Performance Audit:
Retirement Administration
Defined Contribution Plan

July 2016

City Auditor's Office

City of Atlanta

File #16.01

CITY OF ATLANTA
City Auditor's Office
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Performance Audit:

Retirement Administration Defined Contribution Plan

Why We Did This Audit

This audit of the city's administration of its defined contribution retirement plan compares plan design and administration to recommended practices. Risks include management oversight, contract compliance, employee education, and fees and performance compared to benchmarks. As of January 2016, 51% of employees were enrolled in the defined contribution plan, with about one third of these employees enrolled solely in the defined contribution plan and two thirds in a hybrid plan.

What We Recommended

The chief financial officer and the commissioner of human resources should:

- prepare analysis estimating costs associated with increasing the contribution rate and adding employees to the hybrid plan

The management committee should:

- discontinue retirement fund loans from the 401(a) plan
- create a separate plan document
- assess the group annuity plan structure, fund performance, fees and administrative costs

The chief financial officer should:

- coordinate the appointment and election of management committee members
- request the third-party plan manager to report all compensation and create an ERISA budget for excess revenue

The chief information officer, chief financial officer and the commissioner of human resources should:

- implement auto-enrollment as a part of the Oracle upgrade

For more information regarding this report, please contact us through our website at www.atlaudit.org.

What We Found

The city's defined contribution plan offers participants the opportunity to save for retirement, but is missing several elements of best practices. For employees solely in the defined contribution plan, the combined contribution rate is 33% below the level needed to meet recommended income replacement. Among all plan participants, including employees in the hybrid plan, 90% are invested in only one fund, a strategy that could prevent employees from meeting long-term retirement goals. Loans from the plan could also reduce overall savings.

While the 2011 pension reform established a management committee to govern the plan for its participants, consistent with best practices, the management committee has never met. Elements of the plan structure could create disadvantages for participants, including difficulty monitoring fund performance, reduced regulatory oversight, inability to directly rollover assets when leaving the plan, and the fee structure.

The third-party plan manager is compensated for services indirectly through fund-level expenses borne by plan assets. The city has not tracked this indirect compensation, which totaled nearly $1 million from July 1, 2014 through December 31, 2015. Indirect compensation has exceeded the annual target established in the contract by 2.5 basis points and has exceeded the estimated monthly fee per participant, which the city opted not to pay, by nearly $300,000.

City staff is responsible for enrolling employees into the retirement plan. The median time between hire date and enrollment date was 40 days during fiscal year 2015. Delays or errors in enrollment reduce employee benefits because the city does not reimburse its employees for lost profits or unmatched contributions when correcting errors.

Summary of Management Responses

Recommendation #1:	We recommend that the chief financial officer and the commissioner of human resources should prepare for City Council consideration analysis estimating the costs associated with increasing the overall contribution rate to the defined contribution plan to the suggested level of 18% to 20% of annual salary, as well as the costs and benefits of adding the employees currently in the defined contribution plan to the city's hybrid plan.	
Response & Proposed Action:	Finance and HR will develop cost estimates for both increasing funding levels for employees who only have a 401a account and the cost to move these employees to the hybrid plan.	**Agree**
Timeframe:	September 2016	
Recommendation #2:	We recommend that the management committee discontinue retirement fund loans from the 401(a) plan.	
Response & Proposed Action:	Did not seek a response. Management Committee not formed as of July 2016.	
Timeframe:		
Recommendation #3:	We recommend that the management committee review training efforts at least quarterly and develop strategies to target training.	
Response & Proposed Action:	Did not seek a response. Management Committee not formed as of July 2016.	
Timeframe:		
Recommendation #4:	We recommend that the chief financial officer coordinate the appointment and election of management committee members and facilitate the meetings in order to ensure the defined contribution plan is managed according to the intent of Ordinance 11-O-0672.	
Response & Proposed Action:	The CFO will continue to prompt the formation of the management committee	**Agree**
Timeframe:	June 2017	
Recommendation #5:	We recommend that the chief financial officer request that Voya report all compensation, direct and indirect, to the city on a monthly basis for monitoring and contract compliance.	
Response & Proposed Action:	The CFO will request that Voya provide all compensation data to the City on a monthly basis	**Agree**
Timeframe:	September 2016	
Recommendation #6:	We recommend that the chief financial officer request that Voya create an ERISA budget for excess revenue captured during the contract period.	
Response & Proposed Action:	The CFO will request that Voya create ERISA budget or its equivalent to offset administrative costs.	**Agree**
Timeframe:	September 2016	

Recommendation #7:	We recommend that the management committee create a separate plan document, referring to the city code and contract where relevant.
Response & Proposed Action:	Did not seek a response. Management Committee not formed as of July 2016.
Timeframe:	
Recommendation #8:	We recommend that the management committee assess the advantages and disadvantages to participants of holding plan assets in a group annuity plan versus a mutual fund company prior to procuring plan management services when the current contract expires.
Response & Proposed Action:	Did not seek a response. Management Committee not formed as of July 2016.
Timeframe:	
Recommendation #9:	We recommend that the management committee evaluate fund performance for all funds in the plan and consider substituting other assets that out-perform the current funds available in the plan.
Response & Proposed Action:	Did not seek a response. Management Committee not formed as of July 2016.
Timeframe:	
Recommendation #10:	We recommend that the management committee review fees paid to ensure that they are reasonable.
Response & Proposed Action:	Did not seek a response. Management Committee not formed as of July 2016.
Timeframe:	
Recommendation #11:	We recommend that the management committee determine whether the city should bear or share the plan administrative costs with the participants.
Response & Proposed Action:	Did not seek a response. Management Committee not formed as of July 2016.
Timeframe:	
Recommendation #12:	We recommend that the chief information officer, chief financial officer and the commissioner of human resources implement auto-enrollment as a part of the Oracle upgrade, which should eliminate the errors associated with the manual processes.
Response & Proposed Action:	The CFO and CHR will include auto-enrollment in the scope of work for the Oracle upgrade. AIM will investigate the feasibility of including auto-enrollment in the Oracle R12 upgrade. Auto-enrollment is heavily dependent on a defined business process for appropriate employee retirement plan assignment. **Agree**
Timeframe:	October 2017 or Oracle upgrade go-live date

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July 13, 2016

Honorable Mayor and Members of the City Council:

We undertook this audit of the city's administration of its defined contribution retirement plan to compare plan design and administration to recommended practices. Risks to the city and plan participants include management oversight, contract compliance, employee education, and fees and performance compared to benchmarks.

The chief financial officer and commissioner of human resources agreed with the respective recommendations and have begun to address them. We made several recommendations to the yet-to-be formed management committee. We did not seek managements response to these recommendations.

The Audit Committee has reviewed this report and is releasing it in accordance with Article 2, Chapter 6 of the City Charter. We appreciate the courtesy and cooperation of city staff throughout the audit. The team for this project was Diana Coomes Lynn and Ivy Williams.

Leslie Ward
City Auditor

Marion Cameron
Audit Committee Chair

Retirement Administration Defined Contribution Plan

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List of Exhibits

Introduction

This audit of the city's administration of its defined contribution retirement plan compares plan design and administration to recommended practices. Risks include management oversight, contract compliance, employee education, and fees and performance compared to benchmarks. As of January 2016, 51% of employees were enrolled in the defined contribution plan, with about one third of these employees enrolled solely in the defined contribution plan and two thirds in a hybrid plan.

