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DEFERRED COMPENSATION PLAN BOARD REPORT 05-34



Date: November 4, 2005

To: Board of Deferred Compensation Administration

From: Staff

Subject: Plan Staffing and Budget for Calendar Year 2006

Recommendation:

That the Board of Deferred Compensation Administration:

- (a) Approve the addition of a half-time Accounting Clerk authority and full-time Management Analyst authority to expand Personnel Department staffing resources for the Deferred Compensation Plan; and
- (b) Approve staff's proposed Deferred Compensation Plan budget for calendar year 2006 which consolidates resources/expenditures for the Plan's Administrative Fee Trust Fund and Great-West Reserve Fund.

Discussion:

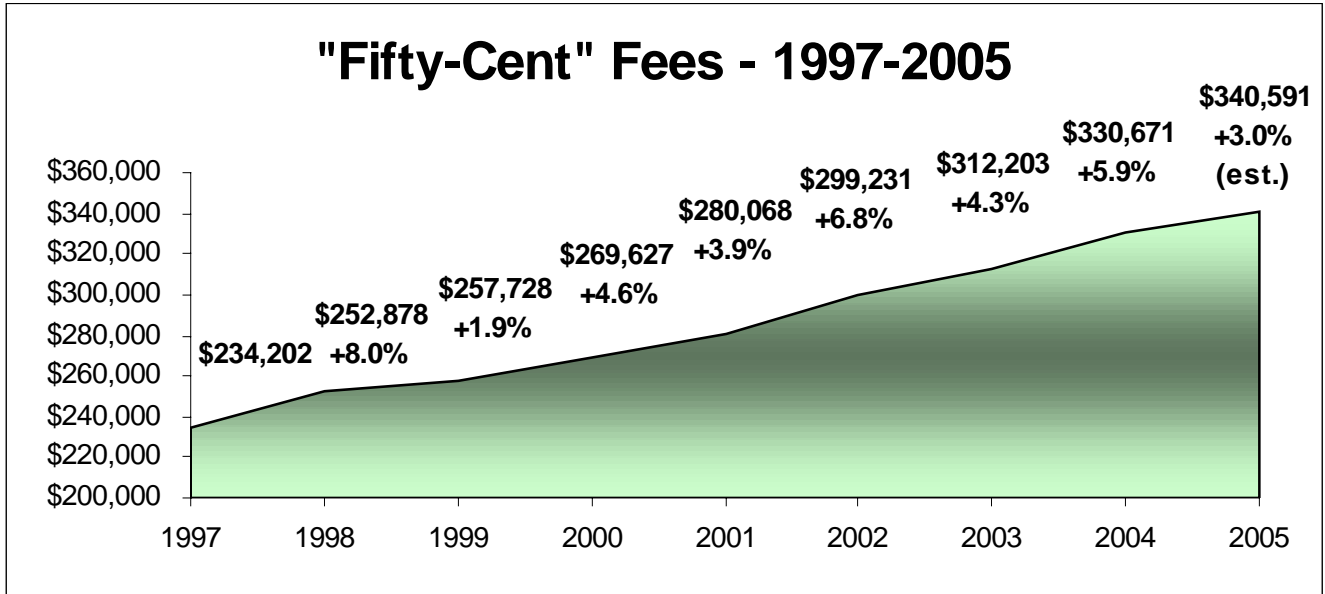
Background - Staff has been giving consideration recently to a range of strategic planning issues concerning the Deferred Compensation Plan, among them the question of whether the Plan's resources are properly aligned with its needs going forward. The focus of this report specifically addresses Plan revenues and the City's internal costs for managing the program.

To begin this review, staff believes it is helpful to take a global perspective of the resources available to the Plan. In the past, separate reporting has been conducted for the City's Administrative Fee Trust Fund (the repository for the bi-weekly fifty-cent fee paid by Plan participants) and the Great-West Reserve Fund (the repository for excess administrative fee revenue paid by Plan participants to Great-West).

In Attachment 1, staff is presenting this global view in the form of a recommended adopted budget for the Plan, which will be discussed more fully at the end of this report. For the moment, however, looking strictly at net inflow/outflow, overall Plan revenue exceeds expenses by approximately **\$400,000** per year, with a current surplus of **\$1.4 million**.

