

**RESEARCH AND ANALYSIS SECTION – LEGISLATIVE REFERENCE BUREAU**

**EXECUTIVE SUMMARY: 2007 Budget Summary Deferred Compensation Plan**

1. The 2007 Deferred Compensation Plan's Proposed Budget of \$1,407,283 increases slightly (\$3,564) from the 2006 Budget. The Plan's 2007 Proposed Budget includes \$1,096,000 for Professional Services, primarily related to services such as the third party administrator, equity option advisor fees, record keeping, and other account maintenance activities. (Pages 1 & 2)
2. As of December 31, 2005, there were a total of 7,740 participants in the Plan. Approximately 68% of current eligible employees participate in the Plan. At year-end, there were 5,313 participants actively deferring into the Plan and 2,427 retired plan members. (Page 3)
3. The value of the entire plan, as of December 31, 2005, was approximately \$507.7 million. As of June 30, 2006, the Plan's valuation was \$528.9 million. As of August 30, 2006, the Plan's valuation had increased to approximately \$530.3 million. (Page 4)
4. For 2006, Plan participants are able to defer salary up to \$15,000 of their salary. (Page 4)
5. The Plan is also offering participants, on a quarterly basis, two newly developed, customized workshops, "Countdown To Your Retirement" and "3 Steps to Plan Your Retirement Income". (Page 5)

## DEPARTMENTAL BUDGET SUMMARY: DEFERRED COMPENSATION PLAN

Expense Category	2005 Actual	2006 Budget	% Change	2007 Proposed	% Change
Total Expenditures	\$ 951,036	\$ 1,403,719	48%	\$ 1,407,283	0%
Capital	\$ -	\$ -	0%	\$ -	0%
Positions	2	2	0%	2	0%

The administrative costs of the Deferred Compensation Plan are offset by charges to Plan participants. **This budget has no tax levy impact.**

### Historical Information

1. The City's Deferred Compensation Plan (DCP) started in October 1974 and is available to all City employees. The plan is administered by a nine member Deferred Compensation Board consisting of the Mayor, Chair of the Finance and Personnel Committee, City Attorney, City Comptroller, City Treasurer, Employee Relations Director, and three appointed plan participants. Mayoral appointments to the Board consist of one management and one non-management employee. The Common Council President appoints one non-management employee. The Board is responsible for all discretionary decisions in the administration of the plan. An Executive Director, who makes policy recommendations regarding investment portfolio management, plan marketing, and participant education strategies, assists the Board.
2. The Deferred Compensation Plan, which was previously staffed by positions located in the Comptroller's Office, became a separately identified budget control unit in 1996.
3. In late 1996, the Federal Government approved the Small Business Protection Act. The legislation improved the relative value of s. 457 plans with respect to other qualified defined contribution plans (i.e., 401 k) and similar tax-deferred arrangements. The legislation required plan assets to be held in trust separate from the employer's assets for the exclusive benefit of the plan's participants and their beneficiaries.
4. In 1998, the Common Council approved a charter ordinance that shifted the Plan's 5 assets to a separate trust account on January 1, 1999, as required by the Small Business Protection Act. This shift protects the assets of individual members from being subject to bankruptcy or other legal action. The Plan currently utilizes a Plan Custodian (Bank) to administer the distribution of benefits, as is required by the law.

### 2007 Proposed Budget

1. The 2007 Deferred Compensation Plan's Proposed Budget of \$1,407,283 increases slightly (\$3,564) from the 2006 Budget. The Plan's 2007 Proposed Budget includes \$1,096,000 for Professional Services, primarily

related to services such as the third party administrator, equity option advisor fees, record keeping, and other account maintenance activities.

