



**SAN DIEGO CITY EMPLOYEES' RETIREMENT SYSTEM  
STAFF REPORT  
FINANCE DIVISION**

**DATE:** February 26, 2015  
**TO:** BUSINESS AND GOVERNANCE COMMITTEE  
**FROM:** Ted LaSalvia, Controller  
**SUBJECT:** Presentation of the FY 2016 SDCERS Budget

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**Summary**

The SDCERS' FY 2016 proposed budget demonstrates a continued emphasis on support and resources for the business, yet balanced with prudent cost controls.

- Administrative expenses in FY 2016 are budgeted at \$14.2 million
  - Down \$0.2 million (1.6%) from the FY 2015 budget
  - Up \$0.6 million (4.1%) from the FY 2015 projection
- Investment Management expenses in FY 2016 are budgeted at \$34.5 million
  - Up \$2.2 million (6.7%) from the FY 2015 budget
  - Up \$2.7 million (8.5%) from the FY 2015 projection
- Total proposed FY 2016 spending is \$48.7 million
  - Up \$2.0 million (4.2%) from the FY 2015 budget
  - Up \$3.3 million (7.2%) from the FY 2015 projection

The decrease of \$0.2 million in Administrative expense over the FY 2015 budget is primarily due to decreases in outside legal fees, salary fringe costs, and fiduciary insurance. The \$0.6 million Administrative expense increase over the FY 2015 projection is primarily due to increases in outside legal counsel associated with ongoing purchase service credit litigation, and salaries for positions that were open for much of FY 2015.

FY 2016 Investment Management expenses are projected to increase over the FY 2015 budget and FY 2015 projection primarily due to the increases in assets under management, and incremental investments in real estate. The FY 2016 basis points for the portfolio are 46 bps compared to the FY 2015 projection of 47 bps. The FY 2016 decrease in basis point is due to a more favorable fee structure in private equity.

Below is a summary comparison of the FY 2016 Proposed Budget compared to the FY 2015 Budget and FY 2015 Projection, and a discussion of each category (amounts are subject to rounding and may not sum):

(In millions)

Category	FY 2015 Budget	FY 2015 Projection	FY 2016 Budget	Increase/ (Decrease) to FY 2015 Budget	Increase/ (Decrease) to FY 2015 Projection
Administrative Expenses	\$14.5	\$13.7	\$14.2	\$(0.2)	\$0.6
				(1.6)%	4.1%
Investment Management Expenses	\$32.3	\$31.8	\$34.5	\$2.2	\$2.7
				6.7%	8.5%
Total	\$46.8	\$45.5	\$48.7	\$2.0	\$3.3
				4.2%	7.2%

**Administrative Expenses**

1. Salaries and Personnel

The total cost for salaries and benefits is projected to decrease \$171,000 (2.2%) from the FY 2015 budget and increase \$322,000 (4.4%) from FY 2015 projection. Fringe expense accounts for \$219,000 and \$36,000 of the decrease over the FY 2015 budget and FY 2015 projection, respectively. The fringe expense of \$3.0 million is a pass through cost from the City primarily composed of pension benefits, health benefits, taxes and changes in the City’s FY 2016 ADC payment and may change based upon the completion of City’s annual budget. FY 2016 salaries have increased by \$45,000 (1.0%) over the FY 2015 budget and increased \$357,000 (8.2%) over the FY 2015 projection.

The increase in projected-to-budget wages primarily reflects a fully staffed organization for FY 2016. With the implementation of the IRIS pension system, staff is expected to continue with follow-on enhancements, issue resolution, and completion of associated data conversion clean-up work. No provision has been made for a general salary increase. FY 2016 fringe rates may be adjusted by the City and any changes, if significant will be communicated to the SDCERS Board at the May Board meeting

The FY 2016 budgeted headcount is unchanged at 58 from the FY 2015 budgeted level of 58.

## 2. Information Technology

The FY 2016 budget for Information Technology decreased \$46,000 (2.3%) from the FY 2015 budget, and decreased \$37,000 (1.9%) from the FY 2015 projection. The \$37,000 decrease in the FY 2016 budget over the FY 2015 projection is primarily due to decreased pension system support contract costs of \$110,000 in FY 2016 as IRIS will be the solely supported pension system. This decrease is partially offset by increased Technical Support labor (i.e., outsourced contract work) for the IRIS system. FY 2016 Technical Support labor is on par with the FY 2015 budget and \$70,000 above the FY 2015 projection.

