

Deferred Compensation Plan BOARD REPORT 16-09

Date: February 4, 2016

To: Board of Deferred Compensation Administration

From: Staff

Subject: Deferred Compensation Plan: Proposed 2016
Budget and Budget Status Report

Board of Deferred
Compensation Administration

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Recommendation:

That the Board of Deferred Compensation:

- (a) Approve reimbursements from the Deferred Compensation Plan Reserve Fund accounts to the Personnel Department for \$389,068 and City Attorney for \$221,865 for the quarters ending 03/31/15 through 12/31/15 and incorporating all prior year adjustments to indirect cost calculations; and
- (b) Adopt the proposed Deferred Compensation Plan budget for plan year 2016.

Discussion:

At the Board's January 19, 2016, meeting, the Board approved a staff recommendation to change the methodology used in calculating the Deferred Compensation Plan's indirect salary costs to provide for greater consistency and transparency. Specifically, the Board approved replacement of City Controller-calculated Cost Allocation Plan ("CAP") rates (which are intended to be used for indirect cost calculations for Federal grant funded programs) with the following City Controller-calculated Special Rates: (a) the Personnel Department Special "Balance of Department – Support Services" rate and (b) the City Attorney Special "Municipal Counsel & Legislative Services" rate. The Board approved retroactively adjusting reimbursements beginning Fiscal Year 2007/2008 and continuing ongoing.

Taking this action was an important prerequisite for:

- (a) Identifying the necessary adjustments for previously adopted reimbursements from 2007 through the Board's last adopted reimbursement for the quarter ending 12/31/14;
- (b) Calculating the salary (direct and indirect) reimbursements due for the quarters ending 03/31/15 through 12/31/15; and
- (c) Creating a proposed Plan budget for Plan Year 2016.

This report will provide information and, where required, recommend actions related to each of these three items.

(A) Adjustments: 2007-2014

As noted last month in Board Report 16-03, the City Administrative Code provides that the City's internal costs of administration be paid by participant fees. Staffing costs are one significant component of those costs. With respect to direct and indirect staffing costs, the Plan's methodology for determining how they should be calculated has evolved over the history of the Plan. Since 2007 the published CAP "Grant Funded Special Programs," Rate has been used to calculate indirect cost reimbursements. Staff identified a number of inconsistencies and a lack of transparency regarding those historical calculations, and recommended a change to the Special "Balance of Department – Support Services" Rate for the following reasons:

- (1) The Deferred Compensation Plan is not a Federal grant-funded program and there is no requirement that it be treated as such for the purposes of calculating indirect costs.
- (2) Staff could identify no compelling reason for Deferred Compensation Plan staff to utilize a different rate than that applied to other similar Employee Benefits Division staff working on similar programs in the same Division and workspace.
- (3) There have been inconsistencies and wide fluctuations in the calculation of the CAP "Grant Funded Special Programs" Rate due to changing methodologies, and the application of a much smaller salary base to the calculation of indirect costs, that cause its consistency and reliability to be suspect.

Staff also compared application of the CAP Rate vs. Special Rate relative to the City Attorney staff supporting the Plan. Staff noted that in the past the Plan had utilized the CAP "Direct Billed – in City Space" Rate but that, as with the Personnel Department calculation, the more applicable and appropriate rate would be to use the Special Rate, "Municipal Counsel & Legislative Services." The basis for this was similar to that for the Personnel Department in that the City's Plan is not Federal grant funded. In addition, staff noted that there was no indication that the City Attorney salary base for the Deferred Compensation Plan was being used exclusively or at all in the calculation of the "Direct Billed" rate, and that the Municipal Counsel & Legislative Services Rate category appeared most directly related and appropriate. The City Attorney's Office concurred with this assessment.

Based on these findings, the Board approved staff's recommendation to direct staff to use the Personnel Department's Special "Balance of Department – Support Services" Rate and the City Attorney Special "Municipal Counsel & Legislative Services" Rate for future calculations of Plan staffing indirect costs, and to retroactively adjust reimbursements for prior fiscal years dating back to Fiscal Year 2007/2008.

