

Deferred Compensation Plan BOARD REPORT 15-03

Date: January 12, 2015
To: Board of Deferred Compensation Administration
From: Staff
Subject: Proposed 2015 Budget: Deferred Compensation Plan

*Board of Deferred
Compensation Administration
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Cliff Cannon, First Provisional Chair
Tom Moutes, Second Provisional Chair
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Recommendation:

That the Board of Deferred Compensation adopt the proposed Deferred Compensation Plan Budget for Plan Year 2015.

Discussion:

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 2015 calendar year as included in **Attachment A**. This attachment includes a narrative description of the assumptions and other relevant factors regarding each budgetary item.

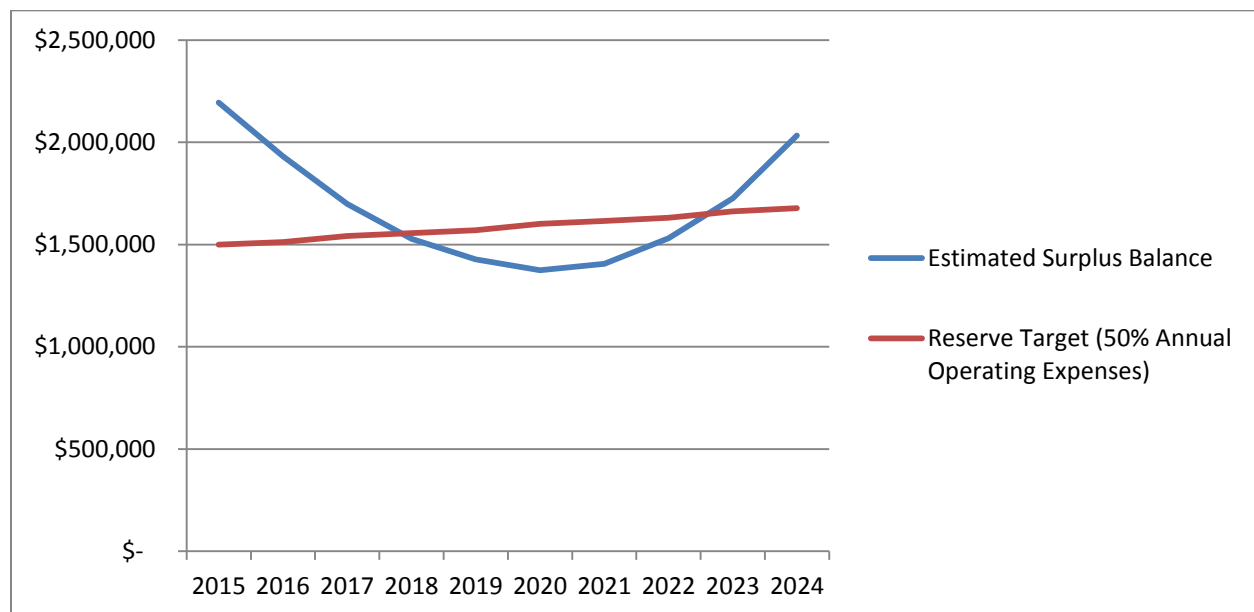
The annual budget supplements the quarterly reconciliations of the Plan's fee revenues and internal administrative expenses. In addition, the annual budget reflects the unique circumstances of the upcoming one-year time period, as opposed to the more generalized five-year forecasts that are incorporated 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 2015 is estimated to be approximately \$241,191, a decrease from the prior budget year and an amount in line with the long-term reserve objective.

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 2015, one-half of annual operating expenses is approximately \$1.4 million. The estimated surplus in the Trust Fund by the end of 2015 is expected to be \$2.3 million.

Over a ten-year period, based on current assumptions, the annual surplus is expected to gradually trend closer to the targeted amount before trending above the target in outlying years.



Additionally, following are updates regarding budget-related items recently discussed with the Board related to the Plan's ongoing expenditures:

- a. **Staffing/Calculation of Indirect Costs** - At its October 21, 2014 meeting, the Board asked staff to report back relative to the staff resources assigned to the Plan. Staff has not completed its review of this topic and will address it in a separate report which will include discussion of current staff and staff assignments/allocations, as well as review of staffing resources relative to Plan administrative responsibilities and Plan revenues. Concurrently, staff is reviewing the methodology by which indirect costs related to Plan salary expenses are calculated using the City Controller Cost Allocation Plan (CAP) rates. Specifically, staff is researching the feasibility of establishing a unique rate specifically for Deferred Compensation Plan staff, rather than the general Personnel Department rate that is presently used. Staff has initiated but not completed its research on this item and will report to the Board once its review process is complete.