## 3. Legal/External

The outside Legal Budget of \$1.0 million is comprised of litigation counsel (\$600,000), fiduciary counsel (\$150,000), tax/general counsel (\$158,000), and disability counsel (\$70,000.) The FY 2016 budget has been reduced by \$174,000 (15.1%) from the FY 2015 budget, and increased \$358,000 (57.8%) from the FY 2015 projection. The Purchase Service Credit (PSC) litigation cases, although potentially resolved through summary judgment at the Superior Court, have been appealed and drive the expected costs in litigation expense. Litigation costs for appeal of the PSC litigation cases have been budgeted for the remainder of FY 2015, and FY 2016 budgeted amounts reflect the possibility of trial should the plaintiffs prevail on appeal. Projected outside fiduciary counsel costs are also included in the FY 2016 legal budget. The fiduciary budget is \$150,000, which reflects the retention of new fiduciary counsel with lower hourly rates. The budget for tax/general includes estimates for work related to Unified Port District's determination letter, and day-to-day tax questions. The FY 2016 budget for disability counsel increased from the FY 2015 budget by \$18,000 due to an increase in disability applications and anticipated hearing-related costs caused by that increase.

## 4. General Operations

The General Operations budget reflects an overall increase of \$165,000 (4.7%) from the FY 2015 budget, and an \$81,000 decrease (2.2%) from the FY 2015 projection. The increase in FY 2016 depreciation expense is due to having under-budgeted in FY 2015. The \$81,000 General Operations decrease from the FY 2015 projection is due to a decrease in fiduciary insurance renewal rates, decreased use of temporary labor, and lower forecasted audit services. The decrease is partially offset by the annual increase in rent and increased disability processing expenses related to increased investigations and exams.

## **Investment Management**

Investment management fees are budgeted based on the assets under management, the projected growth in the investment portfolio, and the investment of assets according to the allocations as approved by SDCERS' Board. The annual growth in assets under management is based on SDCERS' actuarially assumed rate of 7.25%. The asset growth projection is applied to the current contractual fee schedules of SDCERS' investment managers and is calculated on projected average assets of approximately \$7.2 billion for FY 2016.

FY 2016 Investment Management expenses are expected to increase over FY 2015 budget by 6.7% and over FY 2015 projection by 8.5%. The dollar increase is largely driven by new investments in Real Estate and new strategies in the Opportunity Fund. The FY 2016 basis points are 46 bps compared to the FY 2015 projection of 47 bps. The FY 2016 decrease in basis points is due to a more favorable fee structure in private equity.

Compared to the FY 2015 budget, Public Market fees are expected to increase by 9.4% due to new investments in the Opportunity Fund in the form of opportunistic real estate and an allocation to global credit investments. Real Estate fees increase by 30.2% due to the expected purchase of two properties in an existing fund and investment in three new real estate funds. Private Equity fees decrease 29.1% due to two factors: a slight decrease in fees due to the combination of Private Equity and Infrastructure investments, and a major decrease due to the negotiation of a new investment management fee structure. Investment Consulting fees are up 0.4% due to the negotiation of a fixed fee for an additional year of service on real estate consulting fees. Legal fees are down 33.3% as there is an expected decrease in activity for FY 2016.

Compared to the FY 2015 projected, Public Market fees increase by 10.0% due to new investments in the Opportunity Fund. Real Estate expenses are projected to increase by 9.6% based on the expectation that we will purchase two new properties and invest in three new funds. Private Equity fees are projected to be up 8.8% as the fee savings from the newly negotiated fee structure will only impact the expense for half the year. Infrastructure is projected to decrease 6.6% due to fewer miscellaneous expenses. Legal fees are projected to be lower by 48.9% due to less activity during the next fiscal year.

## **Capital Spending**

SDCERS' capital spending is projected at \$90,000 for FY 2016, a decrease of 92.3% from the \$1.2 million budgeted in FY 2015 and a \$1.0 million decrease from the FY 2015 projection. The decrease is due to the estimated completion of IRIS, the pension administration system replacement project. In FY 2016, projects include IRIS work and an upgrade to the SDCERS board room video.

## **Conclusion**

The FY 2016 budget reflects continued cost control over administrative overhead while providing the resources necessary for SDCERS to meet its mandated responsibilities.