Staff's first step was to apply the adopted Support Services Cost Allocation Plan (CAP) rate retroactively as detailed in **Attachment A**. This resulted in a net adjustment to the Personnel Department's indirect costs in the amount of \$487,210 to the City Attorney's indirect costs in the amount of (\$21,703), for a net adjustment of **\$465,506.79** through 12/31/14.

(B) Quarterly Reimbursements: 03/31/15 through 12/31/15

In **Attachment B**, staff has calculated the outstanding quarterly reimbursement amounts for the quarters ending 03/31/15 through 12/31/15. Since the adopted reimbursement amounts for the quarter ending 9/30/14 and 12/31/14 were never transferred, the accounting takes those quarter's original calculations as a starting point and applies the adjustments going forward over each successive quarter. Cumulatively, the net amounts owed for indirect costs for Personnel Department and City Attorney staff through 12/31/15 are **\$389,068** and **\$221,865**, respectively.

(C) Plan Budget: 2016

The Board's Deferred Compensation Plan Governance Policies and Bylaws/Fiscal Administration Policy, Section 5.2, provides that:

"At the beginning of each calendar year staff will present, for adoption by the Board, a recommended budget for the Trust Fund for that Plan Year. The Board, in structuring this budget, will maintain a long-term balance between revenues and expenditures that is consistent with avoiding volatility in the collection of participant fees. In furtherance of that objective, the Board shall maintain a prudent reserve in the Trust Fund to protect against fluctuations in Plan assets. The Board's Plan Year budgets shall be consistent with ongoing 5-year revenue/expense reviews as described in Section 5.1."

Staff is recommending that the Board adopt staff's proposed budget for the Plan's 2016 calendar year as included in **Attachment C**. This attachment also includes a narrative description of the assumptions and other relevant factors regarding each budgetary item.

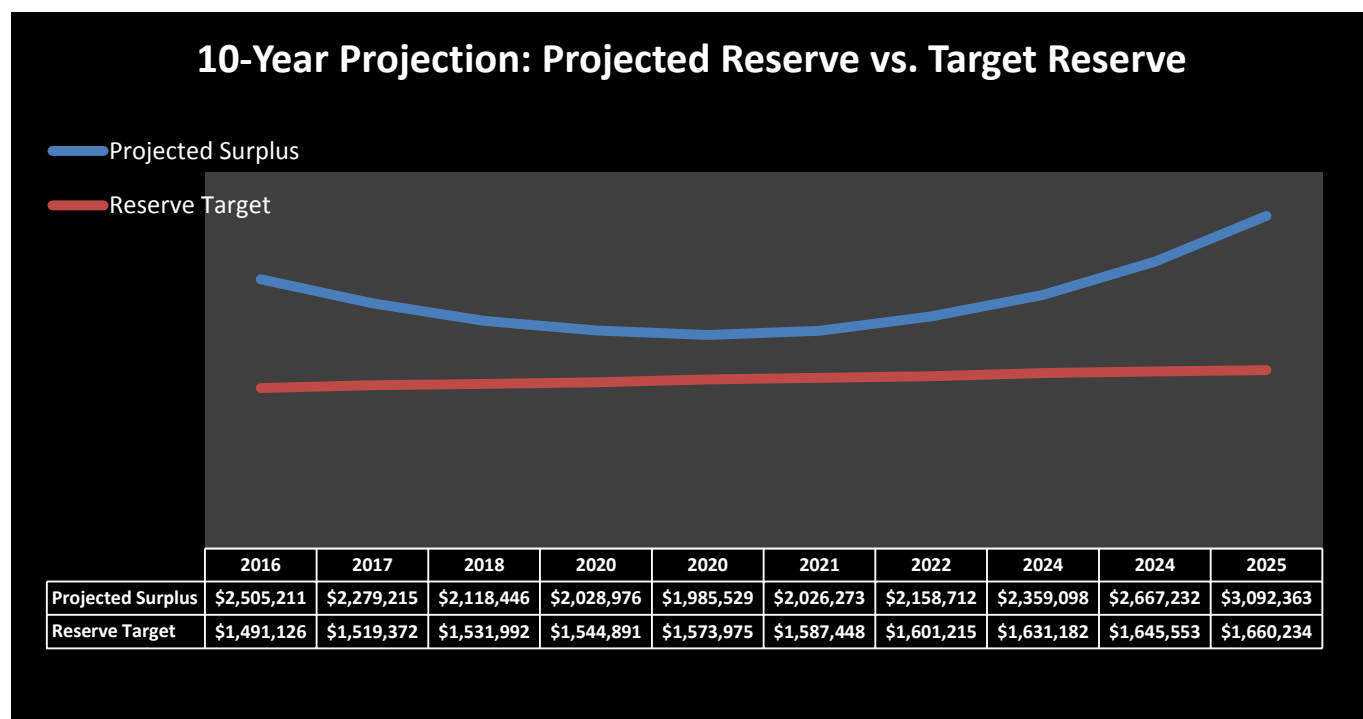
The annual budget supplements the quarterly reconciliations of the Plan's fee revenues and internal administrative expenses. In addition, the annual budget reflects the unique circumstances of the upcoming one-year time period, as opposed to the more generalized ten-year forecasts that are incorporated in the quarterly reconciliations.

