

DEFERRED COMPENSATION PLAN BOARD REPORT 11-59

Date: August 30, 2011
To: Board of Deferred Compensation Administration
From: Staff
Subject: Plan Governance Best Practices

Members
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Recommendation:

That the Board of Deferred Compensation Administration a) receive and file information regarding a survey of local and state plan governance structures; b) amend Section IX of the Plan Document as outlined within this report; and c) adopt the attached Deferred Compensation Plan Accountability Chart as a new Appendix D of the Deferred Compensation Plan Bylaws/Governance Policies.

Background:

In its January 5, 2011 Memo regarding Trustee Services for the Deferred Compensation Plan, Mercer Investment Consulting provided the following suggestions with regards to strengthening governance of the Deferred Compensation Plan:

1. Consider more clarity in documentation around vendor selection and monitoring particularly regarding the City Council's ability to veto and remand decisions back to the Board.
2. Consider greater clarity in documentation around plan amendments specifically in regards to which governing entity has the ability to amend the Plan Document.
3. Develop an accountability chart or similar document to clearly define roles and responsibilities for important Plan functions.

At the January 18, 2011 meeting, the Board requested further elaboration and review of the above suggested best practices. In addition, the Board directed Mercer and staff to review the relationships of state and local government oversight Boards to their respective political bodies to help identify commonalities and review the respective authority of each governing entity.

Plan Governance Survey & Council Veto

Mercer and staff surveyed over fifteen large state and local Section 457 plans across the country regarding their respective governance structures. What became readily apparent from this review is that there is tremendous variation in the ways governmental

defined contribution plans are governed and administered, specifically as it relates to which tasks are delegated and which are retained by a political or oversight body. Staff will review the survey results, beginning with the City's structure:

City of Los Angeles – The City's Plan provides the Board with broad powers. The Administrative Code states: "The Board shall have the sole authority for the operation of the Plan in accordance with its terms and shall rule on all questions arising out of the administration, interpretation and application of the Plan, which determination shall be conclusive and binding on all Participants..." The Board also has contracting authority. The only limitation on the Board's powers is that its actions are subject to City Council veto. The Council may veto a decision and remand it to the Board for reconsideration, but it cannot take jurisdiction over the decision.

County of Los Angeles – The Plan's Administrative Committee has sole and exclusive responsibility for the administration of the Plan including execution of contracts. However, the Board of Supervisors retains the right to amend or terminate the Plan at any time.

County of Orange – An advisory committee makes recommendations to the County Chief Financial Officer who makes administrative decisions regarding fund/service changes and is considered the "sole fiduciary" of the Plan. However, the Board of Supervisors awards contracts and approves Plan document changes.

City & County of San Francisco – The Deferred Compensation Plan Committee oversees the administrative functions of the Plan, however, this Committee reports to the San Francisco Employees' Retirement System (SFERS) Board which has the sole authority to amend the Plan and execute contracts on behalf of the Plan.

City of Chicago – The Deferred Compensation Plan Committee performs all functions and duties regarding the administration of the Plan including the execution of contracts. However, the Committee must obtain approval from the Chicago City Council for Plan Document changes.

City of New York – The Board of Deferred Compensation was established by an executive directive from the Office of the Mayor as opposed to adopted legislation in a charter or administrative Code. The Board retains full oversight of the Plan including the ability to amend the Plan Document and execute contracts. The Mayor appoints positions to the Board.

State of California – The Director of the Department of Personnel Administration serves as the "sole fiduciary" and has sole decision-making and contracting authority. This position is appointed by the Governor of California.

State of Georgia – The 457b Plan is wholly administered by the Employees' Retirement System Board of Trustees, which also has the authority to execute contracts

for the Plan. There is not a separate committee or board that oversees the 457b Plan administration.

State of Maryland – The Maryland Supplemental Retirement Plans Board of Trustees administers the Plan and is comprised of members appointed by the Governor of Maryland as well as participant representatives. The Board has the authority to amend the Plan and execute contracts under \$200,000. For contracts over \$200,000, the Board of Trustees must obtain approval from the Board of Public Works.

