

**OFFICE OF THE CITY MANAGER  
DES MOINES, IOWA**

**CITY COUNCIL COMMUNICATION 96-478  
NOVEMBER 6 1996 AGENDA**

SUBJECT:	TYPE:	SUBMITTED BY:
DISCONTINUATION OF PLAN 60 DEFERRED COMPENSATION PLAN	◆ RESOLUTION ORDINANCE RECEIVE/FILE	ERIC A. ANDERSON CITY MANAGER

**FISCAL IMPACT —**

No additional cost.

**RECOMMENDATION —**

The Committee recommends that the City Council discontinue Plan 60 as of April 1, 1997. This action will require all participants to select some other available option for deferred income or to be placed in the default fund if they do not inform us of their selection. The recommended designation of the default fund will be returned to Council for final approval.

**BACKGROUND —**

Approximately 16 years ago, the City Council created Plan 60 as one of the choices for employees who wished to participate in the deferred compensation program made available under section 457a of the Internal Revenue Code. Currently, there are 1523 participants in Plan 60, of whom 442 are retired and 1081 are currently employed with the City. The market value of the fund is \$46,437,742.

The return on an investment in the fund has been good. Over the last ten years the average rate of return has been 9.58%. If you had invested \$10,000 in the fund in 1986, it would be worth \$25,350 today. This record is competitive with such benchmarks as Lehman Brothers Corporate High Yield Index, Lehman Brothers Aggregate Index, S & P 500 Stock Composite Index, Salomon Long term High Grade Corporation Index, and the 30 Year Treasury Index. All of these comparisons, including Plan 60, are at market value and are shown in the attached exhibits.

The monies in the Plan are currently, as required by federal law, an asset of the City until they are distributed to the participants in accordance with the provisions of the joinder agreement. The Plan is managed by one employee, who has done so from its inception. A committee is established in the plan document adopted by the City Council to oversee the management of the Plan. The committee is made up of a representative of the City Manager, a representative of the Finance Director, the Civil Service/Personnel Administrator, and a City Solicitor. The committee has reviewed the management of the Plan in light of new federal legislative changes that require us to use a trust to hold Plan assets no later than December 31, 1998, and with a view toward generally accepted accounting principles.

The Committee has concluded that the best interests of the City and the Plan participants are best served by elimination of Plan 60. The reasons are several.

First, and most important, we do not have the staff available to assure continued successful management of the fund. This is not a criticism, the committee unanimously notes, of Mr. Dean

Johnson, who has managed the fund from its inception. He has done an excellent job. However, he manages the fund alone, without backup, and has had one serious heart attack. The fund is large enough and important enough in the lives of the participants that the assurance of its professional management is a necessity. The cost of making this assurance is significant. The City cannot incur it without excessive charges to either the taxpayer or each participant.

Second, the federal law changes make management of the fund much more complex for the City. The fund becomes, on December 31, 1998, subject to regulations requiring Plan assets to be held in trust for the benefit of participants. Complying with these regulations increase the cost of managing the fund. Our costs of compliance will be inordinately large for each participant because the base across which the costs will be spread is relatively small (other funds in the private sector spread the same costs over a base that is many times larger).

Third, we are unable to provide participants with the kind of information they should have on a regular basis with a deferred compensation program of this kind. We do not have the staff available nor do we have the technology.

