



THE CITY OF SAN DIEGO

OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

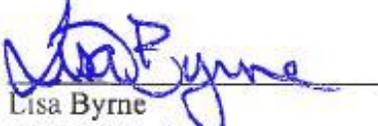
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Review of City Agencies FY 2018 Budgets: San Diego City Employees Retirement System

The IBA has reviewed the San Diego City Employees' Retirement System (SDCERS) proposed budget which is scheduled to be heard Tuesday, May 9th, 2017. Our review is attached.


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City Agencies: City Retirement System

City Retirement System

The San Diego City Employees' Retirement System (SDCERS) FY 2018 budget was approved by the SDCERS Board of Administration in March 2017. The SDCERS budget is scheduled to be presented as an informational item at the May 9, 2017 hearing of the City's Budget Review Committee.

SDCERS maintains that its budget is approved by its Board of Administration and does not require approval of City Council. Article XVI, Section 17 of the California Constitution conveys to the Board "plenary authority and fiduciary responsibility for investment of moneys and administration of the [pension] system..." Per City Attorney's Report to Council 2005-18, the City maintains the authority to examine and audit the Board's accounts

and records.

FY 2018 Operating Budget

The following table presents a summary, by major category, of the FY 2018 SDCERS budget; and budget highlights are discussed on the following pages. Additional details can be found in SDCERS' budget presentation materials.

SDCERS' FY 2018 budget of \$48.0 million is increasing by approximately \$1.0 million, or 2.2%, from the \$46.9 million FY 2017 budget. There are 50.00 budgeted positions, reduced from 54.00 in FY 2017. Note that approximately 7% of the budget is allocated to the other plan sponsors (the Unified Port District and Airport Authority), with the remainder to the City of San Diego.

SUMMARY OF BUDGET CHANGES					
	FY 2016 Actual	FY 2017 Budget	FY 2018 Budget	Increase/ (Decrease)	Percent Change
Budgeted Staff	58.00	54.00	50.00	(4.00)	(7.4%)
<u>Administrative Expenses</u>					
Salaries and Personnel	\$7,234,000	\$7,500,000	\$7,448,000	(\$52,000)	(0.7%)
Information Technology	1,824,000	1,974,000	2,050,000	76,000	3.9%
Legal/External	758,000	550,000	411,000	(139,000)	(25.3%)
General Operations	<u>3,661,000</u>	<u>3,541,000</u>	<u>3,368,000</u>	<u>(173,000)</u>	<u>(4.9%)</u>
<i>Subtotal Administrative Expenses</i>	<i>\$13,477,000</i>	<i>\$13,565,000</i>	<i>\$13,276,000</i>	<i>(\$288,000)</i>	<i>(2.1%)</i>
<u>Investment Management Expenses</u>					
Equity & Fixed Income	\$13,328,000	\$14,934,000	\$14,438,000	(\$496,000)	(3.3%)
Real Estate	9,939,000	10,329,000	11,322,000	993,000	9.6%
Private Equity & Infrastructure	6,239,000	6,707,000	7,677,000	970,000	14.5%
Other	<u>1,169,000</u>	<u>1,400,000</u>	<u>1,259,000</u>	<u>(141,000)</u>	<u>(10.1%)</u>
<i>Subtotal Investment Mgmt. Expenses</i>	<i>\$30,675,000</i>	<i>\$33,370,000</i>	<i>\$34,696,000</i>	<i>\$1,326,000</i>	<i>4.0%</i>
TOTAL	<u>\$44,152,000</u>	<u>\$46,935,000</u>	<u>\$47,972,000</u>	<u>\$1,038,000</u>	<u>2.2%</u>

Table may not total due to rounding.

City Agencies: City Retirement System

Investment Management Expenses

The FY 2018 Investment Management Expenses budget is increasing from the FY 2017 budget by \$1.3 million, or 4.0% (from \$33.4 million to \$34.7 million). The largest contributing factors to this increase are increased real estate and private equity investments.

At \$34.7 million, Investment Management Expenses represent 72% of SDCERS' FY 2018 operating budget. SDCERS estimates that Investment Management Expenses will be 0.46% of assets under management, or 46 basis points, for FY 2018. SDCERS also projects Investment Management Expenses to be 0.43% of assets under management for FY 2017.