Background

The city's retirement plans provide designated employee groups with retirement benefits. The different plans have different characteristics, but the purpose of each is to provide income at retirement for the employees and, in the event of death, to provide funds for their beneficiaries.

Defined contribution refers to a retirement plan that does not guarantee a specific benefit amount at retirement. An employer and/or employee make pre-tax contributions to an individual account and deposit the funds into an investment account. The employer often matches the employee contributions up to a certain percentage rate. Once the employer deducts the funds from the employee's pay, the funds do not become available until termination of employment and/or retirement. By contrast, a defined benefit plan is a traditional pension plan in which an employee's pension payment is calculated according to length of service and the salary earned at the time of retirement.

City defined contribution plan. The city's current defined contribution plan includes all employees hired since July 1, 2001, who are in pay grades G.19 or higher and are not sworn members of the police or fire departments. Participating employees are required to make a pre-tax contribution of 6% of compensation into the section 401(a) defined contribution plan. The city matches the mandatory payment by contributing 6% of each participating employees' compensation into the plan. Employees vest over a 5-year period at 20% per year. All contributions made by the city after the completion of the fifth year are 100% vested. Plan participants also have an option of making voluntary, unmatched contributions into the section 457(b) deferred compensation plan.

City hybrid plan. The city's defined benefit hybrid plan includes all other employees hired on or after November 1, 2011. Participants are required to make a pre-tax contribution of 3.75% of compensation into the section 401(a) plan, which the city matches. In addition to the mandatory payments, participants in the hybrid plan may make a voluntary contribution into the 457(b) deferred compensation plan. The city will match 100% of the voluntary contribution up to 4.25%, which is deposited into the 401(a) plan. Employees vest over a 5-year period at 20% per year. All contributions made by the city after the completion of the fifth year are 100% vested. Employees also contribute 8% of their compensation to the applicable defined benefit plan (general employee, police, or fire). The retirement benefit formula multiplies average salary over ten years by years of service by 1%. The vesting period for the defined benefit component is 15 years. Employees who leave city employment before they are fully vested in the defined benefit may elect to receive a partial benefit at retirement if they have completed at least five years of service or receive their contributions to the plan with accrued interest of 5% per year.

Participants in the defined benefit plans hired prior to September 1, 2011, were given the option to continue in the plan with the employee contribution increased to 12%, or 13% if a beneficiary was designated, or to participate in the hybrid plan. The employee's decision was irreversible.

City Created the Defined Contribution Plan to Cut Costs

In order to reduce costs, the city closed its defined benefits pension plan for general employees to new hires in 2001 and created the defined contribution plan. Public safety employees and existing employees in the general pension plan retained their defined benefit plans, although employees in the general pension plan could elect to participate in the defined contribution plan at their option.

Following the report of a pension task force appointed by the mayor, which recommended doing away with the defined contribution plan, the city amended the plan effective September 1, 2005, to require participation only of new employees and the existing general employees, hired since 2001, in pay grades 19 and above. Existing general employees in pay grades below grade 19 who were in the defined contribution plan were allowed to remain in the plan or transfer to the defined benefit plan without penalty.

In September 2011, the city created the existing hybrid retirement plan consisting of a defined benefit component and a defined contribution component. Employees in pay grades 19 and higher remained in the defined contribution plan.

While the defined contribution plan was intended to reduce city costs, literature identifies some advantages to employees of participating in a defined contribution plan. The primary benefit to employees of participating in a defined contribution plan is its portability. Contributions to a this type of retirement plan are portable and can be taken with the participant upon separation from the employer. Vesting requirements are also shorter than in traditional pension plans. Participants in defined contribution plans have more control over their investments, which can offer a higher earning potential. The higher earning potential is a double-edged sword because employees also take on investment risk previously borne by employers. Employees in defined contribution plans also face higher inflation and longevity risks — essentially risks that retirement income will be insufficient — than employees in traditional pension plans who receive the pension benefit for life and often receive cost-of-living adjustments.

Participant Demographics

As of January 2016, 1,405 employees were participating in the defined contribution plan and 2,790 employees were participating in the hybrid plan (see Exhibit 1).

Exhibit 1 Number of Employees: Defined Contribution or Hybrid Plan

Retirement Plan	Number of Employees	25th Percentile Annual Salary	Median Annual Salary	Median Age	Median Years of Service
Defined Contribution	1,405	$51,731	$64,321	47	4.5
Hybrid	2,790	$41,068	$47,412	49	15.0
Total	4,195	$42,763	$51,611	48	11.3

Source: Oracle Discoverer Reports, January 2016

The median annual salary for employees in the defined contribution plan was $64,321; 25% of the employees earned less than $52,000 per year. The median annual salary for employees in the hybrid plan was $47,412, with 25% earning $41,068 or less. The median age of employees participating in the defined contribution plan was 47 and they had worked for the city for a median of 4.5 years. The median age of employees participating in the hybrid plan was 49 and they had worked for the city for a median of 15 years.

City Contracts with Voya for Plan Management Services

Council Resolution 13-R-3868 authorized the contract between the City of Atlanta and ING Life Insurance and Annuity Company (now Voya Retirement Insurance and Annuity Company) to provide management and recordkeeping services for the 401(a) defined contribution and 457(b) deferred compensation plans. The initial term of the contract is three years, from July 1, 2014, to June 30, 2017, with the option to renew for two additional one-year terms. Total compensation payable by the city for the initial three-year term is not to exceed $2 million. In addition to compensation for plan services, the contract allows Voya to retain "float," bank service credits on contributions awaiting investment and payments awaiting distribution.

Under to the contract, Voya is responsible for:

- developing plan enrollment materials and conducting introductory on-site education and enrollment meetings for employees during transition
- ongoing allocation of plan contributions to individual participant accounts and daily reconciliation of plan and participant activity
- ongoing maintenance of participant beneficiary designations based on mutually agreed upon procedures reflected in the plan document
- ongoing maintenance recordkeeping of individual participant account records and timely processing of all transactions permitted under the plan
- ongoing generation of periodic plan activity reports for the plan sponsor
- ongoing timely provision of necessary tax forms to participants who received taxable distributions during the previous year
- ongoing provision of employee enrollment and education services, including the provision of communication packages that include information for employees to enroll and make investment choices

- establishing and maintaining an electronic interface with the plan sponsor for participant enrollment information and changes to the participant's contribution amount or rate
- providing access to customer service representatives via a toll free telephone line to respond to plan participant inquiries, provide information about participants' accounts and investment options, and enroll and employee into the plan and to distribute administrative forms
- providing access to an automated voice response system via toll free telephone lines, through with participants may obtain updated account and investment information and initiate transactions permitted under the plan
- providing access to an internet site, through which participants may obtain updated account and investment information and initiate transactions permitted under the plan
- ongoing review and processing of participant-initiated rollover or transfer requests on behalf of the sponsor
- ongoing review and processing of participant unforeseeable emergency withdrawal requests on behalf of the sponsor
- ongoing review and processing domestic relations orders on behalf of the sponsor
- ongoing review and processing participant-initiated benefit payment requests on behalf of the sponsor
- access to counseling by licensed agents for plan participants who are retiring or otherwise requesting a benefit payment from the plan based on mutually acceptable standards
- ongoing processing of required minimum distributions in accordance with IRS code
- ongoing facilitation of communications between Voya, the city and plan participants based on mutually acceptable guidelines