Attachments: FY 2016 Expense Budget Proposal  
FY 2016 Capital Budget Proposal

# SAN DIEGO CITY EMPLOYEES' RETIREMENT SYSTEM

## EXPENSE BUDGET (in thousands)

REVISED

FISCAL YEAR 2015 BUDGET, FISCAL YEAR 2015 PROJECTED ACTUALS AND FISCAL YEAR 2016 PROPOSED BUDGET

	2015		2016		
	Budget	Projected	Proposed Budget	Increase (Decrease) to FY2015	
				Budget	Projected
<b>ADMINISTRATIVE EXPENSES</b>					
<b>Budgeted Staff</b>	<b>58</b>	<b>58</b>	<b>58</b>	-	-
<b>Salaries and Personnel</b>					
Salary <sup>1</sup>	\$ 4,639	\$ 4,328	\$ 4,685	\$ 45	\$ 357
Fringe <sup>1</sup>	3,170	2,987	2,951	(219)	(36)
Overtime	20	24	26	6	1
Recognition Program	13	10	10	(3)	(0)
<b>Total Salaries and Personnel</b>	<b>\$ 7,842</b>	<b>\$ 7,349</b>	<b>\$ 7,671</b>	<b>\$ (171)</b>	<b>\$ 322</b>
				-2.2%	4.4%
<b>Information Technology</b>					
Technical Support Labor	\$ 945	\$ 875	\$ 945	\$ -	\$ 70
Pension System Support	505	560	450	(55)	(110)
Network Services	152	155	157	6	3
Licensing and Support	150	150	150	-	-
Professional Services	95	97	97	2	-
Computer Hardware Supplies	102	101	101	(1)	-
Citywide Costs	40	42	42	2	-
<b>Total Information Technology</b>	<b>\$ 1,989</b>	<b>\$ 1,980</b>	<b>\$ 1,942</b>	<b>\$ (46)</b>	<b>\$ (37)</b>
				-2.3%	-1.9%
<b>Legal/External</b>					
Litigation	\$ 780	\$ 275	\$ 600	\$ (180)	\$ 325
Fiduciary	180	189	150	(30)	(39)
Disability	52	49	70	18	22
Legal Tax/General	140	107	158	18	51
<b>Total Legal/External</b>	<b>\$ 1,152</b>	<b>\$ 620</b>	<b>\$ 978</b>	<b>\$ (174)</b>	<b>\$ 358</b>
				-15.1%	57.8%
<b>General Operations</b>					
Rent	\$ 910	\$ 910	\$ 936	\$ 26	\$ 26
Fiduciary Insurance	496	473	440	(56)	(33)
Actuary Services	470	460	450	(20)	(10)
Office Operations Expenses	470	516	423	(48)	(93)
Depreciation Expense	683	882	899	216	17
Disability Processing	118	128	148	31	20
Audit Services	139	162	133	(6)	(29)
Retiree Health Counseling Services	97	97	97	-	-
Travel & Training	97	98	118	22	21
<b>Total General Operations</b>	<b>\$ 3,481</b>	<b>\$ 3,726</b>	<b>\$ 3,645</b>	<b>\$ 165</b>	<b>\$ (81)</b>
				4.7%	-2.2%
<b>TOTAL ADMINISTRATIVE EXPENSES</b>	<b>\$ 14,463</b>	<b>\$ 13,675</b>	<b>\$ 14,236</b>	<b>\$ (227)</b>	<b>\$ 561</b>
				-1.6%	4.1%
<b>INVESTMENT MANAGEMENT EXPENSES</b>					
<b>Management Fees</b>					
Equity & Fixed Income	\$ 15,154	\$ 15,064	\$ 16,577	\$ 1,422	\$ 1,512
Real Estate	8,731	10,377	11,371	2,640	994
Private Equity	5,894	3,844	4,182	(1,712)	338
Infrastructure	1,282	1,280	1,195	(87)	(85)
Consulting	712	701	715	3	14
Legal Fees	150	196	100	(50)	(96)
Custodial Banking Services	365	319	343	(22)	24
Software Applications	36	20	20	(16)	-
<b>TOTAL INVESTMENT MANAGEMENT EXPENSES</b>	<b>\$ 32,325</b>	<b>\$ 31,801</b>	<b>\$ 34,503</b>	<b>\$ 2,178</b>	<b>\$ 2,702</b>
				6.7%	8.5%
<b>GRAND TOTAL</b>	<b>\$ 46,788</b>	<b>\$ 45,476</b>	<b>\$ 48,739</b>	<b>\$ 1,952</b>	<b>\$ 3,263</b>
				4.2%	7.2%

<sup>1</sup> Investment Division salary and fringe costs of are included in Salaries and Personnel expense for budgetary purposes, but are reclassified as investment expenses on the Statement of Changes in Plan Net Position as required under GASB financial reporting standards.

**SAN DIEGO CITY EMPLOYEES' RETIREMENT SYSTEM**  
**CAPITAL EXPENSE BUDGET (in thousands)**

FISCAL YEAR 2015 BUDGET, FISCAL YEAR 2015 PROJECTED ACTUALS AND FISCAL YEAR 2016 PROPOSED BUDGET

	2015		Proposed Budget	2016	
	Budget	Projected		Incr. (Decr.) to FY 2015	
				Budget	Projected
Pension Administration System Replacement	\$1,100	\$984	\$40	\$(1,060)	\$(944)
Website Redesign	35	37	-	(35)	(37)
SAN Storage Space Expansion	20	19	-	(20)	(19)
Accounting Software System Update	20	22	-	(20)	(22)
Board Room HD Video Upgrade	-	-	50	50	50
<b>Total</b>	<b>\$1,175</b>	<b>\$1,062</b>	<b>\$90</b>	<b>(\$1,085)</b>	<b>(\$972)</b>