As the Board is aware, annual budgets may incorporate some level of an assumed deficit as the Plan's long-term surplus is calibrated to be in alignment with the long-term targeted reserve. The projected **annual** operating deficit for 2016 is estimated to be approximately \$254,392.

The Board last reviewed its long-term assumptions for Plan revenues/expenditures at its November 2013 Strategic Plan review. Pursuant to that review, the projected targeted reserve amount for the Plan's reserve fund is one-half of Plan annual operating expenses.

In 2016, one half of the annual operating expenses is approximately \$1.5 million. The estimated surplus in the Trust Fund by the end of 2016 is expected to be \$2.5 million, or \$1 million more than the targeted reserve mount.

In addition, staff has calculated the projected surplus relative to the targeted reserve amount over a ten-year period. As a result of growth in Plan assets and adjustments to indirect cost assumptions, the surplus is projected to be significantly above the target reserve over the entire period. The lowest projected amount above the target reserve is \$412,000 in 2020, increasing to \$1.4 million above target in 2025. Staff will address the topic of these surplus Plan resources in its presentation in connection with Board Report 16-08.



Submitted by: _____
Alexandra Castillo

Approved by: _____
Steven Montagna

Attachment A

FY	Quarter Ending	PRIOR CAP METHODOLOGY USING PUBLISHED RATE				NEW CAP METHODOLOGY USING SPECIAL RATE				REIMBURSEMENT DIFFERENCE	
		Total Personnel Amount Reimbursed under Published CAP Rate	Applied CAP Rate	Total City Attorney Amount Reimbursed under Published CAP Rate	Applied CAP Rate	Total Personnel Amount Reimbursed under Special CAP Rate	Special Rate	Total City Attorney Amount Reimbursed under Special CAP Rate	Special Rate	Difference Personnel	Difference City Attorney
07-08	9/30/2007	\$119,970	78.22%	\$23,922	52.63%	\$120,024	78.30%	\$24,593	56.91%	(\$54)	(\$671)
	12/31/2007	\$109,350	78.22%	\$23,922	52.63%	\$109,399	78.30%	\$24,593	56.91%	(\$49)	(\$671)
	3/31/2008	\$125,302	78.22%	\$26,191	52.63%	\$125,358	78.30%	\$26,925	56.91%	(\$56)	(\$734)
	6/30/2008	\$104,052	78.22%	\$22,578	52.63%	\$104,098	78.30%	\$23,211	56.91%	(\$47)	(\$633)
08-09	9/30/2008	\$158,770	88.53%	\$25,286	43.23%	\$149,852	77.94%	\$27,886	57.96%	\$8,918	(\$2,600)