The most recent SDCERS CAFR indicates FY 2016 investment return was 1.1%—with net investment earnings of approximately \$69.7 million. Note that the pension system's rate of return assumed for FY 2016 (in the FY 2015 actuarial valuation) was 7.125%.

SDCERS target asset allocation is as follows:

- U.S. Fixed Income—22%
- U.S. Equity—21%
- Non-U.S. Equity—14%
- Private Equity/Infrastructure—13%
- Real Estate—11%
- Opportunity Fund—8%
- Global Equity—5%
- Emerging Market Debt—5%
- Emerging Markets Equity—1%

SDCERS' Investment Policy Statement,

which explains its investment philosophy, and goals, asset allocation policy, and implementation and monitoring efforts can be found at the following link: <https://www.sdcers.org/Investments/Overview/Policy.aspx>

Administrative Expenses

Budgeted Administrative Expenses are decreasing by \$288,000, or 2.1%, from \$13.6 million in FY 2017 to \$13.3 million in FY 2018. These expenses are approximately 28% of the total SDCERS operating budget; and they are charged to the plan sponsors, including the City, with the Actuarially Determined Contribution (ADC) pension payment. Components of Administrative Expenses are outlined below.

Salaries and Personnel

The \$7.5 million Salaries and Personnel budget category reflects a decrease of \$52,000. Of this, the decrease in salaries and wages is \$165,000, which is offset with a \$113,000 increase in fringe benefits. With the implementation of the Integrated Retirement Information System (IRIS)¹, there have been operational efficiencies; and SDCERS has been able to reduce the number of budgeted positions through attrition, from 58.00 FTE positions in FY 2016, to 54.00 in FY 2017, and finally 50.00 in FY 2018.

There are no general salary increases budgeted, and the labor terms that apply to City employees also apply to SDCERS employees. Note that the City manages the payment of SDCERS employees' salaries and fringe, and invoices SDCERS for those

¹The pension administration system (IRIS) was placed in service at the end of FY 2014. The system tracks, records, and processes employee contributions and retiree payments. IRIS has online features and information about individual retirement benefits through the online Member Portal. Additionally, several internal processes are now automated.

City Agencies: City Retirement System

costs.

FY 2018 fringe benefits costs are anticipated to be higher than budgeted. Because FY 2018 fringe rates were not available at the time of SDCERS Board approval, the lower FY 2017 fringe rates were incorporated into the FY 2018 budget.

Non-Personnel Expenditures

The \$2.1 million Information Technology budget for FY 2018 is increasing by \$76,000 from FY 2017—which is largely due to contractual increases for the pension system and other technical support.

The \$411,000 Legal/External budget category reflects a decrease of \$139,000. This is primarily attributable to a decrease in estimated legal fees for tax matters and fiduciary counsel.

For the \$3.4 million General Operations budget, there is a net decrease of \$173,000. The largest change is an \$88,000 decrease in fiduciary insurance costs, which are budgeted at \$300,000 for FY 2018.

There are a couple consulting projects of note related to the FY 2017 General Operations budget.

- A pension system administration benchmarking study, completed in January 2017, which can be found at the following link: <https://board.sdcers.org/sirepub/cache/2/uocplqioocdx4cgvjpsbvlw/13139605042017034416865.PDF>
- An information technology risk assessment, which is currently underway

Capital Budget

In addition to the operating budget, SDCERS maintains a capital budget. The capital budget is increasing from \$100,000 in FY 2017 to \$289,000 in FY 2018.

Estimated expenditures in FY 2017 include \$30,000 in computer hardware replacements. Additionally, there is a potential upcoming expenditure related to the Storage Area Network (SAN), which houses SDCERS' data. The cost for replacement of the SAN is anticipated to be approximately \$125,000.

New projects budgeted for FY 2018 include:

- A board agenda and voting system upgrade—\$75,000 (This was delayed from the FY 2017 budget.)
- Core Network Switch replacement for management of network traffic—\$150,000
- Computer hardware replacements—\$25,000
- Accounting software upgrade—\$25,000
- SDCERS website redesign—\$14,000