The city is responsible for:

- providing timely and accurate census information (name, Social Security number, address, date of birth, and date of hire) at least two business days prior to the submission of each contribution
- choosing the appropriate default investment option
- providing enrollment kits to each eligible participant prior to enrollment

- final approval of appeal of denied requests
- establishing an automated contribution remittance process for repayment of loans if permitted by the plan

The city acknowledges that Voya is performing non-discretionary ministerial administrative services at the direction of the plan. As the plan sponsor, the city retains fiduciary responsibilities. The IRS defines a plan fiduciary as "anyone who exercises discretionary authority or discretionary control over management or administration of the plan, exercises any authority or control over management or disposition of plan assets, or gives investment advice for a fee or other compensation with respect to assets of the plan."[1] While government retirement plans are not covered by ERISA (Employee Retirement Income Security Act of 1974), the law provides a reasonable benchmark of expected fiduciary duties:

- acting solely in the interest of plan participants and their beneficiaries and with the exclusive purpose of providing benefits to them
- carrying out their duties prudently
- following the plan documents
- diversifying plan investments
- paying only reasonable plan expenses[2]

As of December 31, 2015, the value of plan assets in the 401(a) plan was $104.7 million and the value of plan assets in the 457(b) plan was $144.7 million.

[1] https://www.irs.gov/Retirement-Plans/Plan-Participant,-Employee/Definitions
[2] US Department of Labor, Meeting Your Fiduciary Responsibilities http://www.dol.gov/ebsa/publications/fiduciaryresponsibility.html

Audit Objectives

This report addresses the following objectives:

- How does the city's defined contribution plan design compare to best practices?
- How do the city's administration and oversight of the defined contribution plan compare to best practices?

Scope and Methodology

We conducted this audit in accordance with generally accepted government auditing standards. We reviewed plan financial data from July 1, 2014 through December 31, 2015, which covered the first 18 months of the existing contract. We reviewed city processes as of October 2015.

Our audit methods included:

- interviewing subject matter experts associated with the administration of the defined contribution plan through enrollment, employment, and separation
- reviewing retirement literature to identify best practices related to defined contribution plan design and administration
- reviewing city code and legislation related to the city's defined contribution plans
- reviewing the city's contract with Voya for plan management services
- reviewing and analyzing documentation provided by Voya for the 401(a) and 457(b) plans, including plan review documents, performance evaluations, investment information reviews, fund prospectuses, and fee structure spreadsheets/reports
- comparing official documents from the city and Voya for participants in the 401(a) and 457(b) plans
- analyzing general demographics of participants in the defined contribution plans

Generally accepted government auditing standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Findings and Analysis

City Should Strengthen Defined Contribution Plan by Applying Best Practices

The city's defined contribution plan offers participants the opportunity to save for retirement, but is missing several elements of best practices, putting participants' retirement security at risk. For employees solely in the defined contribution plan, the combined contribution rate is 33% below the level needed to meet recommended income replacement. Among all plan participants, including employees in the hybrid plan, 90% are invested in only one fund, a strategy that could prevent employees from meeting long-term retirement goals. Loans from the plan could also reduce overall savings.

The 2011 pension reform established a management committee to govern the plan for its participants, consistent with best practices. The management committee has never met. Nor has the city created a formal plan document to support the management committee in administering the plan. The city has a fiduciary responsibility to ensure the plan serves the interests of participants. Elements of the plan structure could create disadvantages for participants, including difficulty monitoring fund performance, reduced regulatory oversight, inability to directly rollover assets when leaving the plan, and the fee structure.

Voya is compensated for its management services indirectly through fund-level expenses borne by plan assets. The city has not tracked this indirect compensation, which totaled nearly $1 million from July 1, 2014, through December 31, 2015. Indirect compensation has exceeded the annual target established in the contract by 2.5 basis points and has exceeded the estimated monthly fee per participant, which the city opted not to pay, by nearly $300,000.

City staff is responsible for enrolling employees into the retirement plan. The median time between hire date and enrollment date was 40 days during fiscal year 2015. Delays or errors in enrollment reduce employee benefits because the city does not reimburse its employees for lost profits or unmatched contributions when correcting errors.

Going forward, the chief financial officer and the commissioner of human resources should prepare for City Council consideration analysis estimating the costs associated with increasing the overall contribution rate to the defined contribution plan to the recommended level of 18% to 20% of annual salary. The chief financial officer should coordinate the formation of the management committee and schedule regular meetings.

The committee should develop a plan document and review the plan and fee structure to evaluate whether it is the best option for city participants. It should also review fund performance quarterly and consider recommending changes to investment options available in the plan. The committee should discontinue allowing retirement fund loans from the 401(a) plan. Finally, the management committee should review training efforts at least quarterly and develop strategies to target training.

The chief information officer, chief financial officer, and the commissioner of human resources should implement auto-enrollment as a part of the Oracle upgrade, which should reduce delay and errors associated with the manual processes.

Plan Design Follows Several Elements of Best Practices, but Poses Risk to Participants' Retirement Security

While the city's defined contribution plan design is consistent with best practices regarding mandatory participation, vesting, number of investment options, default contributions, and recordkeeping, combined contributions are 33% lower than recommended for adequate income replacement in retirement. Also, participant account balances as of 2015 were lower than average benchmarks for government plans, and the gap widened as the age of participants increased.

Ninety percent of participants in the city's 401(a) plan were invested in only one fund, which could reduce earning potential. Most often the participant was invested in the default asset allocation fund. While the funds themselves are diversified, mitigating risk, the lack of multiple selections calls into question the extent to which employees understand or are comfortable choosing among the plan offerings. Nearly 14% of participants had their plan assets invested solely in the stable value fund, which protects assets against daily fluctuations in market value but does not offer long-term growth.

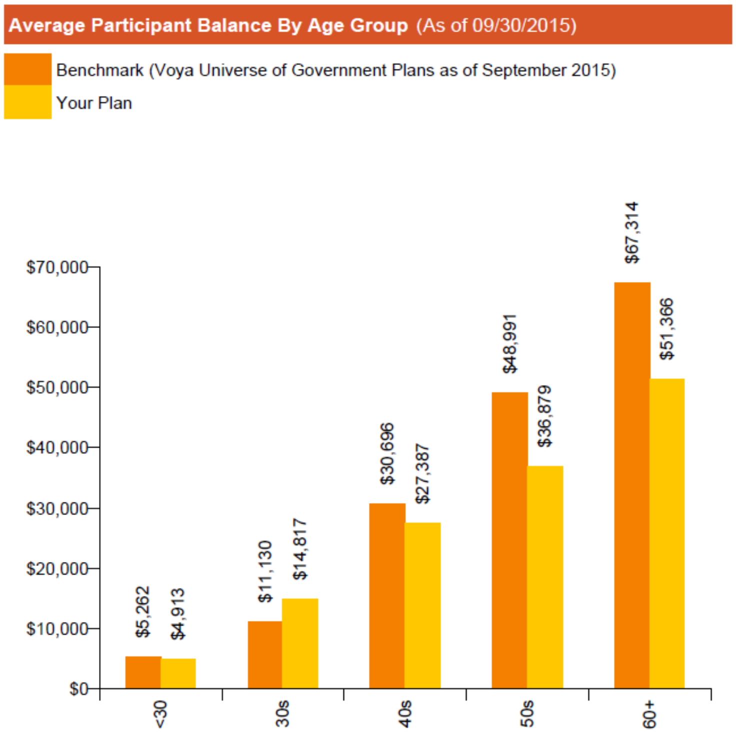
Withdrawals also pose a risk to retirement security. During fiscal year 2015, 8% of defined contribution plan participants took at least one loan from their retirement assets. The city could reduce risk to participants' retirement security by increasing the combined contribution rate and disallowing loans.