	12/31/2008	\$154,904	88.53%	\$19,880	43.23%	\$146,203	77.94%	\$21,924	57.96%	\$8,701	(\$2,044)
	3/31/2009	\$141,132	88.53%	\$19,214	43.23%	\$133,204	77.94%	\$21,190	57.96%	\$7,928	(\$1,976)
	6/30/2009	\$130,224	88.53%	\$19,479	43.23%	\$122,909	77.94%	\$21,482	57.96%	\$7,315	(\$2,003)
09-10	9/30/2009	\$119,070	84.30%	\$27,251	67.21%	\$101,064	56.43%	\$25,755	58.03%	\$18,006	\$1,496
	12/31/2009	\$95,268	84.30%	\$27,412	67.21%	\$80,862	56.43%	\$25,907	58.03%	\$14,407	\$1,505
	3/31/2010	\$92,049	84.30%	\$23,576	67.21%	\$78,129	56.43%	\$22,282	58.03%	\$13,920	\$1,294
	6/30/2010	\$117,410	84.30%	\$27,578	67.21%	\$99,655	56.43%	\$26,064	58.03%	\$17,755	\$1,514
10-11	9/30/2010	\$107,773	84.30%	\$23,402	67.21%	\$92,721	58.56%	\$22,896	63.59%	\$15,052	\$507
	12/31/2010	\$150,933	84.30%	\$27,618	67.21%	\$129,853	58.56%	\$27,020	63.59%	\$21,080	\$598
	3/31/2011	\$135,551	84.30%	\$26,026	67.21%	\$116,619	58.56%	\$25,463	63.59%	\$18,932	\$563
	6/30/2011	\$152,812	84.30%	\$30,502	67.21%	\$131,470	58.56%	\$29,842	63.59%	\$21,342	\$660
11-12	9/30/2011	\$99,912	90.68%	\$21,773	95.25%	\$97,863	86.77%	\$19,646	76.17%	\$2,049	\$2,128
	12/31/2011	\$131,356	90.68%	\$24,230	95.25%	\$128,663	86.77%	\$21,863	76.17%	\$2,694	\$2,368
	3/31/2012	\$122,943	90.68%	\$27,432	95.25%	\$120,422	86.77%	\$24,752	76.17%	\$2,521	\$2,681
	6/30/2012	\$104,869	90.68%	\$14,540	95.25%	\$102,718	86.77%	\$13,119	76.17%	\$2,150	\$1,421
12-13	9/30/2012	\$127,421	124.69%	\$16,554	76.46%	\$105,043	85.23%	\$15,965	70.19%	\$22,378	\$588
	12/31/2012	\$125,468	124.69%	\$33,935	76.46%	\$103,433	85.23%	\$32,730	70.19%	\$22,035	\$1,206
	3/31/2013	\$141,252	124.69%	\$22,586	76.46%	\$116,446	85.23%	\$21,784	70.19%	\$24,807	\$803
	6/30/2013	\$146,149	143.69%	\$13,466	58.56%	\$111,089	85.23%	\$14,454	70.19%	\$35,061	(\$988)
13-14	9/30/2013	\$172,854	143.69%	\$24,206	58.56%	\$134,274	89.30%	\$28,064	83.83%	\$38,580	(\$3,858)
	12/31/2013	\$155,518	143.69%	\$17,193	58.56%	\$120,807	89.30%	\$19,933	83.83%	\$34,711	(\$2,740)
	3/31/2014	\$155,050	143.69%	\$23,090	58.56%	\$120,444	89.30%	\$26,770	83.83%	\$34,606	(\$3,680)
	6/30/2014	\$135,262	143.69%	\$28,127	58.56%	\$105,072	89.30%	\$32,610	83.83%	\$30,190	(\$4,483)
14-15	9/30/2014	\$146,044	143.69%	\$38,684	58.56%	\$114,779	91.52%	\$47,108	93.09%	\$31,266	(\$8,424)
	12/31/2014	\$144,877	143.69%	\$25,387	58.56%	\$113,861	91.52%	\$30,916	93.09%	\$31,016	(\$5,529)
Totals										\$487,210	(\$21,703)

