



THE CITY OF SAN DIEGO

OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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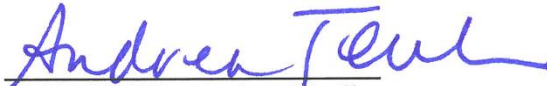
IBA Report Number: 16-07

Budget Review Committee Docket Date: May 10, 2016

Review of City Agencies FY 2017 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 10th, 2016. 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 2017 budget was approved by the SDCERS Board of Administration in mid-March 2016. The City's FY 2017 Proposed Budget document provides a link to the SDCERS budget on page 203 of Volume I.

The SDCERS budget is scheduled to be presented as an informational item at the May 10, 2016 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.

SUMMARY OF BUDGET CHANGES					
	FY 2015	FY 2016	FY 2017	Increase/	Percent
	Actual	Budget	Budget	(Decrease)	Change
Budgeted Staff	58.00	58.00	54.00	(4.00)	-6.90%
<u>Administrative Expenses</u>					
Salaries and Personnel	\$7,415,000	\$7,671,000	\$7,500,000	(\$172,000)	-2.2%
Information Technology	1,883,000	1,942,000	1,974,000	32,000	1.6%
Legal/External	362,000	978,000	550,000	(427,000)	-43.7%
General Operations *	3,681,000	3,645,000	3,541,000	(104,000)	-2.9%
Subtotal Administrative Expenses	\$13,342,000	\$14,236,000	\$13,565,000	(\$671,000)	-4.7%
<u>Investment Management Expenses</u>					
Equity & Fixed Income	\$16,526,000	\$15,250,000	\$14,934,000	(\$316,000)	-2.1%
Real Estate	7,043,000	12,698,000	10,329,000	(2,370,000)	-18.7%
Private Equity & Infrastructure	5,124,000	5,377,000	6,707,000	1,330,000	24.7%
Other	1,209,000	1,178,000	1,400,000	222,000	18.8%
Subtotal Investment Mgmt. Expenses	\$29,902,000	\$34,503,000	\$33,370,000	(\$1,133,000)	-3.3%
TOTAL	\$43,244,000	\$48,739,000	\$46,935,000	(\$1,805,000)	-3.7%

Table may not total due to rounding.

* For comparison purposes, the amount for FY 2015 General Operations has been increased in the table above by \$2.1 million from the FY 2015 actual amount provided by SDCERS. This increase removes a \$2.1 million reduction in FY 2015 expenses related to an accounting change associated with the Net Pension Obligation. Removal of this one-time, \$2.1 million expense reduction allows an easier comparison of the remaining FY 2015 expenses with FY 2016 and FY 2017.

City Agencies: City Retirement System

FY 2017 Operating Budget Adjustments

The table on the previous page presents a summary, by major category, of the FY 2017 SDCERS budget that was approved by its Board in March 2016.

The \$46.9 million FY 2017 budget presented to the SDCERS Board shows a decrease of approximately \$1.8 million, or 3.7%, from the \$48.7 million FY 2016 budget. There are 54.00 budgeted positions, reduced from 58.00 in FY 2016. Note that approximately 7% of the budget is allocated to the Unified Port District and Airport Authority, with the remainder to the City of San Diego.

Investment Expenses

Investment Management Expenses represent 71% of the total SDCERS FY 2017 operating budget, at \$33.4 million. SDCERS estimates that Investment Management Expenses will be 0.44% of assets under management, or 44 basis points, for FY 2017. SDCERS also projects Investment Management Expenses to be 0.43% of assets under management for FY 2016. Note that the most recent SDCERS CAFR indicates that for FY 2015, investment returns were lower than the 7.25% assumed rate of return for the pension system, at 3.3%—with net investment earnings of approximately \$224.1 million.

The FY 2017 Investment Management Expenses budget is decreasing from the FY 2016 budget by \$1.1 million, or 3.3% (from \$34.5 million to \$33.4 million). The largest contributing factor to this decrease is a reduction in estimated real estate fees, which

is partially offset with increases in private equity and infrastructure fees, largely due to the acquisition of a new private equity series.

Administrative Expenses

Budgeted Administrative Expenses are decreasing by approximately \$671,000, or 4.7%, from \$14.2 million in FY 2016 to \$13.6 million in FY 2017. These expenses are approximately 29% of the total SDCERS operating budget. Components of Administrative Expenses are discussed below.

The \$7.5 million Salaries and Personnel budget category reflects a decrease of \$172,000. Of this, the decrease in salaries is \$136,000. With the implementation of the Integrated Retirement Information System (IRIS), there have been operational efficiencies; and SDCERS has been able to reduce the number of budgeted positions through attrition, from 58.00 to 54.00 FTEs

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 costs.

The \$2.0 million Information Technology budget for FY 2017 is increasing by \$32,000 from FY 2016. This is largely due to contractual support increases for the pension system and other technical support.

The \$550,000 Legal/External budget category reflects a decrease of \$427,000. This is primarily attributable to a decrease in esti-

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mated litigation fees related to Purchase Service Credit (PSC) litigation, for which work is expected to be significantly reduced. In late March, the Court of Appeal affirmed the Superior Court's rulings in favor of SDCERS for four of the five related lawsuits. The fifth lawsuit will be returned to the Superior Court for additional proceedings.

For the \$3.5 million General Operations budget, there is a net decrease of \$104,000. The largest changes include \$100,000 decrease in actuary services related to the experience study that is to be completed in FY 2016; \$52,000 decrease in fiduciary insurance costs; and \$86,000 increase in office operations expenses. The increase for office operations is related to an electronic filing and scanning project for which temporary labor is needed, as well as funding for a pension system benchmarking study.

Further details on budget changes can be found in the SDCERS budget presentation materials.

Capital Budget

In addition to the operating budget, SDCERS maintains a capital budget. The

capital budget is increasing from \$90,000 in FY 2016 to \$100,000 in FY 2017.

Completed projects and expenditures for FY 2016 include:

- Payments for the final phase of the pension administration system replacement project¹ are projected to be \$140,000
- Payments for the call center voice monitoring and recording system are projected to be \$17,000
- Payments for the board room high definition video upgrade are projected to be \$250,000²

New projects budgeted for FY 2017 include a SIRE board agenda and voting system upgrade (\$75,000) and computer hardware replacements (\$25,000).

¹The pension administration system replacement project was a major software system conversion: from the Pension Gold system to the Integrated Retirement Information System (IRIS). IRIS was placed in service on May 29, 2014. Total vendor costs for the project are approximately \$6.8 million. Most of the final payments were made by FY 2015; and a portion of the final hold-back payment was rescheduled for FY 2016.

The pension administration system tracks, records and processes employee contributions and retiree payments. IRIS has new online features and information about individual retirement benefits through the online Member Portal. Additionally, several internal processes are now automated.

²Funding for the \$250,000 high definition video upgrade is provided through the City of San Diego and derived from Public, Educational, and Governmental Access (PEG) funds—from 1% surcharges on cable services.