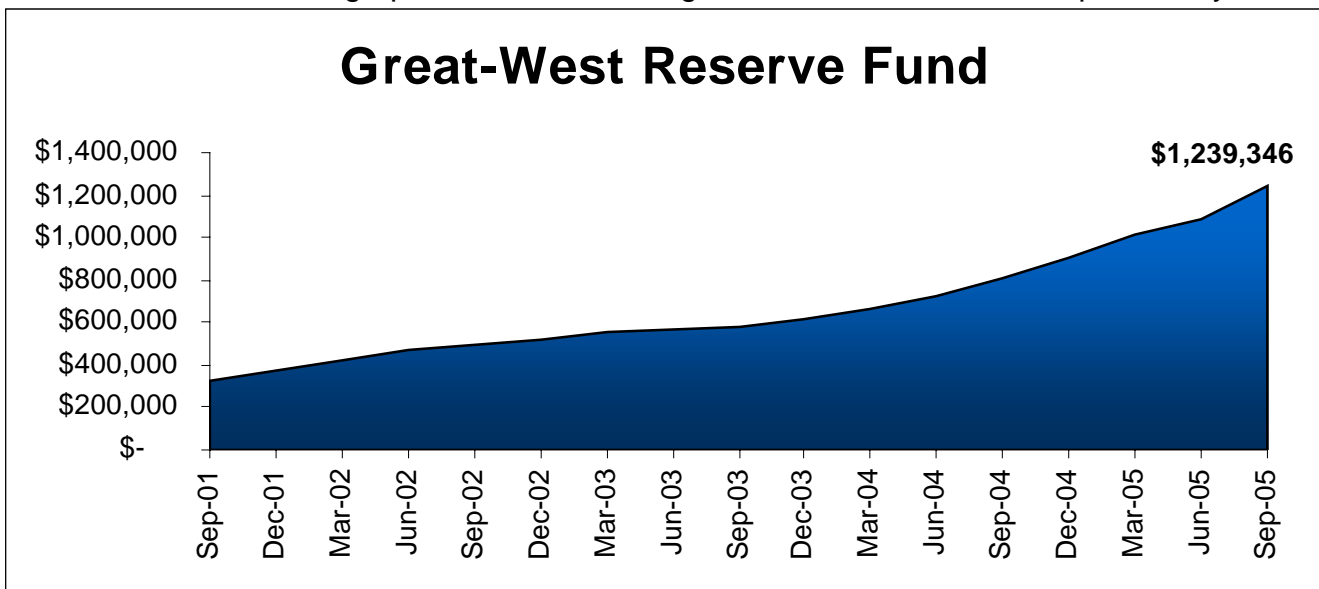
Revenues - From Plan inception in 1983 through July 1999, the Plan's only revenue source was administrative fees charged to Plan participants with their bi-weekly Plan deferrals. Beginning with the City's contract with Great-West, a Reserve Fund was established to hold excess fee revenue from the recordkeeping fees owed to Great-West. Currently the surplus in this Fund is \$1.2 million, expected to grow to approximately \$1.4 million by the end of this calendar year.

Administrative Fee Trust Fund – Administrative Fee Trust Fund revenues have risen steadily in recent years as a result of rising participation rates, as indicated by the following graph:

