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 U.S. DISTRICT COURT
 SOUTHERN DISTRICT OF CALIFORNIA

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10 UNITED STATES DISTRICT COURT
 11 SOUTHERN DISTRICT OF CALIFORNIA
 12

13 SECURITIES AND EXCHANGE
 14 COMMISSION,

15 Plaintiff,

16 vs.

17 THOMAS J. SAIZ, and CALDERON,
 18 JAHAM & OSBORN, an accountancy
 corporation,

19 Defendants.
 20

Case No.

COMPLAINT FOR
 VIOLATIONS OF THE
 FEDERAL SECURITIES
 LAWS

07 CV 2308 L JMA

21 Plaintiff Securities and Exchange Commission ("Commission") alleges as
 22 follows:

23 JURISDICTION AND VENUE

24 1. This Court has jurisdiction over this action pursuant to Sections 20(b),
 25 20(d)(1) and 22(a) of the Securities Act of 1933 ("Securities Act"), 15 U.S.C.
 26 §§ 77t(b), 77t(d)(1) & 77v(a), and Sections 21(d)(1), 21(d)(3)(A), 21(e) and 27 of
 27 the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. §§ 78(u)(d)(1),
 28 78u(d)(3)(A), 78u(e) & 78aa. Defendants have, directly or indirectly, made use of

1 the means or instrumentalities of interstate commerce, of the mails, or of the
2 facilities of a national securities exchange in connection with the transactions, acts,
3 practices and courses of business alleged in this Complaint.

4 2. Venue is proper in this district pursuant to Section 22(a) of the
5 Securities Act, 15 U.S.C. § 77v(a), and Section 27 of the Exchange Act, 15 U.S.C.
6 § 78aa, because certain of the transactions, acts, practices and courses of conduct
7 constituting violations of the federal securities laws occurred within this district,
8 and the Defendants reside and/or are located in this district.

9 **SUMMARY**

10 3. This case involves false and misleading statements by Defendants
11 Thomas J. Saiz, a certified public accountant, and his accountancy corporation,
12 Calderon, Jaham & Osborn in connection with municipal securities offerings by
13 the City of San Diego (the "City"). Defendants were the independent auditor for
14 the City for fiscal years ended June 30, 2001 and 2002. In that capacity,
15 Defendants drafted the footnote disclosures to the City's financial statements;
16 issued unqualified audit reports for these fiscal years stating that the City's
17 financial statements were presented in conformity with generally accepted
18 accounting principles ("GAAP") and that the audits were performed in accordance
19 with generally accepted auditing standards ("GAAS"); and consented to the City
20 including the audit reports in the offering documents for its five 2002 and 2003
21 municipal securities offerings that raised approximately \$261 million from
22 investors. Defendants violated the antifraud provisions of the Securities Act and
23 Exchange Act because:

24 (a) their footnote disclosures to the financial statements, which
25 were included in the City's offering documents, contained materially false and
26 misleading statements regarding the City's funding of its pension and retiree health
27 care obligations; and

28 (b) their audit reports were false and misleading because the City's

1 pension and retiree health care obligations were not presented in conformity with
2 GAAP and Defendants' audits of those obligations were not performed in
3 accordance with GAAS.

4 DEFENDANTS

5 4. Thomas J. Saiz ("Saiz") is a resident of El Cajon, California. He is a
6 certified public accountant licensed with the State of California since 1992. He
7 joined Calderon, Jaham & Osborn in 1989, became a shareholder in 1996, and
8 became its sole shareholder in 2000.

9 5. Calderon, Jaham & Osborn ("CJO"), an accountancy corporation, is
10 an active California corporation with a registered office in La Mesa, California. It
11 is licensed with the California Board of Accountancy. During 2001 and 2002, CJO
12 had approximately 30 employees.

13 RELATED PARTIES

14 6. The City of San Diego, California, is a California municipal
15 corporation with all municipal powers authorized by the California Constitution
16 and laws, including the power to issue debt. The City is the seventh most populous
17 city in the country, with approximately 1.3 million residents. CJO performed
18 annual audits of the City financial statements for fiscal years ended June 30, 2001
19 and 2002. For these years, respectively, the City had total revenues of \$1.2 billion
20 and \$2 billion and total assets of \$15 billion and \$10 billion.