DEFERRED COMPENSATION PLAN QUARTERLY REVIEW OF REVENUES & EXPENSES					
	Pending	Pending	Pending	Pending	Adopted
	Ending	Ending	Ending	Ending	Ending
REVENUE & EXPENSE LINE ITEMS	12/31/2015	9/30/2015	6/30/2015	3/31/2015	12/31/2014
STARTING BALANCE					
Payroll Fee Trust Fund Ending Balance - 9/30/15	\$ 71,967	44,723	51,361	19,776	208,102
Administrative Fee Reserve Fund Balance - 9/30/15	\$ 3,073,495	3,011,427	2,770,386	2,822,365	2,647,722
Total	\$ 3,145,462	3,056,150	2,821,747	2,842,141	2,855,824
REVENUES/FEES					
Interest Earnings on Payroll Fee Trust Fund	\$ 106	75	208	697	169
Payroll Fee Trust Fund Deposit: Travel	\$ -	40,850	-	45,850	
Payroll Fee Trust Fund Deposit: Salary Reimbursements	\$ -	-	-	163,389	172,710
Interest Earnings on Admin Fee Reserve Fund	\$ 14,404	13,301	12,287	10,778	11,348
Revenue from Fees Deducted from Participant Accounts	\$ 640,669	652,311	649,377	641,839	637,040
CAP Adjustment Credits	\$				
Miscellaneous Credits	\$ 27	15	32	1	817
Total Revenue/Fees	\$ 655,206	706,552	661,904	862,554	822,084
TOTAL ASSETS (STARTING BALANCE + REVENUE/FEES)	\$ 3,800,667	3,762,702	3,483,651	3,704,695	3,677,908
EXPENDITURES					
Participant Administrative Fees Paid to Great-West	\$ (383,952)	(381,974)	(379,432)	(378,074)	(376,697)
Prior Quarter Departmental Staffing Reimbursements	\$ -	-	-	(326,779)	-
Consulting Costs	\$ (121)	(94,407)	(7,434)	(18,046)	(61,049)
Plan Administrator Hardship Administration	\$ (18,250)	(19,000)	(18,250)	(20,000)	(21,000)
Plan Administrator Asset Allocation Fund Management	\$ (14,250)	(14,250)	(14,250)	(14,250)	(14,250)
Communications	\$ (1,950)	(29,160)	(10)	(63,136)	-
2130 Travel/Training/Education	\$ (9,759)	(13,697)	(6,876)	(14,962)	(10,370)
Travel/Training/Education - Payment-Steptoe - Training	\$ (600)	(42,785)	-	(46,450)	-
Elections Administration	\$ -	(20,717)	-	-	-
Wells Fargo Custodial Fees	\$ (1,250)	(1,250)	(1,250)	(1,250)	(1,250)
6010 Office and Administrative	\$ -	-	-	-	-
4160 Governmental Meetings	\$ -	-	-	-	-
TOTAL EXPENDITURES	\$ (430,132)	(617,240)	(427,502)	(882,947)	(484,615)
Actual Payroll Fee Trust Fund Ending Balance	\$ 62,314	71,967	44,723	51,361	19,776
Actual Administrative Fee Reserve Fund Ending Balance	\$ 3,308,222	3,073,495	3,011,427	2,770,386	2,822,682
ACTUAL TOTAL ENDING BALANCE	\$ 3,370,535	3,145,462	3,056,150	2,821,747	2,842,458

ENCUMBRANCES/LIABILITIES					
Net from Prior Quarter	(249,441)	(102,581)	60,407	196,288	(146,044)
Quarterly Personnel Direct/Indirect Costs	\$ (139,627)	(146,859)	(162,988)	(135,882)	(144,877)
2007-2015 Personnel Adjustments					\$487,210
Net Ending Balance	(389,068)	(249,441)	(102,581)	60,407	196,288
Prior Quarter Departmental Staffing Reimbursements: 9/30/14	(190,175)	(160,955)	(120,419)	(85,774)	(38,684)
Quarterly City Attorney Direct/Indirect Costs	\$ (31,691)	(29,220)	(40,536)	(34,645)	(25,387)
2007-2015 City Attorney Adjustments					(\$21,703)
Net Ending Balance Owed	(221,865)	(190,175)	(160,955)	(120,419)	(85,774)
TOTAL ASSETS LESS LIABILITIES	2,759,603	2,705,846	2,792,614	2,761,735	2,952,973