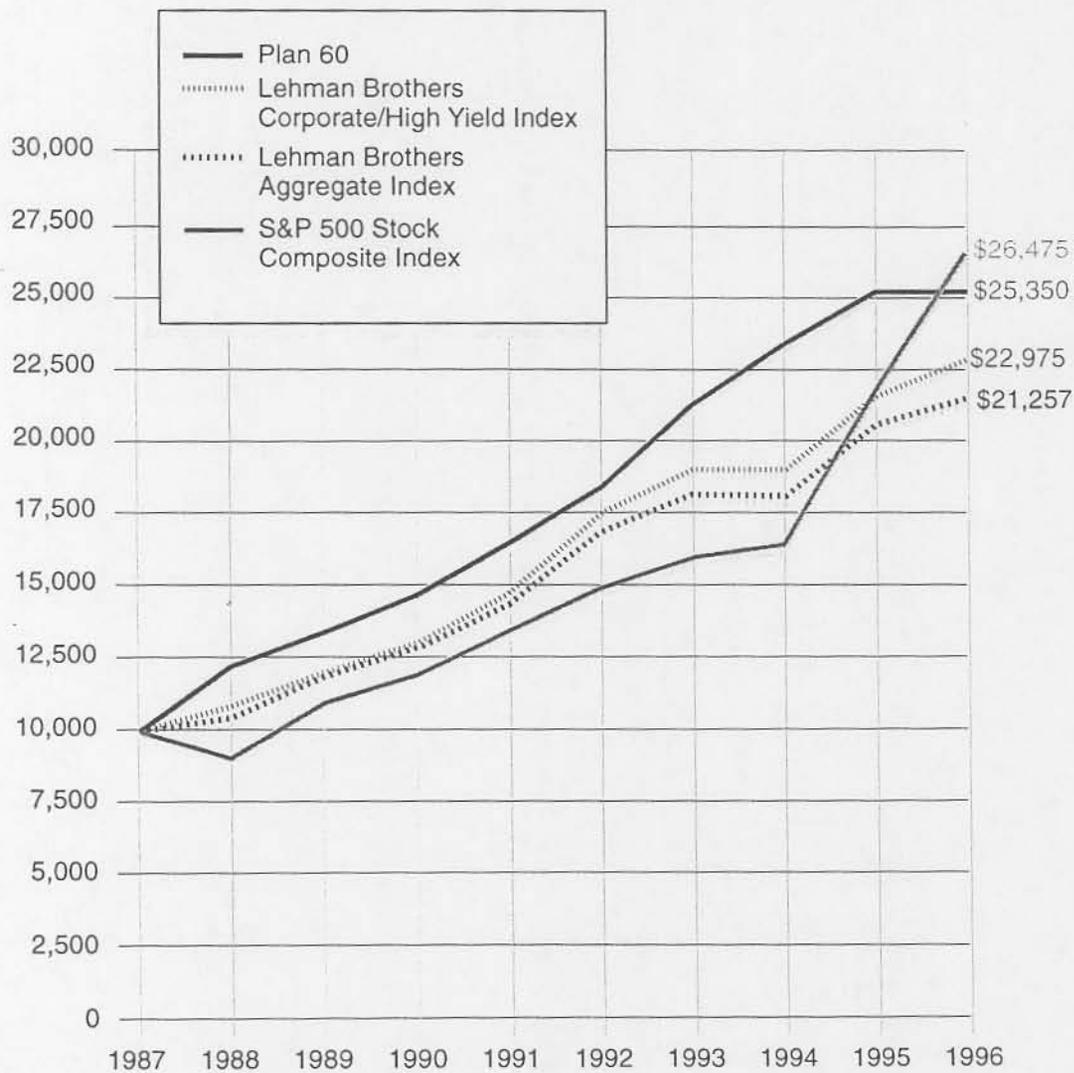
For example, since its inception, the fund has recorded earnings and value for each participant based upon the book value of the fund. We understand that at the beginning this was the best way to do this. However, with the size and complexity of the fund today, this is not the most appropriate way to record value. Technology allows us to be more accurate, using market value as of the end of each month. The committee unanimously voted to change the rules of the fund as of October 21, 1996 to record and report all values at the market value as of the end of each month. A separate report of this action is attached.

While this change has been made, there are other desirable improvements we are not able to make at this time because of the cost of the necessary technology and the availability of staff. Nor do we believe that we will be able to do so in the future without large cost to either the taxpayer or the participant.