- **Third Party Administrator (TPA) (\$577,101)** – This is a \$47,899 increase from the \$577,101 included in the 2006 Adopted Budget. The increase is based on an increase for marketing and monitoring of the asset allocation plan model and a cost of living adjustment included in the TPA contract with National Retirement Solution (NRS). The contract expires in 2008 with 2 options for 1-year renewals.
- **Stable Value Account Manager (\$95,000)** – This is a \$2,111 increase from the \$92,889 included in the 2006 Adopted Budget for management fees of the Stable Value Account (STV) option. The increase is due to an increase in the account's valuation that has an effect on contract payments. The contract with Gartmore Morley Capital Management Inc. expires on June 30, 2008.
- **Active Managed Equity Account Manager (\$98,000)** – This is approximately the same amount that was included in 2006 Budget for the Managed Equity Account Manager. The increase is due to an increase in the account's valuation that has an effect on contract payments.

Lipper Advisory Services has full discretion to purchase and sell mutual funds in the Actively Managed Account, subject however to goals and guidelines that are from time to time approved by the Board. The contract with Lipper Advisory Services expires in 2010.

Other Professional Services line item expenditures include:

- **Insurance (\$100,000)** – This slight (\$2,000) increase from the amount provided in the 2006 Budget reflects an increase in the Plan's payment of insurance premiums for Active Managed Equity Account Manger's Errors and Omission Insurance Policy which was offset by lower premiums for the Plan's fiduciary insurance.
- **Plan Custodian (\$30,000)** - The Plan utilizes a Plan Custodian (Bank) to administer the distribution of benefits, as required by law. The same amount was provided in the 2006 Budget.
- **Audit (\$40,000)** – This amount is \$55,000 less than the amount provided in the 2006 Budget. In 2006, the scope of the audit contract was expanded and the funding in the 2006 Budget was based on an anticipated increase in the cost of the audit contract. The actual cost of the contract was significantly less than the funding provided in the 2006 Budget. The City Comptroller is an ex-officio member of the DCP Board, which is why an independent audit is required.

- **Travel (\$20,000)** -This funding allows all nine Board members and the Executive Director the opportunity to attend an educational seminar or conference. The passage of the Small Business Protection Act of 1996 requires plan assets to be held in trust for the exclusive benefit of the participant or their beneficiary effective January 1999. Because of this change, the Deferred Compensation Board has had an increase in their fiduciary responsibility. The \$20,000 included in the 2007 Proposed Budget is the same amount that was provided for in 2006 Budget.

### Other Line Items

1. **Reimbursements of Other Departments (\$30,000)** - This is the same amount that was included in the 2006 Adopted Budget. This account represents expenditures related to reimbursements for services provided by the City Attorney, Treasurer, and Comptroller.
2. **Contingent Fund (\$75,000)** - The same amount was included in the 2006 Budget. As of September 1, 2006, the Contingent Fund had not been used. The Deferred Compensation Plan budget is offset by revenue collected from member fees. Because government accounting regulations do not allow the City to "net budget" if the Plan under-estimates its costs, the Contingent Fund is the only source of additional revenue. The purpose of the DCP Contingent Fund is to provide contingent expenditure authority that can be repaid by participant charges. If no additional funding (over budget) is required, members will not be charged any additional fee.

### Plan Valuation and Participation

1. The Plan currently offers seven investment options. These options include a stable value fund, an active equity fund, a U.S. passive equity fund, an international passive equity fund, an income (bond) fund, and a balanced socially responsible fund. A fund-of-funds investment approach is utilized, whereby participant selection of an option actually results in investment among multiple funds with similar goals. In March of 2002, the Deferred Compensation Board added a seventh investment option; a Charles Schwab & Co. administered Personal Administered Retirement Account. The self-directed account provides participants with greater investment flexibility and options.

The Plan has not offered any new investment options in 2006 and at this time, does not anticipate additional options in 2007.

2. As of December 31, 2005, there were a total of 7,740 participants in the Plan. Approximately 68% of current eligible employees participate in the Plan. At year-end, there were 5,313 participants actively deferring into the Plan and 2,427 retired plan members. The average monthly cash deferral per-participant during the first quarter of 2005 was \$531.00.

3. The table on page 4 shows the number of participants and valuation performance for each of the plan's options as of June 30, 2006 and 2005 performance.