State of Oregon – The State of Oregon Employees' Retirement System administers the Oregon Savings Growth Plan, which is comprised of members appointed by the Governor of Oregon. An advisory committee comprised of members appointed by the Board makes recommendations to the Board regarding the Savings Growth Plan. The Board has the authority to amend the Plan and execute contracts regarding Plan services. Selection of Investment providers, however, is administered through the State Treasury Department and Oregon Investment Council.

State of Hawaii – The Deferred Compensation Plan Board of Trustees has the authority to amend the Plan and execute contracts. The Board is comprised of participant members as well as members appointed by the Governor of Hawaii.

Commonwealth of Pennsylvania – The State Employees' Retirement Board has the authority to amend the Plan and execute service and investment provider contracts. The Board is comprised of State Representatives and State Senators as well as other members appointed by the Governor of Pennsylvania.

State of Wisconsin – The Wisconsin Deferred Compensation Board has sole authority to administer and amend the Plan as well as execute contracts with investment and service providers. The five-person Board is wholly appointed by the Governor of Wisconsin.

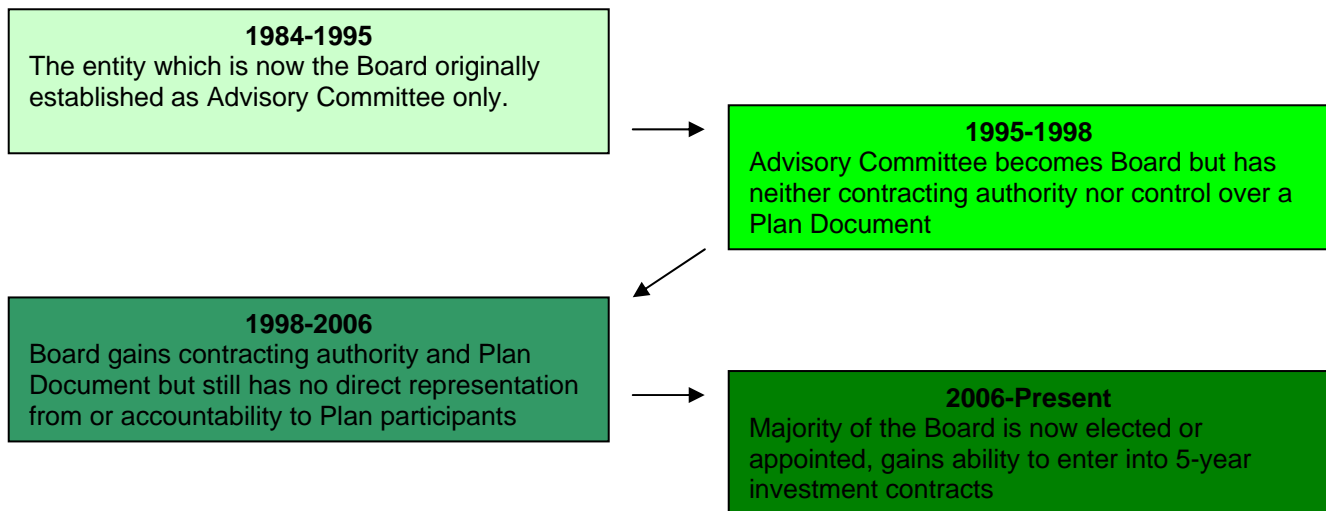
State of Washington – The Deferred Compensation Plan is administered by the Director of the Department of Retirement Systems, who is appointed by the Governor of Washington. The Director has the authority to administer and amend the Plan, however, the State Investment Board, located within the Treasury Department is delegated with selecting investment service providers.