Contribution levels are too low to provide recommended income replacement. The responsibility for ensuring that an employee's retirement is adequate and secure is generally shared among the employee, employer, and the federal government through Social Security. The city does not participate in Social Security. Social Security benefits typically provide one- to two-thirds of an eligible participant's retirement resources. To offset this deficit, best practices recommend mandatory employer and employee contributions to the defined contribution plan totaling at least 18% to 20% for participants not covered by Social Security. The combined contribution rate for employees in the defined contribution plan is 12%, 33% lower than the recommended minimum, thus creating a risk that employees in the defined contribution plan will have inadequate resources at retirement. Employees may increase retirement savings by contributing to the 457(b) deferred compensation plan, but the city does not match these voluntary contributions, thus shifting the shared burden of retirement security more toward the employee.

The calculation used to estimate the recommended contribution rate assumed a target retirement income replacement ratio of 75-89%, consistent with the 2004 *Georgia State University/Aon RETIRE Project*. The updated 2008 study found that required income replacement ratios had increased to 77% for a person earning $80,000 and to 94% for a person earning $20,000. Income replacement ratio—gross income after retirement divided by gross income before retirement—is commonly used to measure retirement adequacy. A person generally needs less income after retirement to maintain a similar standard of living because income and payroll taxes go down, saving for retirement is no longer needed, and work-related expenditures are reduced. A higher replacement ratio is generally required for lower paid employees because tax and saving before retirement are a lower proportion of their spending and work-related expenditures do not decrease by as much.

Average 401(a) participant account balances were below other government plans. As of September 30, 2015, the average city 401(a) participant account balance was $21,993. The gap between average account balance and Voya's benchmark based on other government plans it administers was wider for older age groups, also indicating that employees may not be on track with retirement goals (see Exhibit 2).

Exhibit 2 Average Participant Balance for City Employees



Source: Voya's Plan Review 401(a), October 1, 2014, through September 30, 2015

While employees may have resources from other employment to draw on in retirement, federal law reduces Social Security benefits for employees for whom a substantial amount of income was not subject to Social Security taxes. The Windfall Elimination Provision affects how the Social Security Administration calculates benefits for retirees who are entitled to both Social Security and to retirement benefits from work not covered by Social Security. The amount of reduction depends on the year the worker is eligible to retire, the amount of earnings covered by Social Security, and the amount of the retirement benefit that was not covered by Social Security. The amount of reduction therefore varies based on individual circumstances, but can be substantial.

Previous evaluations of the city's retirement plans that considered joining Social Security met with opposition from employee groups, most of whom receive an annuity benefit from the defined benefit or hybrid plans.

We recommend the chief financial officer and the commissioner of human resources prepare for City Council consideration analysis estimating the costs associated with increasing the overall contribution rate to the defined contribution plan to the recommended level of 18% to 20% of annual salary. Increasing both the city and employee contributions to 9% would cost the city about $3 million annually based on current salaries. The chief financial officer and commissioner of human resources should also estimate the costs and benefits of adding the employees currently in the defined contribution plan to the city's hybrid plan.

Although allowed by IRS regulations, best practices caution against offering hardship withdrawals or loans because of effect on overall savings. The IRS allows qualified plans to offer loans to participants from the balances in their retirement accounts. The city began offering participant loans from the 401(a) plan in 2014 as an employee benefit. The maximum loan amount a participant may borrow from his or her account is the lesser amount of 50% of the vested account balance or $50,000. The participant must pay a $100 loan origination fee and repay the loan with interest; the rate is set based on Moody's Corporate Bond Yield Average in effect the month the loan is initiated. Repayments are processed through city payroll deductions and are applied back to the participant's account. The maximum repayment period is 57 months, except for loans used to acquire the participant's principal residence, in which case the maximum repayment period is 360 months.

Approximately 8% of defined contribution plan participants acquired loans from the 401(a) retirement plan during 2015. Participants who default on loans may be subject to increased tax liabilities. As of fiscal year 2015, 9% of employees who had acquired loans defaulted by failing to make scheduled payments. The median default loan amount was approximately $3,800. According to Internal Revenue Code, loans are considered taxable distributions if they fail to comply with the plan loan rules in terms of amount, duration, and repayment terms. Voya reports approximately $2.5 million in loans issued in 2014 and $2.9 million in 2015. About half of the loans were for less than $3,500.

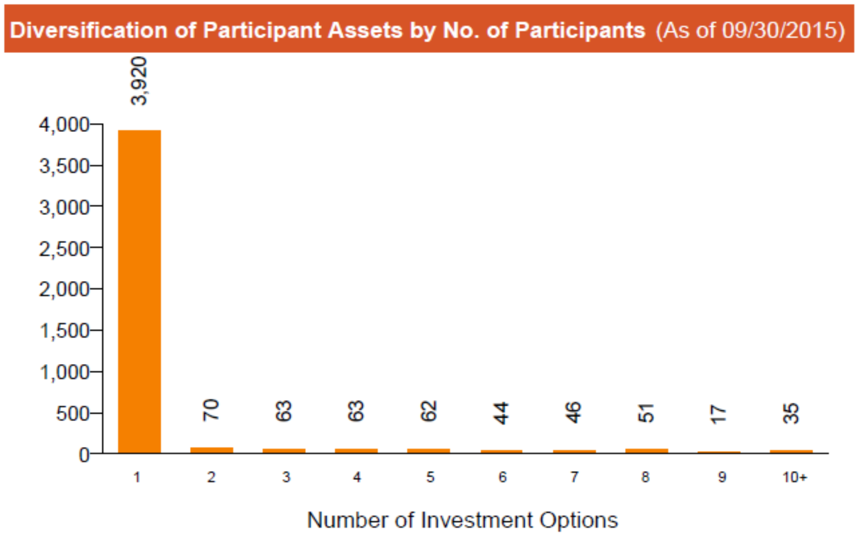
Participant may also request an unforeseeable emergency hardship withdrawal from the 457(b) plan. As defined by the contract, an unforeseeable emergency means "extraordinary and unforeseeable circumstances arising as a result of events beyond the control of the participant, including severe financial hardship from an illness or accident…; the loss of property due to casualty…; and other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the control of the participant." Hardship withdrawals are limited to the amount reasonably necessary to satisfy the emergency need.