21 7. San Diego City Employees' Retirement System ("CERS") is a
22 multiple-employer, defined benefit plan established by the City to provide
23 retirement benefits to its members, i.e., City employees and their beneficiaries.
24 CJO performed audits of CERS's financial statements for fiscal years ended June
25 30, 2001 and 2002. For these years, CERS had net assets of \$2.5 billion.
26 Additionally, it had, respectively, revenues of \$110 million and \$86 million in
27 fiscal years ended June 30, 2001 and 2002.

28 ///

Fiscal Year ending	Funded Ratio	Unfunded Liability	Net Pension Obligation
6/30/00	97.3%	\$69 million	\$23.05
6/30/01	89.9%	\$284 million	\$30.98 million
6/30/02	77.3%	\$720 million	\$39.23 million
6/30/09 projected	65.6%	\$2 billion	\$446 million

11. The City conducted its own analysis in mid-2003, which yielded similar projections.

12. This fall in CERS's funded ratio and the increase in the City's unfunded liability and net pension obligation was the result of many factors, including:

(a) CERS twice agreed to permit the city to underfund its annual contributions to CERS, as further alleged below;

(b) The City used surplus earnings to pay additional pension and other non-pension benefits to on behalf of CERS's members, as further alleged below; and

(c) CERS suffered substantial investment losses in fiscal years 2001 and 2002 -- \$193.2 million in fiscal year 2001 and \$364.8 million in fiscal year 2002.

1. **CERS Agrees To Two Proposals By The City Permitting The City To Underfund Its Annual CERS Contributions**

a. **CERS Agrees To The City's Proposal In 1997 To Underfund Its Pension Obligations—"Manager's Proposal 1"**

13. In fiscal year 1996, the City agreed to increase significantly and retroactively all employees' pension benefits. Because the City could not afford to fund the cost of the benefit increases, it made them contingent on CERS's

1 agreement to the City's underfunding of its annual contribution to CERS.

2 14. In fiscal year 1997, the City and CERS entered into an agreement,
3 referred to as Manager's Proposal 1, that allowed the City to intentionally
4 underfund its annual liability to CERS in fiscal years 1997 through 2006. This
5 funding method was not approved by GASB. Manager's Proposal 1 also required
6 that if CERS's funded ratio fell below 82.3%, the City would have to increase its
7 CERS contribution.

8 15. As part of Manager's Proposal 1, CERS, at the City's request,
9 recorded \$39.2 million from the surplus earnings as a net pension obligation
10 "reserve" or "NPO Reserve." The amount represented the difference between what
11 the City would have contributed under a GASB-accepted funding rate and what the
12 City actually contributed under Managers Proposal 1. The NPO reserve, despite its
13 name, was not a true reserve. Therefore, the creation of this "reserve" entry had no
14 effect on CERS's funded ratio or the City's unfunded liability to CERS.

15
16 **b. CERS Agrees To The City's Proposal In 2002 To Extend**
17 **The Time It Would Underfund Its Pension Obligations—**
18 **"Manager's Proposal 2"**

19 16. In the second half of fiscal year 2002, the City agreed to again
20 increase pension benefits for fiscal year 2003. From as early as October 2001,
21 however, the City was aware that CERS's funded ratio would likely fall below the
22 82.3% floor established by Manager's Proposal 1, which would require the City to
23 increase its annual fiscal year 2004 contribution to CERS by at least \$25 million.
24 The actuarial reports as of February 2002 also confirmed this downward trend in
25 the funded ratio.

26 17. Concerned about likely having to pay the additional amount, the City
27 conditioned the pension benefit increases on the City's obtaining from CERS relief
28 from the floor of Manager's Proposal 1. In November 2002, the City and CERS

1 agreed to Manager's Proposal 2, which provided that once CERS's funded ratio
2 fell below the 82.3% required by Manager's Proposal 1, the City would have five
3 years to increase its CERS contributions to reach a GASB-accepted funding rate.
4 Manager's Proposal 2 thus effectively allowed the City an additional five years to
5 underfund its annual CERS contribution.