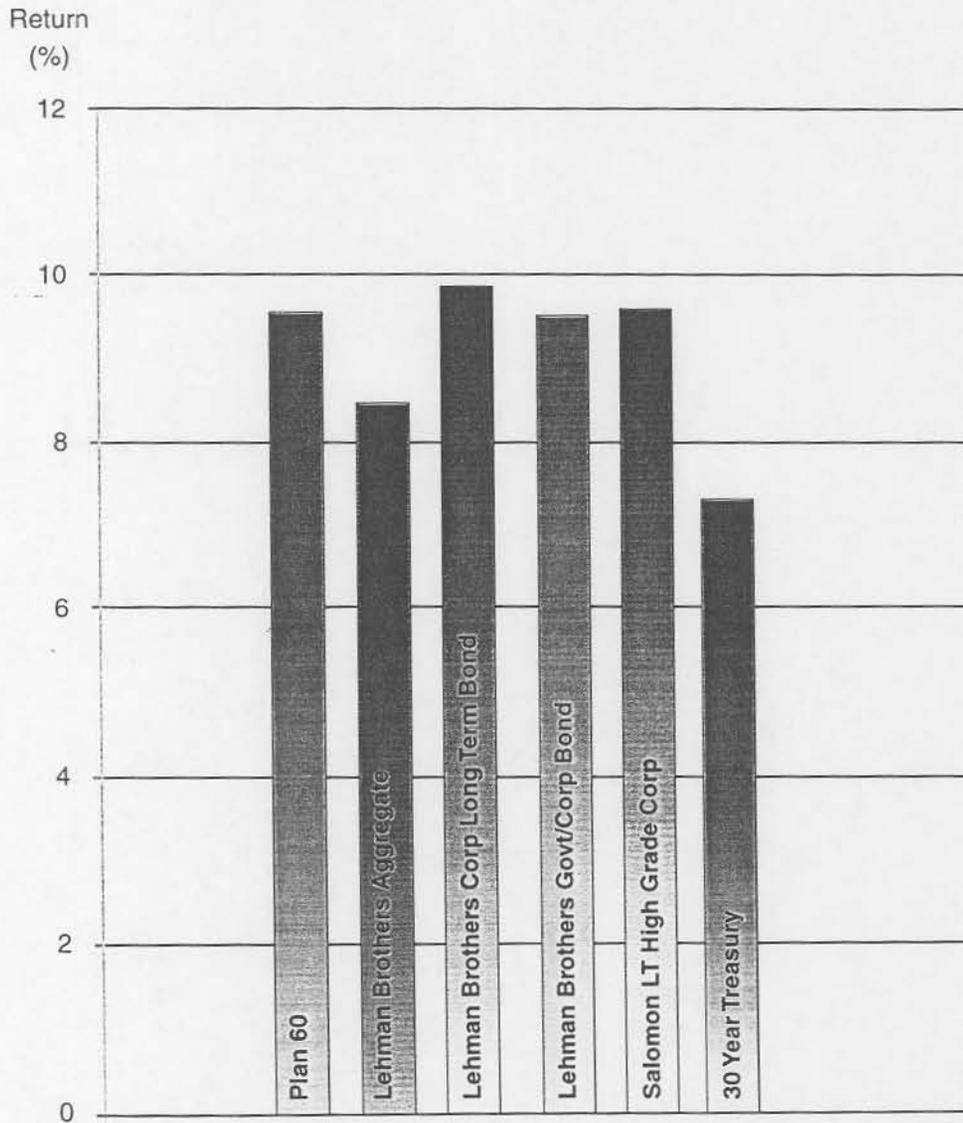
For these reasons, staffing, increased regulation, technology, and cost, we unanimously believe that Plan 60 should be discontinued as of April 1, 1997. We also believe that a fund should be selected as a "default" option for participants that do not notify the City of their choice of alternative investment. All participants should be given timely and adequate notice of the discontinuation of the Plan 60 and should be directed to make their choice of a replacement investment by March 1, 1997. The final selection of the "default" or City selected fund should be returned to Council for their approval by December 31, 1996.

Attachments

# COMPARISON OF CHANGE IN VALUE OF \$10,000 INVESTMENT OVER TEN YEARS ENDING OCTOBER 31, 1996



# COMPARATIVE PERFORMANCE OVER TEN YEARS ENDING SEPTEMBER 30, 1996



November 6, 1996

Dear Plan Participant:

You are a participant in the Plan 60 deferred compensation plan (the Plan) managed by the City. The Committee charged with administering the Plan, consisting of myself, the Acting Finance Director, the Civil Service/Personnel Administrator and the Corporation Counsel, recently completed a comprehensive review of the Plan. As a result of our review, one change the committee determined should be made immediately is to implement market value accounting procedures throughout the Plan. This change was made effective October 21, 1996. Market value accounting procedures have become the standard in the investment industry. These procedures will provide you and other Plan participants with more accurate information concerning the current value of your accounts and will protect you and other Plan participants from differences in book to market value.

Previous Plan statements have reflected your account balance on the basis of the book value of the assets held in the Plan. With this letter I am enclosing an interim statement reflecting the market value of your account in Plan 60 as of October 31, 1996.

As of October 21, 1996, the market value of all assets held for the benefit of Plan participants will be established on the last business day of each month. In addition, rollovers and complete account withdrawals by or on behalf of Plan participants will be valued as of the last business day of each month and disbursed within seven business days thereafter. The quarterly statements sent to you in the future will reflect all transactions completed in your account during the period shown along with the current balance of your account on a market value basis.

This change represents a departure from past practice. The Committee believes it is a prudent and necessary step.