DEFERRED COMPENSATION PLAN		
PROPOSED BUDGET		
Plan Year 2016		
REVENUES		
Projected Starting Balance on 01/01/16	\$	2,759,603
Estimated Annual Administrative Fee Revenue	\$	2,672,669
Estimated Interest Earnings	\$	55,192
Opening Balance Plus Projected Revenues	\$	5,487,463
EXPENDITURES		
Participant Administrative Fees	\$	(1,561,472)
Personnel Staffing	\$	(753,996)
City Attorney Staffing	\$	(163,107)
Estimated Consulting Costs	\$	(185,000)
TPA Hardship Administration	\$	(100,000)
TPA Asset Allocation Fund Management	\$	(72,000)
Communications	\$	(75,000)
2130 Travel/Training/Education	\$	(59,178)
Elections Administration	\$	-
Wells Fargo Custodial Fees	\$	(5,000)
6010 Office and Administrative	\$	(7,000)
4160 Governmental Meetings	\$	(500)
Total Estimated Expenditures	\$	(2,982,253)
Annual Revenues Less Annual Expenditures	\$	(254,392)
Projected Ending Balance on 12/31/16	\$	2,505,211

Detail regarding budget items and assumptions included therein:

REVENUES

- **Projected Starting Balance on 01/01/16** – The projected starting balance includes amounts held in both the Empower Reserve Fund account and the City's Administrative Fee Trust Fund account.
- **Administrative Fee Revenue** – Projections for administrative fee revenues (amounts collected from participant accounts) reflect an increase in Plan assets. The one-year Plan assets growth rate assumption is 6.5% as established in the Strategic Plan revised by the Board in November 2013. Plan assets are impacted by both investment gains as well as participant contributions/rollovers.

- **Interest** – The Board previously adopted a long-term average rate of return for the Stable Value Fund of 2.75%. However, for the purpose of this report and the illustration within the 10-year projection, staff is assuming a 2% long term rate of return in order to be consistent with the current prolonged low-interest rate environment.

EXPENDITURES

- **Participant Administrative Fees Owed to Plan Administrator** – The City's contractual obligation to the Plan Administrator is \$36.97 per participant. The long-term projected participant growth rate is 1%.
- **Estimated Personnel Department and City Attorney Reimbursements** – The City's Plan reimburses for direct and indirect staffing costs for its various positions. The estimated expenditures for these positions for 2016 takes into account current paygrade levels and other factors. These rates reflect the Special Rate as adopted through Board Report 16-03.
- **Estimated Consulting Costs** – The Board has contracts for various consulting services (investment, plan administration, and communications consulting), and also pays for tax consulting services on an as-needed basis via a contract administered by the City Attorney's Office. Staff projects a total of \$185,000 in consulting expenditures for 2016.
- **Plan Administrator Hardship Administration** – Staff is projecting approximately 400 hardship cases to be processed next year at a cost of \$250 per completed case.
- **Plan Administrator Asset Allocation Fund Management** – This category includes charges from the Plan Administrator for recordkeeping and unitization services for the Plan's asset allocation funds and custom Plan-branded funds.
- **Communications** – This category includes special communication costs over and above the amounts already included within the Plan Administrator budget (e.g. for enhancements to the Plan's Retirement Income Projection Calculator). This amount was increased in 2015 for special communication initiatives.
- **Travel/Training** – For Plan Year 2015, the Board adopted an annual training/travel amount of \$59,178. Actual training expenditures have consistently been significantly below adopted budget amounts. Staff does not recommend an increase of this amount for 2016. This amount should be considered the upper range of potential expenditures if all Board members and staff availed themselves of all training opportunities provided for within the Board's adopted training program.

- ***Elections Administration*** – No elections are scheduled to take place in 2016.
- ***Wells Fargo Custodial Fees*** – These are fees paid annually for Wells Fargo trustee services.
- ***Office and Administrative*** – This expense is generally utilized for smaller office supply purchases. An amount of \$7,000 has been budgeted to cover computer and software purchases/upgrades and other office equipment.
- ***Governmental Meetings*** – This includes all incidental costs tailored for special Board meetings. A nominal amount of \$500 has been budgeted.