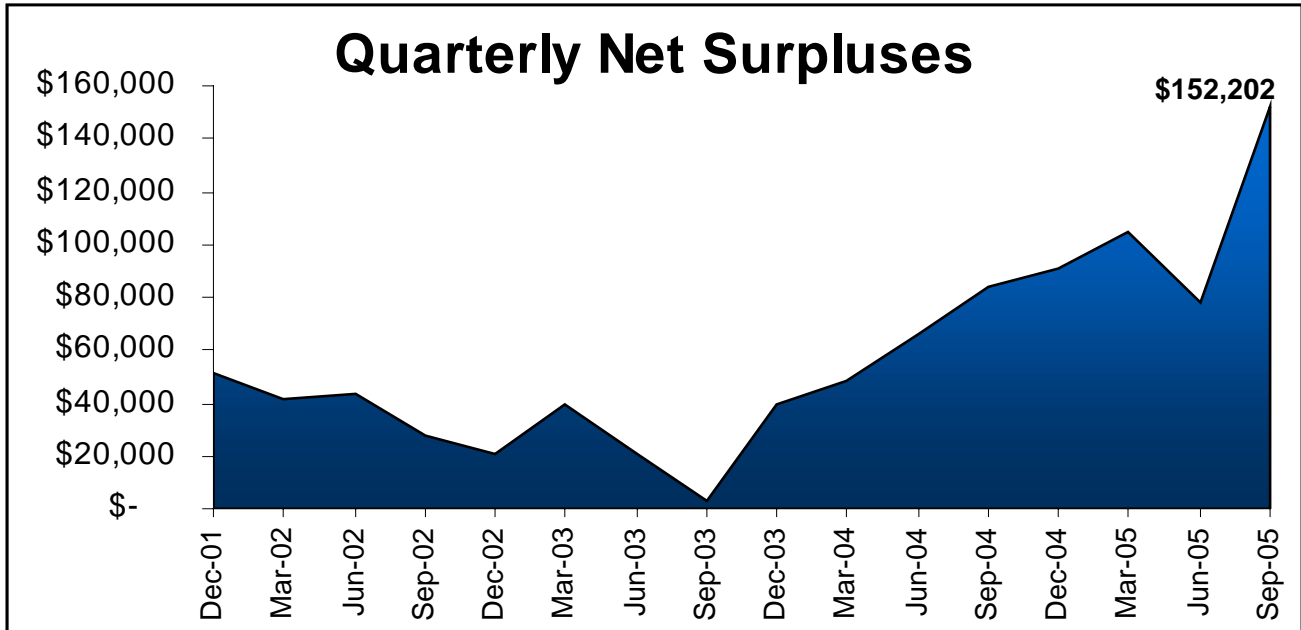


Although, as the City's Plan matures, the rate of increased participation can be expected to slow, history demonstrates the stability of this revenue stream.

Great-West Reserve Fund – As of September the Great-West Reserve Fund has reached the \$1.2 million mark. The graph below shows the growth in the Fund over the past four years:



Perhaps more revealingly, the graph below shows the quarter-by-quarter net surplus added to the Reserve Fund. This graph shows that, with Plan assets now having passed the \$2 billion mark, the surpluses generated by the Plan's fee structure are now growing significantly:



Expenses – Staff believes there are two structural deficiencies in the Plan with respect to resources: (a) staffing and (b) consulting services. Staff will address each of these resource items separately.

Staffing – Currently there are 2.5 staff assigned to the Plan. Although historically this staffing level has been largely sufficient for the needs of the Plan, the real question is whether this has been true more recently and will continue to be the case.

Much has changed in the Plan in the last several years since the passage of the 2001 Economic Growth and Tax Relief Reconciliation Act (EGTRRA). EGTRRA provided for a substantial expansion of the potential benefits that can be offered under Section 457 plans, virtually all of which the City's Plan has phased in over the last few years. This has resulted in a substantial increase in the administrative "back-office" workload for Personnel Department staff, as follows:

- Distributions - the ability of participants to process multiple distribution requests, as opposed to pre-EGTRRA rules which allowed only one lifetime request, has more than tripled the annual caseload – as an example, in 1999 staff processed 788 distributions, compared to 2,726 in 2004;
- Loan Program – the loan program, introduced a year and a half ago, has created a host of new responsibilities for Department staff, who must facilitate issues regarding payroll-deducted loan repayments, loan deferments based on approved leave, and notifications for employees in danger of going into default;

- Rollovers – EGTRRA expanded rollovers (both in and out of the Plan) to include IRAs, 401(k) plans, and other similar qualified plan arrangements, compared to the pre-EGTRRA rules which permitted only transfers between Section 457 plans;
- Service Credit Purchases – also not permitted pre-EGTRRA, these transactions frequently require substantial staff intervention in dealing with the City pension systems.

In addition to demands on the Plan’s administrative staff, professional staff are also facing challenges with the growing complexity of the Plan. Some samples of new initiatives (beyond existing ongoing assignments such as hardship withdrawals, beneficiary claims, qualified domestic relations orders, existing RFP processes and contract execution, etc.) likely to demand attention include:

- An anticipated expansion of investment contracts (and related Requests for Proposal) as the Plan continues to evolve from mutual funds to separate accounts/commingled funds;
- A possible expansion of other Plan contracts (and related Requests for Proposal) for regular Plan audits, investment review and multiple consulting relationships;
- An expansion of staff time devoted to the work resulting from standing or ad hoc Board committees;
- More direct staff involvement in the planning and execution of communication/outreach efforts;
- Potential new initiatives such as auto-enrollment, accumulated leave deferrals into the Plan, accumulated leave deferrals into other pre-tax programs, investment menu consolidation, etc.
- Drafting of bylaws and ethics policies, and redrafting of the City’s Administrative Code provisions and Plan Document provisions, as a result of work performed by the Plan Governance Task Force and Plan Governance Committee.