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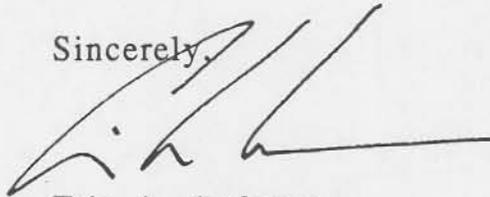
ALL-AMERICA CITY 1949, 1976, 1981

Plan 60 Participants  
November 6, 1996  
Page 2

In addition to this change, the Committee has also made a recommendation to City Council to discontinue Plan 60 effective April 1, 1997. The reasons for this recommendation are fully detailed in the enclosed letter to the City Council.

Questions concerning the new procedures or your account statements may be directed to the City Treasurer at 283-4279 or Employee Benefits at 283-4803.

Sincerely,

A handwritten signature in black ink, appearing to read 'Eric A. Anderson', with a long horizontal flourish extending to the right.

Eric A. Anderson  
City Manager

EAA/rg

Enclosures

November 6, 1996

The Honorable Mayor  
and  
Members of the City Council  
City of Des Moines

Re: Plan 60 Deferred  
Compensation Plan

In the ordinance creating Plan 60, the City fund for the deferred income of City employees, a committee is created to oversee the management of the fund. This committee is made up of the City Manager, Corporation Counsel, Finance Director and Civil Service/Personnel Administrator. This committee met and has taken the following action:

**Effective October 21, 1996 to record and report the value of the fund and of each participant's account on the basis of market value of Plan assets.**

The reasons for the change are several:

First, this is a more accurate way of reporting the current value of each account.

Second, it assures that the value of all accounts, those held in the fund and those rolled out of the fund, are protected from differences in book to market value. For example, if the book value of the Plan assets is higher than their market value, rollovers at book value decrease the value of accounts left in the fund. If book value is lower than market value, rollovers increase the value of those remaining.

Third, technology is now readily available for recording market value at the end of each month at no additional cost. However, the cost of valuing the fund daily is, we believe, too expensive to be contemplated at this time.



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November 6, 1996  
Page 2

Fourth, market value accounting has become the standard for the investment industry. In a separate memorandum, we have recommended that Plan 60 be discontinued as of April 1, 1997. If we are to do so, we must first meet the industry standard for the valuation of our Plan.

Fifth, federal regulation will, within a relatively short time, require us to use a trust to hold Plan assets. We will not be able to hold them in their present form. Although this will not occur until December 31, 1998, we believe that the requirements of this regulation, together with the other factors outlined in the attached memorandum, are great enough that the fund should be discontinued. If Council agrees, we will need a value methodology at industry standard to do so. If Council disagrees, we will still need a similar methodology that best reflects current practice in this area to meet federal requirements. It is fair and necessary, in our view, to adopt that methodology now.

This action has several immediate impacts. First, each participant's current account value will be reduced by 6.24%. This is the difference between the book value used to report the accounts in the past and the market value of Plan assets as of October 21, 1996. You will recall the audits for Plan 60 which were given to the Council last April and were distributed to each participant. Those audits, for FY 1993-4 and 1994-5, recorded differences in book to market value of 22% and 9%, respectively.

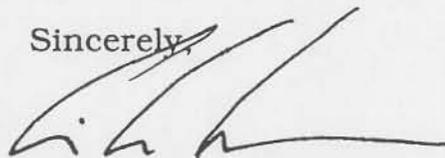
Second, all rollovers requested after October 21, 1996 will be calculated at market value and will be disbursed at the end of the month in which they are requested. Rollovers requested prior to October 21, 1996 were calculated and disbursed at book value and were executed upon request, according to the rules in place at that time. Although there is a difference in the basis of value of the rollovers prior to October 21, 1996 and after, this procedure is intended to be as even handed to participants as possible.

The Honorable Mayor  
and  
Members of the City Council  
November 6, 1996  
Page 3

We have reviewed prior rollouts. Our conclusion is that we should not adjust them to give effect to the new methodology. It is neither practical, given the complexity and cost, nor reasonable to do so, since those distributions were made under the rules in force at the time.

Each participant in the Plan will be receiving a special interim statement, as of October 31, 1996, which will show the adjustment from book to market value. They will also receive a copy of the attached letter, explaining this change and the recommendation you have received today to discontinue Plan 60. These were placed in the mail today.

Sincerely,

A handwritten signature in black ink, appearing to read 'Eric A. Anderson', written over the word 'Sincerely,'.

Eric A. Anderson  
City Manager

EAA/rg

Attachment