6 **2. The City Used Surplus Earnings For Non-Pension Purposes**

7 18. For the purpose of the annual actuarial calculations, the CERS actuary
8 assumed a projected 8% rate of return. Any actual earnings above 8% were
9 considered to be surplus earnings to be used in years in which the earnings fell
10 below the assumed return rate.

11 19. Since the early 1980s, the City used CERS's surplus earnings to fund
12 an ever-increasing amount of additional non-pension benefits for CERS members
13 including, but not limited to, paying retiree health care benefits and funding certain
14 portions of the employee pension contributions.

15 20. In total, the City used surplus earnings of \$150 million as of the end
16 of fiscal year 2001 and an additional \$25 million as of the end of fiscal year 2002
17 primarily to fund non-pension benefits for CERS members. From fiscal years
18 1997 through 2003, this use by the City of surplus earnings accounted for 17% of
19 the increase in the City's unfunded liability to CERS.

20 **B. The City's 2002 and 2003 Municipal Securities Offerings**

21 21. In 2002 and 2003, the City conducted five municipal securities
22 offerings totaling \$261,850,000 in par value. These offerings were entitled:

- 23 • \$25,070,000 Public Facilities Financing Authority of the City of San
24 Diego Lease Revenue Bonds, Series 2002B (Fire and Safety Project)
25 (June 2002);
- 26 • \$93,200,000 City of San Diego, 2002-03 Tax Anticipation Notes
27 Series A (July 2002);
- 28 • \$15,255,000 City of San Diego/Metropolitan Transit Development

1 Board Authority 2003 Lease Revenue Refunding Bonds (San Diego
2 Old Town Light Rail Transit Extension Refunding) (April 2003);
3 • \$17,425,000 City of San Diego 2003 Certificates of Participation
4 (1993 Balboa Park/Mission Bay Park Refunding) (May 2003);
5 • \$110,900,000 City of San Diego 2003-04 Tax Anticipation Notes
6 Series A (July 2003).

7 22. For each of the offerings, the City issued offering documents that
8 purported to disclose the material information regarding the offering and the City.
9 The offering documents included the City's fiscal year 2001 and 2002 financial
10 statements. Saiz and CJO's role in these offerings was twofold. First, as further
11 alleged below, Saiz drafted the footnote disclosures to the City's financial
12 statements, which draft disclosures were subject to review and approval by the
13 City. Second, as further alleged, Saiz and CJO consented to the inclusion in the
14 offering documents of CJO's unqualified fiscal year 2001 and 2002 audit reports
15 on the City's financial statements.

16
17 **C. Saiz And CJO Draft False And Misleading Footnotes To The City's**
18 **Financial Statements**

19 23. Saiz drafted footnote disclosures for the City's fiscal year 2001 and
20 2002 financial statements, which were subject to the review and approval of the
21 City, that included false and misleading information regarding the City's funding
22 of CERS, the City's NPO, and the City's retiree health care obligations. These
23 false and misleading statements were included in the City's offering documents for
24 its 2002 and 2003 municipal securities offerings.

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28 ///

1 **1. Saiz Drafts False And Misleading Financial Statement Footnotes**
2 **Regarding The City's Funding Of CERS**

3 24. Saiz drafted footnote disclosures for the City's financial statements
4 that included the following false and misleading information regarding the City's
5 funding of CERS:

6 (a) The 2002 financial statement footnotes falsely stated that the
7 City's method for funding CERS included "a provision to assure the funding level
8 of [CERS] would not drop below a level [CERS's actuary] deem[ed] reasonable to
9 protect the financial integrity of [CERS]." In fact, this statement was false and
10 misleading in that CERS's funded ratio at the end of fiscal year 2002 was 77.3%,
11 which was less than the 82.3% that the CERS actuary deemed reasonable. Further,
12 the footnote failed to disclose that (i) Manager's Proposal 1 had established a
13 trigger level of 82.3% for the funded ratio; (ii) by the latter half of fiscal year 2002,
14 the City was aware that CERS funded ratio would likely fall below this trigger
15 level; and (iii) if Manager's Proposal 2 were not approved, the City would have
16 had to make a large additional payment to CERS.