To address these needs effectively, staff is proposing that the Plan add 1.5 positions: a half-time Accounting Clerk II to assist with new administrative duties, and a full-time Management Analyst to assist with expanded professional duties. Attachment 2 provides a salary breakdown and Attachment 3 breaks out the proposed duties of all positions associated with the Plan.

The half-time Accounting Clerk position will take over many of the current payroll-related duties of the current Retirement Benefits position, allowing the focus of that position to be on distributions, loans, and daily participant contact. The full-time Management Analyst I position will have exposure to most of the professional duties associated with the program but with a focus on contracting, which will allow the Management Analyst II position to focus more on communications.

Consulting Services – The City’s Plan first began utilizing the services of a consultant in 1995, with an annual contract amount set at \$50,000. Over the course of the last ten years the annual budgeted amount for those services has grown to \$100,000, but given the complexity of the City’s Plan, more resources are needed.

As an example, the survey project alone will cost approximately \$85,000. In the past the Plan, limited by having only the Administrative Fee Trust Fund as a source of funding, has had to live within its means by performing certain tasks periodically (e.g. Plan audits and performance review) as opposed to annually or semi-annually. As an example, staff anticipates that one of the policies likely to emerge from the Board's Investment Committee will be an investment policy that recommends regular annual performance review conducted by the consultant. Bi-annual audits, and either annual or bi-annual surveys, may be other tasks the Board may wish to mandate.

Beyond these types of projects are ongoing responsibilities such as Requests for Proposal for Plan administrative services and investment management services. Further, as City decision-makers express interest in related programs and initiatives (e.g. establishment of a tax-deferred vehicle for accrued leave at retirement) and as the legal backdrop for retirement savings programs continues to evolve in Washington, the City's needs in this area are likely to grow ever more complex for years to come. Finally, it is possible that expert legal advice may be needed for special or more complex projects.

In consideration of all this, staff is recommending that the budget for annual consulting expenditures be increased to \$300,000. This level of funding should be sufficient for annual investment reviews, bi-annual audits, bi-annual surveys, multiple manager searches annually, ongoing consulting needs, and perhaps as-needed legal or other services.

Annual Budget – If the Board agrees with staff that this basic framework makes sense, staff recommends that the Board go a step further in approaching its resource decisions in the context of adopting an annual budget for the Plan. Creating a global means of planning for and reporting on Plan resources and expenditures will allow the Board to better prioritize its initiatives going forward and provide greater transparency to Plan participants. As a result, staff is recommending that the Board adopt the attached budget for the Plan for calendar year 2006.

It should be noted that virtually all of the assumptions in this budget are conservative. With respect to salaries, the budget assumes that all of the positions for the program are filled for the entire year at their full position authority, when in fact adding any positions to the program will first require CAO approval as part of the City's regular budget process – the earliest that could go into effect would be July 2006, and may not take place until a subsequent fiscal year. In addition, it is likely that the newer positions would be filled in-lieu at a lower level, so further salary savings are likely to accrue.

Further, until Board Committees develop recommended policies and the Board adopts them, some of the potential new consulting expenses may not be incurred in 2006. As a result, total consulting costs for 2006 are likely to be substantially less than \$300,000.

On the revenue side, estimates for additional surplus from the Great-West Reserve Fund are based on a modestly conservative estimate relative to the Plan's current asset base. In the most recent quarter, the surplus amount that flowed into the Reserve Fund was \$152,202 –

extrapolated to four quarters, the net increase would be \$608,808. Even an average of the last four quarterly net increases produces an annual increase of \$425,000.

Staff's budgetary assumption calls for an annual net increase of \$375,000 based on the potential impact of a substantially declining market, which is always a risk. Given (a) the existing surplus, which provides further margin for error; and (b) the fact that this budget still provides for a surplus of annual revenue less current-year expenses in the amount of \$67,000, staff believes that adopting this budget with its increased staffing and consulting expenditures presents no danger of over-extending the Plan on either a near-term or long-term basis. Further, given that any increased staffing or consulting expenses must be phased in over at least a year's time, there will be ample time to monitor and make adjustments in the event revenue assumptions are not met.

