003-2004, and then twenty (20) days in 2004-2005), since, as salary, the benefit was no longer vested and would be paid only for so long as he was employed by ██████████ – upon termination of his employment he would no longer be paid his salary, including the additional amount paid in lieu of vacation days.”

The first question that has arisen regarding the conversion of unused vacation to salary is whether such a conversion can occur at all. To that end, you have pointed to the list of items excluded from salary and wages, for TRS purposes, set forth in Tex. Gov't Code § 822.201(c) which, amongst ten other items, excludes “payments for unused vacation.” Standing alone, perhaps, without any contrary interpretation by the TRS, that statute may have had the effect of precluding the conversion of *any* of the items listed – including, for example, auto allowances – that are commonly converted into salary. The reason why auto allowances have commonly been converted to salary, and the reason, I would submit, that unused vacation can likewise be converted, is because the TRS, by rule, has permitted such conversion for approximately twenty years. Specifically, the TRS has long repeated the exclusions found in Tex. Gov't Code § 822.201(c), in 34 T.A.C. § 25.21(d), listing them as items “excluded from annual compensation.” Up to its

repeal in December 2001, a provision was also included in 34 T.A.C. § 25.21(e), stating that “[a]nnual compensation may be further limited by rule of the retirement system to prevent the conversion of noncreditable compensation to salary and wages in anticipation of retirement.” (Emphasis added.) Further, up to its repeal in December 2001, a rule limiting conversion was included as 34 T.A.C. § 25.30, “Conversion of Noncreditable Compensation to Salary.” This rule provided that any noncreditable compensation converted to salary within a given number of years prior to a member's retirement (most recently five) would be excluded from the member's annual compensation for purposes of calculating retirement benefits. See 34 T.A.C. § 25.30(a) (repealed December 2001). By repealing the longstanding rules limiting conversion in December 2001, the TRS created the inescapable legal conclusion that conversion of noncreditable compensation to salary could occur without limitation. Had these rules not

The same is true with respect to an earlier accrued “vacation bank” which was converted to salary of \$3,215 per year. By conversion to salary the bank was eliminated and the amount placed at risk, entirely subject to continued employment.

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been repealed, members such as [REDACTED] would not be engaging in any conversion process.*

Since there are no longer any restrictions on the ability to convert noncreditable compensation to creditable compensation, the questions TRS then poses appear to be (1) whether [REDACTED] unused vacation has actually been converted, and (2) whether it would constitute present compensation since the unused vacation has already been earned. I believe both questions can be answered with the same analysis, which is unique to the particular fact situation at hand.

In the typical situation, of course, unused vacation that is cashed out is paid in one lump sum, usually at the conclusion of one's employment, but sometimes on an annual basis. In this typical situation, no TRS contributions are made on the lump-sum payment, because the amount being paid is not actually salary, but rather the cash value of the benefit. This, in my view, is the payment for unused vacation contemplated to be excluded from salary in Tex. Gov't Code § 822.201(c)(3) and 34 T.A.C. § 25.21(d)(3). If

[REDACTED] unused vacation were to be paid in such a lump-sum fashion, or for that matter, over time, but with no risk (i.e., with a guarantee that the benefit would be paid out regardless of whether his employment continued), then the above questions would have to be answered in the negative. That, however, is not the case here. Instead, with mutual consideration, the parties have chosen to change the nature of the benefit to salary that can be earned only based on continued employment. Viewed from a different perspective, while [REDACTED] may have earned the forty days of unused vacation and the vacation bank for purposes of future payment, to be made upon mutual termination of employment at some later date, he did not earn it for purposes of current payout, while still employed, and in order to earn the additional salary, he must now remain employed. Since it is contingent on his continued employment, the benefit is in whole or in part at risk, and when paid in this fashion is as much salary as his other regular compensation that is earned and paid only if he continues to be employed.

Thus, in practical terms, if [REDACTED] were to leave the employ of [REDACTED] today he would be paid, in cash, for twenty days of accrued vacation (as opposed to the forty previously contracted for), and he would no longer receive any salary, including the amounts converted from twenty days of vacation and the vacation bank. If [REDACTED] were to leave the employ of the District during the 2004-2005 school year he would not

* The benefits booklet the TRS currently circulates and has posted on the web is dated September 2001 and still includes language based on the repealed rules. Unfortunately, this has helped to create a misconception in the public's mind regarding the permissibility of conversion. Similarly, it appears that TRS benefit coordinators may have given conflicting responses to third parties, versus members, inquiring about the permissibility of conversion....

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be entitled to payment for any accrued vacation, and he would no longer receive any salary, including the amounts converted from twenty days of vacation and the vacation bank. The payment for unused vacation leave, which would otherwise be noncreditable, has therefore been converted to salary, and, it must, therefore be deemed creditable compensation for TRS purposes.