Early withdrawals and loans reduce asset accumulation for retirement. The Center for Retirement Research at Boston College estimates that pre-retirement distributions reduce asset accumulation by 25%. Most of the leakage is through lump sum distribution at job change, but early withdrawals and loans also contribute. In order to reduce pre-retirement leakage from participant accounts, best practice suggests prohibiting withdrawals or loans. If the plan offers hardship withdrawals or loans, the plan should limit the number of loans and withdrawals a participant may take at one time. The IRS suggests participants consult with a financial planner prior to borrowing from retirement accounts to determine whether obtaining a loan from a financial institution or another source would be a better alternative.

Because contribution to the 401(a) plan is mandatory and is the primary retirement saving vehicle for employees enrolled in the defined contribution plan, we recommend the management committee discontinue allowing retirement fund loans from the 401(a) plan, but continue to allow for hardship withdrawals from the 457(b) deferred compensation plan.

Despite education efforts, participant investment accounts lack diversity. In response to the city's request for proposals for management services for the defined contribution plan, Voya stated that it would evaluate education services by the extent to which participants diversified their investment selections. Voya's benchmark suggests that a well-diversified portfolio has three or more investments. Diversification of the retirement portfolio reduces the investor's exposure to risk while increasing the opportunity for potential returns. As of September 30, 2015, 90% of plan participants were using only one investment (see Exhibit 3).

Exhibit 3 Voya's Diversification Statistics for the 401(a) Account



Source: Voya's Plan Review 401(a), October 1, 2014, through September 30, 2015

Employees were most often invested solely in the default option asset allocation fund (see Exhibit 4). While these asset allocation funds are themselves diversified, the lack of other selections calls into question the extent to which employees understand or are comfortable choosing among the different plan offerings. The stable value fund was the second most selected fund for investors with one selection. The stable value fund is a type of cash fund that protects the principal dollars in the account while paying a modest current rate of interest expressed as an annual effective yield. Voya determines and publishes the interest rate quarterly. For the first quarter of 2016, the stable value fund paid 1.37% annually. The stable value investment option is intended to help participants protect their assets against the daily fluctuations in market value, but should not be viewed as a long-term growth investment because it will not provide the same level of return as stock funds over time. As of September 30, 2015, 610 employees were using this account as their only investment type.

Exhibit 4 Number of Participants Selecting One Fund Type

Fund Type	Participants Invested
Asset Allocation	*3,289*
Voya Target Solution Trust Fund 2020 Fund	12
Voya Target Solution Trust Fund 2025 Fund	454
Voya Target Solution Trust Fund 2030 Fund	48
Voya Target Solution Trust Fund 2035 Fund	668
Voya Target Solution Trust Fund 2040 Fund	77
Voya Target Solution Trust Fund 2045 Fund	1,533
Voya Target Solution Trust Fund 2050 Fund	134
Voya Target Solution Trust Fund 2055 Fund	229
Voya Target Solution Trust Fund: Income Fund	134
Stability of Principal	*610*
Bonds	*1*
Large Cap Value	*10*
Large Cap Growth	*3*
Small/Mid/Specialty	*4*
Global/International	*3*
TOTAL PARTICIPANTS UTILIZING 1 INVESTMENT OPTION	**3,920**

Source: Voya's Plan Review 401(a), October 1, 2014, through September 30, 2015

Best practices call for broad-based retirement and investment education services. Under the contract, Voya is responsible for the employee education program, including new employee orientation, workshops, one-on-one appointments with representatives, and training via the participant account website. New and current employees receive the information booklet provided by Voya, which includes information on education, investments, fees and other costs, as well as plan features. It includes the "Your Number" formula to help participants determine how much money is needed to save for retirement. Employees can access training videos and literature via the "Education and Tools" tab on the Voya website (www.voyaretirementplans.com), which includes such topics as:

- basic and advanced investing
- retirement needs
- plan benefits, investment strategies, account management, and retirement planning
- debt and credit management, estate planning

While the education programs offered appear to be comprehensive, we noted an instance in which Voya representatives misinformed training participants by stating that the federal Windfall Elimination Provision does not apply to city employees in the defined contribution plan. The Social Security Administration confirmed that the provision does apply to city employees; defined contribution participants who paid Social Security taxes during previous employment may experience reductions in their Social Security benefits upon retirement.

We recommend the management committee that is charged with overseeing the defined contribution plan review training efforts at least quarterly and develop strategies to target training.

The city places no limits on lump sum retirement distributions upon retiring. Best practices recommend plans establish a minimum amount of a retiree's account be annuitized to mitigate inflation and longevity risks, however the practice is not common among public sector plans. The city's plan offers annuity options upon retirement, but most retirees choose lump sum distributions. The city could help mitigate longevity risk by enrolling employees currently in the defined contribution plan in the city's hybrid plan.

Other elements of the plan's design are consistent with best practices. These include mandatory participation, immediate vesting upon hire, limiting investment options, default contribution selections, and a single record-keeper structure for larger plans:

- Best practices recommend mandatory employee participation in the plan with low or no age restrictions and maximum waiting periods for participation of one year. All permanent, fulltime city employees are required to participate in a retirement plan. All permanent, fulltime employees hired since November 2011 are required to participate in the defined contribution or hybrid plan.
- Best practices recommend immediate vesting; currently, the city uses a graduated vesting schedule and employees are vested in 20% of the city's contributions after one year.
- Best practices recommend the plan offer diverse investment options but limit the number to 15-20 in order to reduce decision paralysis. The city's plan offers 19 investment options in different classes intended to meet different investment goals.
- Best practices recommend that contributions default into a lifecycle target date fund to address investment risk. Employee contributions are automatically placed into the asset allocation fund, a similar type of fund, until the participant adjusts the selections.

- Best practices recommend a single record keeper structure to deliver plan services at lower cost. The city has contracted with Voya to provide recordkeeping services.

Plan Governance and Oversight Should Ensure the City is Fulfilling Its Fiduciary Responsibilities

The city pension reform ordinance requires a management committee to manage the defined contribution plan for its participants. The management committee has never met since its creation in 2011. The city is also lacking a formal plan document to assist the management committee in administering the plan. The city has a fiduciary responsibility to ensure the plan serves the interests of participants. Several elements of the plan structure could pose disadvantages to participants, including difficulty monitoring fund performance, reduced regulatory oversight, inability to directly rollover assets when leaving the plan, and the fee structure.

While the contract limits Voya's compensation to $2 million over the three-year duration, Voya earned over $1 million in total compensation in the first 18 months of the contract. Most of Voya's compensation was earned by revenue sharing agreements paid through fees from plan assets. The city has not tracked indirect compensation, which represents 93% of the total earnings to date. Compensation from revenue sharing has exceeded the annual target established in the contract by 2.5 basis points and has exceeded the estimated monthly fee per participant by nearly $300,000.

We recommend the chief financial officer coordinate the formation of the management committee and schedule regular meetings. The committee should address the lack of a plan document and review the plan and fee structure to evaluate whether it is the best option for city participants. We also recommend the committee review fund performance quarterly and consider adding other assets that out-perform the funds currently available in the plan.