Submitted by: _____
Steven Montagna

Approved by: _____
Maryanne Keehn

| PROPOSED DEFERRED COMPENSATION PLAN BUDGET ADMINISTRATIVE AND OPERATING EXPENSES CALENDAR YEAR-ENDING 12/31/06 | |
|---|---------------------|
| REVENUES/FEES | |
| Estimated Year-End Balance Trust Fund #896 | \$ 326,589 |
| Estimated Year-End Balance Great-West Reserve Fund | \$ 1,400,000 |
| Total Current Surplus | \$ 1,726,589 |
| Estimated City Administrative ("Fifty Cent") Fees | \$ 340,000 |
| Estimated Net Increase to Reserve Fund | \$ 375,000 |
| Estimated Interest Earned on Administrative Fee Trust Fund | \$ 8,000 |
| TOTAL REVENUE/FEES | \$ 2,449,589 |
| EXPENDITURES | |
| Reimbursements to Personnel | \$ (318,363) |
| Contractual Services (Admin Consulting, Annual Investment Review, Bi-annual Plan audit, Legal as needed) | \$ (300,000) |
| NAGDCA/Education | \$ (35,000) |
| Office & Admin | \$ (2,000) |
| TOTAL EXPENDITURES | \$ (655,363) |
| ESTIMATED ACTUAL BALANCE AS OF YEAR-END | \$ 1,794,226 |
| Regular Plan Revenue | \$ 723,000 |
| Regular Plan Expenses | \$ (655,363) |
| Regular Revenue Less Expenses | \$ 67,637 |

| PERSONNEL SALARY POSITION AUTHORITIES | PROJECTED NEXT FOUR QUARTERS | | | | |
|--|------------------------------|--------------|--------------|--------------|---------------|
| | 3/31/2006 | 6/30/2006 | 9/30/2006 | 12/31/2006 | Annual Total |
| Senior Personnel Analyst I | | | | | |
| Annual | \$ 86,830.32 | \$ 86,830.32 | \$ 88,566.92 | \$ 88,566.92 | |
| Three Month Salary | \$ 21,707.58 | \$ 21,707.58 | \$ 22,141.73 | \$ 22,141.73 | |
| Reimbursable Percent | 50.00% | 50.00% | 50.00% | 50.00% | |
| Reimbursable Amount | \$ 10,853.79 | \$ 10,853.79 | \$ 11,070.87 | \$ 11,070.87 | \$ 43,849.31 |
| Management Analyst II | | | | | |
| Annual | \$ 73,455.42 | \$ 73,455.42 | \$ 74,924.53 | \$ 74,924.53 | |
| Three Month Salary | \$ 18,363.86 | \$ 18,363.86 | \$ 18,731.13 | \$ 18,731.13 | |
| Reimbursable Percent | 100.00% | 100.00% | 100.00% | 100.00% | |
| Reimbursable Amount | \$ 18,363.86 | \$ 18,363.86 | \$ 18,731.13 | \$ 18,731.13 | \$ 74,189.98 |
| Management Analyst I | | | | | |
| Annual | \$ 56,949.78 | \$ 56,949.78 | \$ 58,088.78 | \$ 58,088.78 | |
| Three Month Salary | \$ 14,237.45 | \$ 14,237.45 | \$ 14,522.19 | \$ 14,522.19 | |
| Reimbursable Percent | 100.00% | 100.00% | 100.00% | 100.00% | |
| Reimbursable Amount | \$ 14,237.45 | \$ 14,237.45 | \$ 14,522.19 | \$ 14,522.19 | \$ 57,519.28 |
| Retirement Benefits Specialist | | | | | |
| Annual | \$ 59,548.09 | \$ 59,548.09 | \$ 60,739.05 | \$ 60,739.05 | |
| Three Month Salary | \$ 14,887.02 | \$ 14,887.02 | \$ 15,184.76 | \$ 15,184.76 | |
| Reimbursable Percent | 100.00% | 100.00% | 100.00% | 100.00% | |
| Reimbursable Amount | \$ 14,887.02 | \$ 14,887.02 | \$ 15,184.76 | \$ 15,184.76 | \$ 60,143.57 |
| Accounting Clerk II | | | | | |
| Annual | \$ 52,839.35 | \$ 52,839.35 | \$ 53,896.13 | \$ 53,896.13 | |
| Three Month Salary | \$ 13,209.84 | \$ 13,209.84 | \$ 13,474.03 | \$ 13,474.03 | |
| Reimbursable Percent | 50.00% | 50.00% | 50.00% | 50.00% | |
| Reimbursable Amount | \$ 6,604.92 | \$ 6,604.92 | \$ 6,737.02 | \$ 6,737.02 | \$ 26,683.87 |
| | | | | | |
| | | | | | |
| TOTAL PERSONNEL DEPARTMENT | \$ 50,709.59 | \$ 50,709.59 | \$ 51,723.78 | \$ 51,723.78 | \$ 262,386.01 |
| | | | | | |
| Total Salary Costs | | | | | \$ 262,386 |
| Estimated Retirement/Overhead | | | | | 52,477 |
| Office Supplies | | | | | \$ 3,500 |
| Total Department Costs | | | | | \$ 318,363 |