Please note that the foregoing has been discussed with [redacted] personal attorney [redacted] and he is in agreement with this analysis. Recognizing the hypothetical nature of this fact situation (since we do not know when [redacted] may retire or what rules may be in place at that time), it is still our hope that, with this submission, you can assist in laying the controversy to rest, both in the context of a generalized response to citizen correspondence or a more specific communication directed to [redacted] and the [redacted] Board.

Thank you again for your patience and cooperation. Should you have any further questions, please feel free to call [redacted] or myself.

Very truly yours,

[redacted signature block]

DMF:car

cc: [redacted]

Enclosure

2003 ADDENDUM

**To
CONTRACT OF EMPLOYMENT OF**

[REDACTED]

THE STATE OF TEXAS

§
§
§

COUNTY OF HARRIS

THIS AGREEMENT is by and between the Board of trustees of the [REDACTED] Independent School District, a body politic and corporate of Harris County, Texas, herein called Employer, and [REDACTED] of Harris County, Texas, herein called Superintendent.

WITNESSETH:

WHEREAS, on April 21, 1993, a Contract of Employment (Contract) was entered into between the Employer and the Superintendent for the period of May 1, 1993 through April 30, 1996; and said Contract was amended each year thereafter to, amongst other things, extend the term of the Contract to June 30, 2007, as of July 1, 2002; and

WHEREAS, Section V of the Contract is deleted in its entirety and the following substitution in Lieu thereof, effective July 1, 2003:

V.

Compensation and Expenses

(a) Effective July 1, 2003, the base salary of the Superintendent shall be **TWO HUNDRED FORTY THOUSAND ANY) NO/100 DOLLARS (\$240,000.00) per annum**, which shall be payable in installments in accordance with practice followed for other professional employees. Extensions to the Contract, if any, salary increments, and fringe benefits granted during the Contract period shall be memorialized in the form of an Addendum to this Contract.

(b) The Superintendent shall receive the same insurance benefits and sick leave benefits as those provided other professional staff of the District on twelve month contracts.

(c) The Employer shall provide the Superintendent with a District credit card for his use in connection with expenses incurred while on District business and shall, on the Superintendent's behalf, pay dues to professional organizations that are appropriate for the position of Superintendent. The Employer shall also furnish the Superintendent with a computer and software for use in his residence, for District purposes.

(d) The Superintendent shall receive vacation at the rate of fifteen (15) working days per year for each year of employment. The accumulation of unused vacation days may not exceed ten (10) days per year, up to a maximum total of twenty (20) days of accumulated vacation days. In the event of mutual termination of this Contract prior to July 1, 2004, the Superintendent will be paid for such accumulated vacation days at the then current daily rate of pay in effect at the time the Contract is terminated. During the period of July 1, 2003 to June 30, 2004, the Superintendent shall be paid, as additional salary, for twenty (20) vacation days that he heretofore accumulated, at his current daily rate (totaling \$20,000.00), along with one-half of the value of his vacation bank established pursuant to Board Policy DED (totaling \$3,815.00). Further, during the period of July 1, 2004 to June 30, 2005, the Superintendent shall be paid, as additional salary and to the extent such days are available, for twenty (20) additional vacation days that he has heretofore accumulated, at his current daily rate (totaling \$20,000.00), along with the remaining one-half of the value of his vacation bank established pursuant to Board Policy DED (totaling \$3,815.00). The payment of the Superintendent's accumulated vacation days and vacation bank as salary shall be for all purposes, including creditable compensation under the Texas Teacher Retirement System.

(e) The Employer shall also establish for the Superintendent a deferred compensation plan under Internal Revenue Code Section 401(a). The terms of the 401(a) plan are set forth in a separate Adoption Agreement which shall be modified in accordance with the terms of this Section V(e), and as modified, are incorporated herein by reference. Said Plan shall fully vest upon the completion of four years thereunder (i.e., as of June 30, 2005), and the Employer shall be under no obligation to make any further contributions to the Plan beyond September 2002. Instead, the amount of \$15,000 per year shall be paid to the Superintendent as additional salary during the 2003-2004 and 2004-2005 school years, such amounts to be

considered salary for all purposes, including creditable compensation under the Texas Teacher Retirement System.

NOW, THEREFORE, this amendment to the Contract is effective pursuant to action by the Board of Trustees of the [REDACTED] Independent School District on May 27, 2003. Except as hereinabove amended, all other terms of the Contract, as set forth through the 2002 Addendum executed on June 25, 2002, shall remain in full force and effect.

EXECUTED IN DUPLICATE ON THIS THE 17 DAY OF June 2003.