17 (b) The 2002 financial statement footnotes also falsely stated that
18 CERS's actuary believed that the City's funding method was an excellent method
19 for the City and was superior to certain GASB-accepted funding methods. In fact,
20 this statement was false and misleading in that the actuary ceased to have this view
21 once CERS's funded ratio fell below 82.3%.

22 (c) The 2001 financial statement footnotes also falsely stated that
23 CERS's actuary "is in the process of requesting the GASB to adopt the [City's]
24 funding method as an approved expending method which would eliminate any
25 reported NPO." In fact, although the CERS actuary had initiated communication
26 with GASB, GASB had never responded.

27 25. As required by GAAS, Saiz read the information in the City's 2003
28 offering documents and learned that in fiscal year 2002, CERS's funding ratio had

1 fallen from 89.9% to 77.3% and that the City's unfunded liability to CERS had
2 increased from \$284 million to \$720 million. Despite this substantial negative
3 change, Saiz flagged these issues for the 2003 audit but did not conduct any
4 inquiry into the facts or determine whether the 2002 financial statement footnotes
5 needed to be revised. Had Saiz inquired, he would have learned that in fiscal year
6 2002, the City was aware that CERS's funding ratio would likely fall below the
7 82.3% trigger level and the City had proposed Manager's Proposal 2 to avoid the
8 City being required to make a large additional payment to CERS, and that in early
9 fiscal year 2003, the City and CERS had agreed to Manager's Proposal 2, which
10 extended the time for the City to underfund CERS and increased the amount by
11 which the City could underfund CERS.

12 26. Saiz also never inquired of CERS's actuary whether the statements in
13 the offering documents' financial statement footnotes regarding the actuary's
14 opinions and actions were true. Had Saiz inquired, he would have learned that the
15 actuary did not support the City's funding method after CERS's funded ratio fell
16 below 82.3% and that as of the 2001 audit, GASB had never responded to the
17 actuary's request to approve the City's funding method.

18
19 **2. Saiz Drafts False And Misleading Footnotes Regarding the City's**
20 **NPO**

21 27. Saiz drafted footnote disclosures for the City's financial statements
22 that included the following false and misleading information regarding the City's
23 net pension obligation, or NPO:

24 (a) The City's 2002 financial statements reported that the City's
25 NPO was \$39.2 million as of the end of fiscal year 2001, but failed to disclose that
26 at the time of the 2003 offerings, the City had already calculated that its NPO for
27 fiscal year 2003 would be \$51.9 million; and
28

1 (b) The City's 2001 and 2002 financial statements reported that the
2 NPO was "funded in a reserve," when, in fact, there was no such reserve.

3 28. Saiz read the information in the City's 2003 offering documents and
4 learned that in fiscal year 2002, CERS's funding ratio had fallen from 89.9% to
5 77.3% and that the City's unfunded liability to CERS had increased from \$284
6 million to \$720 million. Despite this substantial negative change, and although
7 Saiz flagged these issues for the 2003 audit, he did not conduct any inquiry into the
8 facts or determine whether the financial statement footnotes needed to be revised.
9 Had Saiz inquired, he would have learned that prior to the 2003 offerings, the City
10 had already calculated that its NPO for fiscal year 2003 had grown from \$39.2
11 million to \$51.9 million.

12 29. Saiz signed the unqualified audit reports without understanding the
13 meaning of his statement that the NPO was "funded in a reserve." As both the
14 City's and CERS's auditor, Saiz had access to all of their records and personnel.
15 Saiz, however, did nothing during the audits to understand the statement or to
16 ensure its accuracy. Had he done so, he would have discovered that the NPO
17 "reserve" was not, in fact, a reserve.

18
19 **3. Saiz Drafts Misleading Financial Statement Disclosures**
20 **Regarding the City's Retiree Health Care Obligation**

21 30. Saiz drafted footnote disclosures for the City's financial statements
22 regarding the City's retiree health care obligations, which stated that the City
23 provided such benefits to certain retirees at a cost of \$7.2 million in fiscal year
24 2001 and \$8.9 million in fiscal year 2002 and that "expenses for [such retiree
25 health care benefits] are recognized as they are paid." This statement was
26 misleading because there was no disclosure that the retiree health care expense was
27 being paid with surplus earnings from CERS; that this surplus earnings reserve was
28 running out of money; and that the City would have to begin paying this

1 substantial expense out of its own budget.

