

Reply to Common Council File No. 100502  
From DOA-Budget and Management Division

October 5, 2010

Ref: 10004

Common Council File 100502 contains a substitute charter ordinance relating to the Employers' Reserve Fund.

On April 11, 2000, File 991585 enacted what is known as "The Global Pension Settlement," which took effect January 19, 2001. This legislation included the creation of an Employers' Reserve Fund. Voluntary employer contributions made by the city and city agencies for financing pension obligations are deposited into the Employers' Reserve and credited into accounts separate from those of the retirement system. The city may make withdrawals from the reserve through annual resolutions.

The purpose of the Employers' Reserve is to enable the city and city agencies to develop a reserve specifically for financing pension contributions. The nature of public pension financing can result in significant variations in the level of contributions required from one year to the next. As a result of the Global Pension Settlement, the Employees' Retirement System enjoyed a "funded ratio" (ratio of assets to liabilities on an actuarial basis) of more than 102%. Generally speaking, Chapter 36 requires employer contributions when the funded ratio is below 102% on an actuarial basis.

Current projections indicate that the ERS funded ratio, currently about 113%, will fall below 100% for the budget year 2013. These projections also indicate that, even if the ERS achieves its assumed rate of investment return each year, more than \$300 million of employer contributions will be required through budget year 2016. Therefore, the Administration has proposed through the 2011 Budget a voluntary contribution of \$17.35 million that will increase the Employers' Reserve balance. (The projected 2010 year-end balance is approximately \$10 million.)

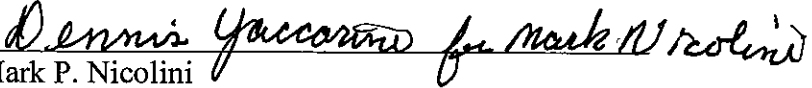
Currently, the Charter provides that the funds on deposit in each Employers' Reserve account shall be credited annually based on the earnings of the retirement system as a whole. Consequently, the Reserve is exposed to significant variation in investment return. This potential variation, and the accompanying risk of principal loss, is counter-intuitive to the notion of maintaining a reserve which is intended to help the city and city agencies deal with the financial consequences if the ERS funded ratio falls below 102%.

This substitute charter ordinance provides that the city's funds in the employers' reserve fund shall be invested in a manner consistent with guidelines approved by the common council and that the city shall bear any incremental costs associated with the administration or investment of the funds. The Department of Administration will propose these investment guidelines for consideration during the next Common Council cycle. These guidelines will prioritize Reserve principal preservation.

Discussions with ERS staff indicate that principal preservation is an achievable investment strategy objective for the Employers' Reserve; the tradeoff for the foreseeable future is likely to be very modest return on principal given current interest rates and projected fixed income financial market volatility. The return could be expected to increase when relatively more normal market conditions establish themselves.

In any event, prioritizing principal preservation stabilizes the financial planning environment for pension contributions and avoids the potential for substantial loss in principal when the need for withdrawals from the Employers' Reserve is most urgent. Finally, this substitute charter ordinance makes no change to the Annuity & Pension Board's status as the sole trustee for the investment of the System's funds.

**RECOMMENDATION: ADOPT COMMON COUNCIL FILE NUMBER  
100502, SUBSTITUTE 1**

  
Mark P. Nicolini  
Budget and Management Director

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