POSITION DUTIES

| Sr. Personnel Analyst | | Management Analyst II | | Management Analyst I | |
|--|-----------|---|-----------|--|-----------|
| Assignment | % of Time | Assignment | % of Time | Assignment | % of Time |
| Plan Manager - Oversee overall operation of Plan, including functioning as primary point of contact for Board, Personnel Department management, contractors and outside agencies. | 25% | Communications Coordinator – Work directly with key departmental and union personnel for the purpose of developing successful enrollment outreach; identify measurable goals and objectives; generate reports on results to Board. | 35% | Request for Proposals/Contracts - Develop and issue RFPs for Plan services, analyze responses, manage vendor selection and contract development/execution | 40% |
| Plan Design - Develop recommendations/reports concerning high-level issues affecting the Plan including Plan services, investment menu design, Plan policies, regulatory compliance, and communication/enrollment strategies. | 15% | Request for Proposals/Contracts - Develop and issue RFPs for Plan services, analyze responses, manage vendor selection and contract development/execution | 25% | Hardship Applications - counsel potential applicants telephonically, write reports and recommendations, process distributions | 15% |
| Contract Oversight - Coordinate all Plan-related RFP scheduling, development & review processes, and develop/monitor all contracts for Plan. | 10% | Projects & Reports - Miscellaneous Board reports, research, correspondence, respond to participant or outside requests for information, etc. | 25% | Qualified Domestic Relations Order Processing - process account separations due to divorce - create file, impose account restrictions, monitor City Attorney approval, facilitate final account separation. | 15% |
| | | Board Meeting Preparation - schedule meetings, copy Board materials and distribute Board packages, facilitate all aspects of meeting preparation [e.g. parking, meeting set-up, etc.] | 5% | Beneficiary Claims for both DCP & PSP, provide affidavits, review documentation, obtain approval or guidance from City Attorney as cases demand process distribution when finally approved | 10% |
| | | NAGDCA Planning - Make reservations, work with Board members, and work with Accounting/Controller to prepare for and reconcile all aspects of Board/staff attendance at annual NAGDCA conference | 5% | Board Meeting Minutes - prepare Board meeting minutes | 5% |

Retirement Benefits Specialist

100%

Accounting Clerk

50%

| Assignment | % of Time | Assignment | % of Time |
|---|-----------|---|-----------|
| Deferred Compensation Plan Distributions - verify termination of employment, interact w/operating departments and Great-West to resolve disputes re term date | 50% | Payroll Resolution - Provide data entry for contributions and loan repayments; address all payroll refunds and errors related to contributions | 15% |
| Loan Program - address issues related to participants having gone off payroll, generate loan statistics for program manager | 20% | Contract Payments, Auditing & Review - process all contract payments to vendors, provide auditing for all recordkeeping and payroll transactions | 10% |
| Rollovers & Purchase of Service Credit - facilitate participant plan-to-plan transfers including purchase of service credit with retirement/pension systems | 5% | Bi-weekly Wire Transfers - responsible for processing wire transfers for Deferred Compensation Plan & Pension Savings Plan for both City and DWP | 5% |
| Participant Phone Inquiries - Primary respondent for Deferred Comp/Pensions Savings Plan participant questions re all aspects of Plan participation (enrollment, distribution, etc.) | 10% | Trust Fund Payments/Transfers of Funds - responsible for all transfers in and payments from Administrative Fee Trust Fund #896 | 5% |