

# *City of Alexandria, Virginia*

## MEMORANDUM

DATE: FEBRUARY 26, 2009

TO: THE HONORABLE MAYOR AND MEMBERS OF CITY COUNCIL

FROM: JAMES K. HARTMANN, CITY MANAGER

SUBJECT: BUDGET MEMO # 14 : AN EXPLANATION OF THE ADMINISTRATIVE COMPONENTS OF THE PENSION ADMINISTRATION PROGRAM IN THE FINANCE DEPARTMENT

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This is in response to a query from Council Member Wilson regarding the City's Pension Administration Program, specifically which components are in-sourced and which ones are out-sourced.

Out-sourced activities primarily include investment advisory and custodial services, legal expenses, actuarial valuation support, and benefits payment administration. The investment advisory services relate to professional independent financial advisory services for pension investment funds. Legal expenses generally relate to plan technical compliance review with the complex Federal IRS tax code and other federal tax regulations. Actuarial valuation support is primarily for the independent valuation required for the financial audit. Benefits payment administration relates to making benefit calculations, including cost of living adjustments, and maintaining participant statements and support. Additional legal expenses have been incurred when changes in the plan have been requested and analyzed. In house activities include all training, communication, retirement processing, staffing and supporting retirement and other post employment benefits boards, and counseling employees.

The primary focus for out-sourced items is when independent assessment and verification is either prudent or required. Given the size of the assets and the fiduciary responsibility the City has for these investments, it is generally prudent and considered a best practice to have outside professional advice. Most outside legal expenses are incurred when there are legal questions that are quite specific to the plan. Most actuarial costs are now related to a required external valuation for both pensions and other post-employment benefit costs. Other costs include complex cost analyses, such as those prepared for a potential public safety buyback option several years ago.

Federal pension laws provide guidelines for what costs can be considered the cost of the fund and what costs are considered employer costs that must be funded by the City. In general, costs that are paid to administer and maintain the current plan can be charged to the pension fund. These costs would include routine actuarial valuations, investment advice, training for board members, and legal costs for maintaining the funds' tax status. Costs that consider changes to

the plan or benefit structure are considered to be the responsibility of the plan sponsor and would be paid by the General Fund. Examples of these costs include costs associated with technical and financial evaluation of a proposed change to the pension, and the cost for legal assistance to draft a proposed plan amendment that changes benefits.

At this time it is proposed that all currently out sources pension services continue to be out sourced. However, over the long term, City staff will be looking to other models of benefits payment administration.

It is the norm to charge these outside costs, as well as internal administrative costs, to a pension plan. The City's long standing practice has been not to charge the plans with these administrative costs. Starting in FY 2010 it is proposed to change this practice so that those costs are allocated and charged to the City's various pension plans. While this reduces the Finance Department's costs, there will be an equal cost increase to the pension plans that will be calculated back into the employer's share rate charge by each plan to the various pension plans in the various department budgets.