Option Name	# of Participants	Valuation (in millions)	2005 Performance
Stable Value	4,518	\$167.4	4.1%
Income Account	2,037	\$ 25.3	2.6%
Active Account	4,889	\$170.3	10.6%
Passive U.S. Account	4,271	\$92.2	6.2%
Passive International Account	3,622	\$45.3	15.4%
Social/Balance	1,845	\$16.3	3.8%
Self Directed	134	\$10.5	N/A
AUL (old)	123	\$1.7	N/A

4. The value of the entire plan, as of December 31, 2005, was approximately \$507.7 million. As of June 30, 2006, the Plan's valuation was \$528.9 million. As of August 30, 2006, the Plan's valuation had increased to approximately \$530.3 million.
5. The total Plan's 2006 proposed costs (\$1,407,283) represent less than 1/3 of one percent (0.26) of the Plan's present valuation. A study conducted by R.V. Kuhns & Associates of the Plan's peer group of deferred compensation fees showed the Plan's expenses were below the average cost of 0.50% basis points listed in the Deloitte Consulting 2004 Annual 401(k) Benchmarking Survey.

#### **s. 457 Legislative Impacts**

The Economic Growth and Tax Reduction Reconciliation Act (EGTRRA) of 2001 benefited Deferred Compensation participants. Under the Act the maximum contribution a Plan participant can make increased by \$1,000 each year from 2003 to 2006. After 2006, the maximum increase is indexed to the rate of inflation at \$500 increments. For 2006, Plan participants are able to defer salary up to \$15,000 of their salary.

The (EGTRRA) also provided enhancements to the catch-up provisions for plan participants who are 50 years or older and who may be eligible to use a catch-up provision allowing an extra \$4,000 contribution per year for a maximum contribution of \$18,000 in 2005. In 2006, the maximum catch-up limit is \$5000, for a total maximum contribution of \$20,000.

Instead of the age-50 catch-up provision, there is a limited catch-up provision, which can be used for any or all of the last three years prior to normal retirement age. Under this catch-up provision, a participant may be able to contribute twice the normal limit.

The 2002 Tax Relief Act provided a tax credit for low to moderate-income plan participants. The table on page 5 shows the amount of the credit and the income

limits. The credit applies to the first \$2,000 a participant contributes to the Plan. The tax credit provision expires in 2006.

Credit	Single Return	Head of Household	Joint Return
50%	0 - \$15,000	0-\$22,500	0 - \$30,000
20%	\$15,000 - \$16,250	\$22,501- \$24,375	\$30,000 - \$32,250
10%	\$16,250 - \$25,000	\$24,376 - \$37,500	\$32,250- \$50,000

The EGTRRA also provides portability to Plan participants. Dollars from a traditional IRA, 401(k) and a 403(b) can be rolled into the Plan and amounts distributed from the Plan can roll into a traditional IRA, 401(k) and a 403(b) plan. (Dollars rolled out of the Plan are subject to tax rules of the receiving plan.)

### **Plan Marketing**

In 2007, representatives from the Plan will continue to attend new employee orientations and meet with employees of departments that give permission to the Plan to give presentations. The Plan will also be using PeopleSoft queries to identify and reach the 30 percent of employees that are not enrolled in the Plan.

The Plan is also offering participants, on a quarterly basis, two newly developed, customized workshops:

#### **“Countdown To Your Retirement” “3 Steps to Plan Your Retirement Income”**

The “Countdown To Your Retirement” workshop will be tailored to meet the needs of those participants that are 1 to 10 years away from retirement and the “3 Steps to Plan Your Retirement Income” will be tailored to meet the needs of those participants that are within one year of retirement.

Both of these new workshops will be offered to Plan participants on an “Invitation” basis. The invitation will encourage married participants to have their spouse join them at the workshop as well as schedule a one-on-one meeting with the Plan’s “Retirement Income Management Specialist”. To further accommodate the attendees, the workshops will be offered in the evening, with refreshments provided, at various locations throughout the City.

In addition, the Plan will offer enhancements for the Plan’s retired participants by creating “Retiree” section within the Plan’s newsletter and website. A “Retirement Income Management Specialist” will also be available on a quarterly basis at the 735 N. Water Street NRS office for the purpose of meeting “one-on-one” with interested participants.

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