b. **Travel/Training** - At its April 15, 2008 meeting, the Board adopted an annual (calendar year) training base budget of \$50,000 with an annual inflation component in anticipation of rising training costs over time. At its July 17, 2012 meeting, the Board approved a Training, Education and Travel Policy developed by the Board's Plan Governance & Administrative Issues Committee. This policy provides that unused training amounts from prior years will carry forward into subsequent years. In practice, however, the Plan routinely expends closer to half the annually budgeted amount. Given this, staff recommends that the Board direct staff to return with proposed revisions to the Board's Training, Education and Travel Policy to remove the revision providing that funds will carry over to future years. Staff recommends that the estimated funding for training/travel be established each year on a calendar year basis within the Board's adopted budget. Should a need for additional training/travel funds be required within a given calendar year, the Board always has the discretion to authorize that additional funding. Unused training/travel funds at the end of a calendar year would be returned to the Plan's reserve balance.

Staff recommends that the Board adopt the proposed budget for calendar year 2015.

Submitted by:

Paul Makowski

Reviewed by:

Esther Chang

Approved by:

Steven Montagna

DEFERRED COMPENSATION PLAN		
PROJECTED REVENUES/EXPENDITURES Plan Year 2015		ADOPTED Plan Year 2014
REVENUES		
Projected Starting Balance on 01/01/15	\$ 2,414,398	\$ 2,511,969
Estimated Annual Administrative Fee Revenue	\$ 2,614,308	\$ 2,498,774
Estimated Interest Earnings	\$ 42,277	\$ 70,552
Opening Balance Plus Projected Revenues	\$ 5,070,983	\$ 5,081,295
EXPENDITURES		
Participant Administrative Fees Owed to Great-West	\$ (1,506,786)	\$ (1,498,320)
Estimated Personnel Department Reimbursements	\$ (739,761)	\$ (762,949)
Estimated City Attorney Reimbursements	\$ (108,552)	\$ (106,134)
Estimated Consulting Costs	\$ (185,000)	\$ (185,000)
Plan Administrator Hardship Administration	\$ (100,000)	\$ (100,000)
Plan Administrator Asset Allocation Fund Management	\$ (78,000)	\$ (72,000)
Communications	\$ (75,000)	\$ (50,000)
2130 Travel/Training/Education	\$ (59,178)	\$ (59,178)
Elections Administration	\$ (35,000)	\$ (21,200)
Wells Fargo Custodial Fees	\$ (5,000)	\$ -
6010 Office and Administrative	\$ (5,000)	\$ (5,000)
4160 Governmental Meetings	\$ (500)	\$ (500)
Total Estimated Expenditures	\$ (2,897,777)	\$ (2,860,281)
Annual Revenues Less Annual Expenditures	\$ (241,191)	\$ (290,955)
Projected Ending Balance on 12/31/15	\$ 2,173,207	\$ 2,221,014

Detail regarding budget items and assumptions included therein:

REVENUES

- **Projected Starting Balance on 01/01/15** – The projected starting balance includes amounts held in both the Great-West 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 adopted a long-term average rate of return for the Stable Value Fund of 2.75%. However, for calendar year 2015, based on current returns and the present interest rate environment, staff is estimating that this return will be approximately 1.75%.

EXPENDITURES

- **Participant Administrative Fees Owed to Plan Administrator** – The City's contractual obligation to the Plan Administrator is \$36.97 per participant. Civilian net employment has been trending negative while Police and Fire net employment have been static. Balanced against this are the ongoing efforts of the Plan to encourage new enrollments and implementation of the Auto Enrollment Program, anticipated later this year. Staff is therefore projecting a 1% growth rate in 2015.
- **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 2015 takes into account current paygrade levels and other factors.
- **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 2015. Over the past two years actual expenditures have averaged approximately \$150,000 annually. In 2015, in addition to ongoing recurring services, special assignments will include the passive managers search, the Stable Value Fund search, and work on developing the next RFP for third-party-administrative services.
- **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). An increase of \$25,000 is recommended for this category because of pending enhancements for the calculator and other potential special communications initiatives that may be considered by the Board in 2015.

- ***Travel/Training*** – For Plan Year 2014, the Board adopted an annual training/travel amount of \$59,178. As noted earlier in this report, actual training expenditures have consistently been significantly below adopted budget amounts. Staff does not recommend an increase of this amount for 2015. 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*** – Staff has included estimated costs for administering Board elections for the DWP and Retiree Representatives. Actual costs for administering the Civilian/Sworn elections totaled approximately \$42,000; costs for the DWP and Retiree positions are expected to be slightly lower because they involve smaller populations.
- ***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 \$5,000 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 has been budgeted.