2 31. As auditor for both the City and CERS, Saiz knew in 2001 that CERS
3 was paying for this expense with surplus earnings. Nevertheless, he failed to
4 disclose this critical information in the 2001 and 2002 financial statements.

5 **D. Saiz Signs False Audit Reports**

6 32. For fiscal years ended June 30, 2001 and 2002, CJO issued
7 unqualified audit reports on the City's financial statements stating that the City's
8 financial statements were fairly presented in conformity with GAAP and that the
9 audits were performed in accordance with GAAS. Saiz signed the unqualified
10 audit reports on behalf of CJO.

11 33. Saiz and CJO consented to allow the City to include CJO's audit
12 reports in the City's offering documents for its 2002 and 2003 municipal securities
13 offerings. As further alleged below, Saiz and CJO's audit reports were false in that
14 the City's financial reports were not fairly presented in conformity with GAAP and
15 their audits were not conducted in accordance with GAAS.

16 34. For the City's financial statements to be presented fairly in conformity
17 with GAAP, the City was required to account, and provide footnote disclosure, for
18 its pension in accordance with GASB Statement 27, "Accounting for Pensions by
19 State and Local Governmental Employers." GASB Statement 27 requires
20 disclosure of an employer's policy for funding its pension plan; its NPO; and
21 factors that significantly affect the identification of trends in the amounts of the
22 plan's funded ratio or the employer's unfunded liability to its plan. As alleged
23 above, the City's financial statements contained false and misleading information
24 regarding the City's funding method for CERS and its NPO and were not presented
25 in accordance with GAAP.

26 35. GAAS requires that the audit be performed by a person or persons
27 having adequate technical training and proficiency as an auditor and the auditor
28 with final responsibility for the engagement should know, at a minimum, the

1 relevant professional accounting and auditing standards and should be
2 knowledgeable about the client. AICPA Codification of Auditing Standards, AU
3 §§ 210.01 & 230.06. As alleged above, Saiz failed to have sufficient proficiency
4 as an auditor in that he did not understand what “funded in a reserve meant” and
5 was not knowledgeable about his client in that he did not know that the City and
6 CERS had agreed to Manager’s Proposal 2.

7 36. Under GAAS, by issuing an unqualified audit report, Saiz opined that
8 the footnote disclosures in the financial statements were reasonably adequate.
9 AICPA Codification of Auditing Standards, AU § 431.01. For this purpose,
10 GAAS required Saiz to, among other things (a) obtain sufficient competent
11 evidential matter through inspection, observation, inquiries, and confirmations to
12 afford a reasonable basis for such audit report; and (b) exercise due professional
13 care in performing the audit, including exercising professional skepticism in
14 performing audit procedures and gathering and analyzing audit evidence. As
15 alleged above, with respect to the footnote disclosures, Saiz failed to obtain
16 sufficient competent evidential matter and to exercise due professional care.

17 37. GAAS additionally imposes certain requirements on auditors when
18 they consent to their audit opinions being included in a securities offering
19 document. Specifically, GAAS requires the auditor to read the information in the
20 offering document and determine whether such information, or the manner of its
21 presentation, is materially inconsistent with information, or the manner of its
22 presentation, appearing in the financial statements. AICPA Audit & Accounting
23 Guide, “Audits of State and Local Governments” §16.07. Upon concluding that
24 that there is a material inconsistency, the auditor should determine whether the
25 financial statements, the audit report, or both require revision. AICPA
26 Codification of Auditing Standards, AU § 550.04. As alleged above, in 2003,
27 upon learning of the substantial negative change in CERS’s funded liability and the
28 City’s unfunded liability, Saiz failed to inquire into such matters or to determine

1 whether the financial statements, audit report, or both required revision.

2
3 **E. The City's Voluntary Disclosure Results In The Lowering Of The**
4 **Rating On The City's Bonds**

5 38. The City eventually filed a Voluntary Report of Information on
6 January 27, 2004, which disclosed information regarding CERS's current and
7 estimated future funded status; the City's current and estimated future liabilities to
8 CERS; the reasons for the substantial decrease in CERS's funded ratio and
9 increase in the City's liability to CERS; and the City's previous use of CERS funds
10 to pay for retiree health care and the City's estimated future liabilities for retiree
11 health care.