The management committee established in legislation to oversee the defined contribution plan has never met. During the 2011 pension reform, Ordinance 11-O-0672, Section 4, Article 14 established a management committee as the internal governance structure for the defined contribution plan. The committee is responsible for managing and operating the defined contribution plan, including but not limited to all powers necessary to enable all duties of a retirement plan manager to be properly carried out. The management committee comprises nine members:

- the Mayor or her/his designee
- the City Council president or his/her designee
- the chairperson of the City Council Finance and Executive Committee
- the city attorney
- the chief financial officer
- the commissioner of the Department of Human Resources
- a city councilmember appointed by the Mayor
- a finance management industry expert
- an employee representative of the defined contribution plan who is elected by the mandatory participants and the defined benefit hybrid participants, and who is a member of one of those two groups.

Since the legislation became effective, no management committee meetings have been held to oversee the defined contribution plan. In June 2014, the City Council approved resolution 14-R-3607 requesting the chief financial officer, in his role as plan administrator for the defined contribution plan, to create the management committee and reiterated the committee's role. The committee still has yet to be established. While the committee's role is more limited than that of a pension board, which is responsible for investing funds, best practices call for a five to nine member board or committee to oversee defined contribution plan governance. Key responsibilities include:

- designing the plan investment menu and monitoring the investment options
- approving plan administrative and investment policies
- approving changes to the plan's services and features
- establishing a communications and education plan
- overseeing and monitoring the delivery of services in relation to goals and objectives

- procuring plan services and evaluating performance of any hired service providers or consultants[3]

As the plan sponsor, the city has a fiduciary duty to ensure the plan is administered in accordance with the plan document and in the best interests of the participants.

Best practices recommend a formal, written plan document as the framework for the operation and administration of the retirement plan. A plan document is a written document that describes the terms and conditions related to the operation and administration of a plan. Best practice is to review the plan document annually to ensure the plan is current and aligns with sponsor goals and objectives. According to the city's agreement with Voya, the contract serves as the plan document if city does not prepare an official plan document. While the city code establishes the plan and the contract describes some of the plan's policies and procedures, best practices suggest incorporating operational procedures and processes related to the retirement plan in the plan document. In several instances, the contract refers to mutually agreed upon procedures or duties of the sponsor that are not currently documented, which include:

- beneficiary designations and benefit payment authorizations
- incoming rollovers/transfer authorization
- facilitation of communication among Voya, the city, and plan participants

In addition to the plan document, the National Association of Government Defined Contribution Administrators suggests plan sponsors have other documents in place:

- bylaws for charter documents for the plan's management committee
- a policy manual for guiding administrative policies
- an investment policy statement that details the plan's investment options and how they are selected and monitored

We recommend the chief financial officer, as the plan administrator, coordinate the appointment and election of management committee members and convene meetings. The chief financial officer should facilitate the meetings in order to ensure the

[3] Keith Overly and Michael J. Studebaker, "Best Practices for Public Sector DC Plans," *Benefits Magazine*, Volume 52, No. 8 August 2015, pp. 42-47.

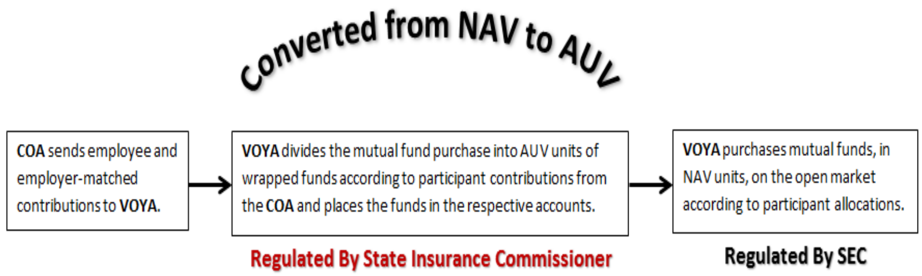
defined contribution plan is managed according to the intent of Ordinance 11-O-0672. We also recommend that the management committee create a separate plan document, referring to the city code and contract where relevant, to capture all aspects of plan administration and operation in one document. The committee should review the plan document annually to ensure that it is current.

Plan structure makes it difficult to monitor performance. Under the current contract, the city's defined contribution plan is structured as a group annuity invested in the Voya Government Custom Choice Blend product. This is a funding agreement, called a "wrapper" or "wrap fund" in the industry, that is a group contract with valuation of individual participant accounts based on accumulated unit value (AUV) pricing. It offers plan participants a product that looks and acts similar to a mutual fund, but is not the actual publicly traded mutual fund, which is priced based on net asset value (NAV). While Voya does not charge an additional wrap fee for its offerings in the city plan, the pricing conversion from NAV to AUV prevents city participants from directly comparing the purchase price of Voya's fund offerings to their publicly traded versions. This ambiguity is due to the conversion of the funds using calculations based on Voya's internal determination, not the open-market recognized trading price.

Plan structure reduces external oversight. The city forwards employee and employer contributions to Voya the week after distributing paychecks. Voya purchases publicly traded mutual funds, which are subject to regulation by the Securities and Exchange Commission (SEC). Voya retains ownership of the purchased funds and allocates their value into the internal variable wrap funds. These wrap funds are then allocated to participant accounts using the AUV price, according to the participants' investment selections and contribution amounts. Because Voya owns the mutual funds, it retains the SEC investor protections. The SEC does not offer protections for investors in the variable-wrapped funds. These funds are considered an insurance product that is subject to regulation by the State Insurance Commissioner. Exhibit 5 illustrates how the plan works.

Plan structure prevents participants from rolling over fund assets when leaving the plan. The conversion from the publicly traded mutual funds to the new variable funds is also a disadvantage to participants exiting the plan because the actual assets cannot directly roll over to another plan through an in-kind transfer. Assets instead must be sold and the cash value, or distribution, can then be applied to another investment account. Since the cash value is determined by the original calculations performed when creating the variable fund, there is no clear method to verify the value of the assets prior to the cash out. While literature cites termination penalties as a disadvantage of this type of plan, city participants are not subject to penalties when exiting the plan.

Exhibit 5 Contribution and Investment Process: the City and Voya



Source: Interviews with COA Payroll, COA General Accounting and Voya Representatives

Group annuity plans typically have lower start-up costs and may have lower overhead because their products are not registered with the SEC. The primary disadvantages of group annuity plans cited in literature, higher and/or hidden fees and termination penalties, are not present in the city's plan. Nor does the plan offer typical benefits of an annuity such as a minimum guaranteed return.

We recommend the management committee assess the advantages and disadvantages to participants of holding plan assets in a group annuity plan versus a mutual fund company prior to procuring plan management services when the current contract expires.

Fund performance information for the variable funds in the defined contribution plan is inaccurate or non-existent. The city contracts with Grey and Co. to independently evaluate plan performance quarterly. The evaluator was unaware of the plan structure and had reviewed the publicly traded versions of the fund offerings within the plan, rather than the variable funds offered to participants. Voya also submits evaluations of fund performance quarterly to the finance department, but the evaluations did not include the asset allocation funds, which accounted for 21% of participant investments as of December 31, 2015. According to Voya, the asset allocation funds have not been scored because the funds are relatively new (with the inception date matching the plan management date). They suggested the funds should be reviewed over a full market cycle and are evaluating whether to begin the scoring process.