What became clear from staff's review is that attempting to compare one oversight entity's "independence" vs. another's is challenging at best. Different entities have discretion in different areas. So, as an example, while in L.A. City only the Board can amend the Plan Document, in the City of Chicago only the Chicago City Council can do so. While in L.A. City the Council has veto authority over all Board decisions, in New York City, Maryland, Pennsylvania, Wisconsin, and Washington, a political entity (the Mayor or Governor) has a much more direct role by actually appointing certain positions on the Board. While in L.A. City the Board has contracting authority, in Orange County the Board of Supervisors approves contracts. In addition, Oregon and Washington

separate the oversight authority of administration from the oversight authority of their Plans' investments.

From the inception of the City's Deferred Compensation Plan, an ongoing challenge has been to better insulate the decision-making process from "political" pressures. Political pressures might be thought of as any consideration not strictly aligned with what is in the best interests of Plan participants.

The graphics below outline the evolution of the Board's role and powers over time:



From 1983 through 1999 political pressures manifested both internal and external to the Board, with the more consequential results coming externally. As a result, entities representing Plan participants moved to provide the Board with much greater independence and insulation. In 2004, however, political pressures manifested much more significantly within the Board, and it was the City Council that checked an outcome that did not appear to be aligned with the best interests of Plan participants.

The result is a Board that now has greater accountability to Plan participants, even while retaining its fairly broad independence. The only limitation on Board discretion is the Council veto authority. However, staff believes that while the City Council, a political body, has the right to veto and remand decisions of the Board, this power actually provides participants with an important safety valve - immediate recourse should participants feel the Board has failed to act on their behalf. Even now with elections, certain potentially unpopular decisions (e.g. award of a contract, as happened in 2004) are not likely to be reversed through an electoral process, given the short window of time over which a contracting decision is made and the much wider window of time over which elections are administered. The Council, by contrast, can veto a decision before its implementation becomes intractable.

Given that the Board has broad administrative authority over the Plan, including the ability to make Plan amendments and execute contracts, and given that the City Council's veto power is limited to its ability to remand, rather than take jurisdiction of, decisions of the Board, staff believes that the present system compares favorably to those utilized in the plans we surveyed.

Having said this, improvements can always be made. As Mercer indicated in its report, greater clarity within certain veto scenarios may be desirable. For example, it is not clear what would happen in a situation where the Council vetoes a Board decision and the Board reaffirms its decision, the Council re-vetoes and the Board again reaffirms, and the cycle repeats itself indefinitely. If the Board is interested in pursuing this type of relatively modest refinement of the existing rules, it may be best to do so in the context of other adjustments to the Administrative Code if and when such adjustments are warranted.

Plan Document Amendments

In the January 5, 2011 Memo, Mercer indicated that the Plan should consider adding more clarity in documentation regarding Plan amendments. Mercer has explained that Section IX of the Plan Document grants the Board the power to amend the document at any time "consistent with applicable law and consistent with the governing provisions of the Plan as contained in the City of Los Angeles Administrative Code." However, Administrative Code Section 4.1409 broadly states that the Plan may be amended or terminated by "the City", which is defined as "all offices, bureaus, and departments of the City of Los Angeles and includes therein departments which have control of their own definite revenues."

To address this ambiguity, the Administrative Code could be amended to specify the Board's authority to amend the Plan. However, staff recommends that a more practical solution would be to amend Section IX of the Plan Document as follows (changes are in bold):

"Pursuant to section 4.1409 of the Administrative Code, the Board has the full authority to act on behalf of the City to amend the Plan Document at any time, consistent with applicable law and consistent with the governing provisions of the Plan as contained in the City of Los Angeles Administrative Code."

Accountability Chart

Mercer had recommended that the Plan develop an accountability chart or similar document to clearly define roles and responsibilities for important functions of the Plan. Since receiving the Memo, the Plan has adopted the Bylaws/Governance Policies document, which clearly specifies the duties and responsibilities of the Board, staff, Board Counsel, and the Board Committees. However, staff recommends that the Board adopt the attached accountability chart as a new "Appendix D" of the Bylaws/Governance Policies since it provides a summary of the roles and functions of not only the Board and staff, but also those of the Plan's consultant and third-party-administrator.

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