12 39. Shortly after the disclosures in the Voluntary Report, the rating
13 agencies lowered their ratings on the City's bonds.

14
15 **FIRST CLAIM FOR RELIEF**
16 **FRAUD IN THE OFFER OR SALE OF SECURITIES**
17 **Violations Of Section 17(a) Of The Securities Act**

18 40. The Commission realleges and incorporates by reference paragraphs 1
19 through 38 above.

20 41. Defendants Saiz and CJO, and each of them, by engaging in the
21 conduct described above, in the offer or sale of securities by the use of means or
22 instruments of transportation or communication in interstate commerce or by use
23 of the mails directly or indirectly:

- 24 a. with scienter, employed devices, schemes, or artifices to
25 defraud;
26 b. obtained money or property by means of untrue statements of
27 a material fact or by omitting to state a material fact necessary
28 in order to make the statements made, in light of the
circumstances under which they were made, not misleading;

1 or

2 c. engaged in transactions, practices, or courses of business
3 which operated or would operate as a fraud or deceit upon the
4 purchaser.

5 42. By engaging in the conduct described above, Defendants Saiz and
6 CJO violated, and unless restrained and enjoined will continue to violate, Section
7 17(a) of the Securities Act, 15 U.S.C. § 77q(a).

8
9
10 **SECOND CLAIM FOR RELIEF**
11 **FRAUD IN CONNECTION WITH THE PURCHASE OR SALE OF**
12 **SECURITIES**
13 **Violations Of Section 10(b) Of The Exchange Act And Rule 10b-5 Thereunder**

14 43. The Commission realleges and incorporates by reference paragraphs 1
15 through 38 above.

16 44. Defendants Saiz and CJO, and each of them, by engaging in the
17 conduct described above, directly or indirectly, in connection with the purchase or
18 sale of a security, by the use of means or instrumentalities of interstate commerce,
19 of the mails, or of the facilities of a national securities exchange, with scienter:

- 20 a. employed devices, schemes, or artifices to defraud;
- 21 b. made untrue statements of a material fact or omitted to state a
22 material fact necessary in order to make the statements made,
23 in the light of the circumstances under which they were made,
24 not misleading; or
- 25 c. engaged in acts, practices, or courses of business which
26 operated or would operate as a fraud or deceit upon other
27 persons.

28 45. By engaging in the conduct described above, Defendants Saiz and
CJO violated, and unless restrained and enjoined will continue to violate, Section

1 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17
2 C.F.R. § 240.10b-5.

3 **PRAYER FOR RELIEF**

4 WHEREFORE, the Commission respectfully requests that the Court:

5 **I.**

6 Issue findings of fact and conclusions of law that defendants Saiz and CJO
7 committed the alleged violations.

8 **II.**

9 Issue judgments, in a form consistent with Fed. R. Civ. P. 65(d),
10 permanently enjoining each of the defendants and their officers, agents, servants,
11 employees, and attorneys, and those persons in active concert or participation with
12 any of them, who receive actual notice of the judgment by personal service or
13 otherwise, and each of them, from violating Section 17(a) of the Securities Act, 15
14 U.S.C. § 77q(a), and Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and
15 Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5.

16 **III.**

17 Order defendant Saiz to pay a civil penalty under Section 20(d) of the
18 Securities Act, 15 U.S.C. § 77t(d), and Section 21(d)(3) of the Exchange Act, 15
19 U.S.C. § 78u(d)(3).

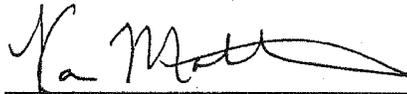
20 **IV.**

21 Retain jurisdiction of this action in accordance with the principles of equity
22 and the Federal Rules of Civil Procedure in order to implement and carry out the
23 terms of all orders and decrees that may be entered, or to entertain any suitable
24 application or motion for additional relief within the jurisdiction of this Court.

V.

Grant such other and further relief as this Court may determine to be just and necessary.

DATED: December 10, 2007



KAREN MATTESON
Attorney for Plaintiff
Securities and Exchange Commission

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