We compared average annual returns for one, three and five years for the 2035 and 2045 asset allocation funds in the city's plan to five similar funds on the open market. The funds offered in the city's plan underperformed the other funds for all periods except the one-year annual performance (see Exhibit 6). For example, over five years the city's 2035 asset allocation fund averaged annual returns net of fees of 7.03%; the comparison funds averaged 9.12% with the lowest 7.86% and the highest 10.14%.

Exhibit 6 Asset Allocation Fund Performance Comparison

2035

		Annual Performance		
	Symbol	**1 Year**	**3 Years**	**5 Years**
Voya Target Trust 2035	**N/A**	**-0.54%**	**8.33%**	**7.03%**
Voya 2035 Class I	ISQIX	-0.89%	9.70%	8.20%
Schwab 2035	SWIRX	-0.72%	11.26%	10.14%
Fidelity 2035	FFTHX	-0.88%	9.59%	7.86%
T. Rowe Price 2035	TRRJX	-0.52%	11.48%	10.11%
Vanguard 2035	VTTHX	-1.86%	10.55%	9.31%

2045

		Annual Performance		
	Symbol	**1 Year**	**3 Years**	**5 Years**
Voya Target Trust 2045	**N/A**	**-0.62%**	**9.36%**	**7.51%**
Voya 2045 Class I	ISRIX	-1.30%	10.89%	8.80%
Schwab 2045	SWMRX	-0.93%	N/A	N/A
Fidelity 2045	FFFGX	-0.82%	9.96%	8.06%
T. Rowe Price 2045	TRRKX	-0.51%	11.94%	10.40%
Vanguard 2045	VTIVX	-2.25%	10.94%	9.58%

Source: Asset Allocation Fund Comparison from Morningstar.com and Voya Fund Performance through December 31, 2015.

We recommend the management committee evaluate fund performance for all funds in the plan and consider substituting other assets that out-perform the current funds available in the plan.

The city does not track indirect compensation to Voya for services rendered under the contract, which totaled almost $1 million from July 1, 2014 through December 31, 2015. According to the contract, the plan is responsible for paying a monthly recordkeeping fee of $6.08 per participant per account, or Voya can offset the administrative expenses using revenue sharing arrangements with the third parties offering the investment funds within the plan. According to Voya representatives, the city selected the second option and Voya is compensated for its management services indirectly through the fund-level expenses borne by plan assets. Thus, participants pay for plan administration through fees included in the plan investment options. The contract established a 0.30% revenue sharing target to cover administrative expenses.

Voya does not disclose indirect revenue earned from the plans. The contract requires Voya to prepare and send invoices to the city for payment of charges associated with the recordkeeping and administrative expenses, if any, but the indirect compensation requires no invoicing because the city owes no reimbursable or compensable fees to Voya. Voya provides monthly statements to the finance department for the 401(a) account that summarize the account balances. Finance uses the reports to record assets and liabilities in the trial balance accounts associated with the defined contribution plan. The reports disclose direct compensation, such as loan origination fees, self-directed brokerage account fees, and Morningstar management fees, but do not disclose indirect compensation. The city does not receive monthly statements on the 457(b) plan.

Since the contract went into effect July 1, 2014, compensation from revenue sharing has exceeded the 0.30% annual target established in the contract. Voya provided us with an accounting of indirect compensation received related to the city contract through December 31, 2015. Compensation indirectly earned from the 401(a) and 457(b) accounts totaled $487,257 and $508,777, respectively (see Exhibit 7). The annualized revenue sharing amount over the 18 months totaled 0.325% of average monthly plan assets, 2.5 basis points above the target established in the contract to cover administrative expenses.

Exhibit 7 Indirect Compensation for Plan Management Services by Fund Offering

Fund Name	Net Expense Ratio	Fund Revenue	401(a) Revenue	457(b) Revenue	Total Revenue
Stable Value Option	0.75%	0.41%	$139,354	$198,888	$338,241
Voya Large Cap Growth Portfolio - Institutional Class	0.67%	0.30%	$895	$72,991	$73,886
American Funds EuroPacific Growth Fund - Class R-4	0.84%	0.35%	$9,563	$51,452	$61,015
Voya Fixed Account	NA	0.38%	$52,205		$52,205
Voya Target Solution Trust Fund: 2045 Fund - Class 11 CIT	0.70%	0.25%	$40,690	$155	$40,845
Voya Target Solution Trust Fund: 2035 Fund - Class 11 CIT	0.70%	0.25%	$36,935	$2,202	$39,137
American Beacon Holland Large Cap Growth Fd - Investor Cl	1.16%	0.35%	$25,837	$9,197	$35,034
Franklin Small Cap Value VIP Fund - Class 2	0.88%	0.45%	$15,454	$15,058	$30,512
JPMorgan U.S. Equity Fund - Select Class Shares	0.76%	0.25%	$6,478	$23,383	$29,861
Voya MidCap Opportunities Portfolio - Class I	0.80%	0.30%	$8,548	$20,650	$29,198
Voya U.S. Stock Index Portfolio - Institutional Class	0.27%	0.30%	$8,993	$18,323	$27,316
Voya Target Solution Trust Fund: 2025 Fund - Class 11 CIT	0.70%	0.25%	$25,767	$477	$26,244
Voya Solution 2045 Portfolio - Initial Class	0.89%	0.32%	$18,117		$18,117
Edgar Lomax Value Fund	0.96%	0.40%	$331	$16,311	$16,642
Voya Solution 2035 Portfolio - Initial Class	0.87%	0.32%	$14,664		$14,664
Voya Solution 2025 Portfolio - Initial Class	0.80%	0.32%	$12,682		$12,682
Voya Intermediate Bond Fund - Class I	0.33%	0.17%	$3,617	$9,010	$12,627
Wells Fargo Advantage Growth Fund - Class A	1.13%	0.55%	$10,544		$10,544
Invesco Comstock Fund - Class Y	0.58%	0.25%	$64	$10,347	$10,412
Ariel Appreciation Fund - Investor Class	1.13%	0.35%	$151	$10,149	$10,301
Touchstone Total Return Bond Fund - Class A	0.90%	0.40%	$156	$9,389	$9,545
American Beacon Mid-Cap Value Fund - Investor Class	1.15%	0.35%	$212	$9,132	$9,344
Invesco Mid Cap Growth Fund - Class A	1.19%	0.70%	$8,194		$8,194
Prudential High Yield Fund - Class Z	0.57%	0.25%	$114	$7,932	$8,046
Voya Target Solution Trust Fund: 2040 Fund - Class 11 CIT	0.70%	0.25%	$1,313	$6,716	$8,029
Voya Target Solution Trust Fund: 2020 Fund - Class 11 CIT	0.70%	0.25%	$902	$5,062	$5,964
Voya Target Solution Trust Fund: 2015 Fund - Class 11 CIT	0.70%	0.25%	$5,368	$507	$5,875
Pioneer Fund - Class A Shares	0.96%	0.60%	$5,631		$5,631
Voya Target Solution Trust Fund: Income Fund - Class 11 CIT	0.70%	0.25%	$4,494	$735	$5,229
Oppenheimer Capital Appreciation Fund - Class A	1.06%	0.50%	$4,999		$4,999
Voya Solution 2015 Portfolio - Initial Class	0.73%	0.32%	$4,514		$4,514
Voya Small Company Portfolio - Class I	0.85%	0.30%	$4,172		$4,172
Voya Target Solution Trust Fund: 2030 Fund - Class 11 CIT	0.70%	0.25%	$1,188	$2,721	$3,910
VY® Invesco Equity and Income Portfolio - Initial Class	0.65%	0.36%	$3,709		$3,709
Voya Target Solution Trust Fund: 2050 Fund - Class 11 CIT	0.70%	0.25%	$410	$3,132	$3,542
Voya Index Plus LargeCap Portfolio - Class I	0.44%	0.30%	$3,413		$3,413
Voya International Index Portfolio - Class I	0.48%	0.30%	$3,328		$3,328
The Brown Capital Management Small Company Fund - Inst	1.06%	0.10%	$408	$2,475	$2,882
VY® Clarion Real Estate Portfolio - Institutional Class	0.71%	0.28%	$381	$1,553	$1,935
Voya Intermediate Bond Portfolio - Class I	0.49%	0.17%	$1,443		$1,443
PIMCO VIT Real Return Portfolio - Administrative Class	0.65%	0.35%	$31	$666	$697
Voya Strategic Allocation Moderate Portfolio - Class I	0.70%	0.24%	$486		$486
Voya Target Solution Trust Fund: 2055 Fund - Class 11 CIT	0.70%	0.25%	$444	$8	$451
Voya Strategic Allocation Growth Portfolio - Class I	0.71%	0.24%	$420		$420
Voya Strategic Allocation Conservative Portfolio - Class I	0.65%	0.24%	$320		$320
Voya Solution Income Portfolio - Initial Class	0.68%	0.32%	$314		$314
TD Ameritrade - SDBO			$8	$154	$162
Voya Target Solution Trust Fund: 2060 Fund - Class 11 CIT	0.70%	0.25%	$1	$0	$1
		Total Indirect Revenue	**$487,257**	**$508,777**	**$996,034**

Source: Voya's Estimated Revenues for 401(a) and 457(b) through December 31, 2015

In its request for proposals for management services for the defined contribution plan, the city asked providers whether they would consider establishing an "ERISA budget" if compensation exceeded the target. An ERISA budget is an account that captures excess income collected by the recordkeeper that can be used to pay eligible plan expenses or be allocated back to participants. While Voya indicated its willingness to do so, the city has not established a mechanism to track or recapture the excess fee revenue paid from plan assets. We estimate excess revenue to be about $77,400 from July 2014 through December 2015. We cannot independently verify the compensation received through revenue sharing because there is no third party accounting. Because the city's plan is not subject to ERISA, Voya is not required to submit an IRS form 5500. The inputs to the calculations Voya provided us are consistent with other information either provided to the city or to plan participants.

The current contract states the total compensation amount payable to Voya by the city during the initial term of three years shall not exceed $2 million. During the first 18 months, indirect compensation totaled $996,034, while direct compensation associated with the plan was $73,507. According to the Law Department, total compensation includes all direct and indirect compensation paid to Voya. Because the finance department is unaware of the amount of indirect compensation paid from the plan, it is not monitoring to ensure compliance with the contract maximum payment amount, which will likely exceed $2 million as plan assets grow.

While indirect compensation from plan assets is a common practice, it has come under increased regulatory emphasis and has been the subject of litigation in private sector plans. Industry experts warn that revenue sharing arrangements may result in higher and less transparent fees. Even relatively small fee increases can have a large effect on participant returns over time. Under ERISA, which does not apply to the city, the plan sponsor has a duty to evaluate recordkeeper's plan fees and expenses to ensure fees charged to participant accounts and the plan are reasonable and accurate. Over the first 18 months of the contract the indirect revenue generated by fees exceeded what the monthly per participant fee would have been if the city had opted to pay it by about $278,000 (see Exhibit 8).

Exhibit 8 Comparison of Revenue Sharing to Per Participant Fees

Plan	# of participants x months x fee		Actual Indirect Revenue	Difference
401(a)	4,357 x $6.08 x 18 months =	$476,830	$487,257	$10,427
457(b)	3,303 x $6.08 x 12 months =	$240,987	$508,777	$267,790
		$717,817	$996,034	$278,217

Source: Voya Contract, Exhibit A.1, Plan Reviews for 401(a) & 457(b) as of September 30, 2015, Voya's Estimated Revenues for 401(a) and 457(b) through December 31, 2015

Industry experts also warn that revenue sharing arrangements could create potential conflicts of interest because the brokerage firms could have an incentive to promote funds that pay the most instead of those that are best for their clients. Under the contract, the city can request changes in fund offerings, but changes must be mutually acceptable and Voya reserves the right to amend the agreement, including pricing, to the extent that its revenue is reduced by a change in the investment products offered under the plan. Of the funds currently offered in the city plan, the lowest total fee is 0.27% and the highest total fee is 1.19%. Revenue sharing fees (the portion of the total fee that is returned to Voya) range from 0.10% to 0.45%. The asset allocation funds that are the default selection for city employees charge a total fee of 0.70% with a revenue sharing of 0.25%. The plan offers only one index fund, which typically have much lower fees than actively managed funds.

We recommend the chief financial officer request that Voya report all compensation, direct and indirect, to the city on a monthly basis for monitoring and contract compliance. The chief financial officer should also request that Voya create an ERISA budget for excess revenue captured during the contract period. We recommend the management committee review fees paid to ensure that they are reasonable. The committee should also assess whether the city should bear plan administrative costs rather than the participants.

Plan Administration Should Ensure Employees Are Promptly Enrolled in the Correct Plan

Best practices recommend auto-enrollment features; the city's manual processes pose risk of error. The city does not automatically enroll employees into a retirement plan. Staff in human resources is responsible for manually enrolling new hires into the correct plan based on turn-around documents provided by the hiring department. For employees hired in fiscal year 2015, the median time between hire date and Voya's enrollment date was 40 days.

Delays or errors in enrollment into the correct plan reduce employee benefits. Some employees who are not enrolled in a plan are put into the FICA alternative, which is intended for extra help or temporary employees who are not eligible for benefits. Six percent of their pay is withheld pre-tax and deposited in the alternative account, but they do not receive the city's matching contribution. In other cases, the employee and employer contribution are transmitted to Voya but are kept in a holding account pending enrollment.

The benefits division reviews pension plan assignments quarterly for accuracy. When an employee is enrolled in the wrong retirement plan, the division sends a letter to the employee explaining the retirement plan policy and their official enrollment date into the correct plan. Currently, there is no remediation to correct the error; the 401(a) does not receive rollovers, and the city does not reimburse its employees for lost profits or unmatched contributions. If the plan were subject to ERISA, the city could be liable for losses stemming from these errors.

As of January 2016, 20 full-time regular employees were listed as enrolled in the FICA alternative.

We recommend the chief information officer, chief financial officer and the commissioner of human resources implement auto-enrollment as a part of the Oracle upgrade, which should eliminate the errors associated with the manual processes.

Recommendations

To standardize plan design and ensure adequately funded retirement accounts, the chief financial officer and the commissioner of human resources should:

1. Prepare for City Council consideration analysis estimating:
   - costs associated with increasing the overall contribution rate to the defined contribution plan to the suggested level of 18% to 20% of annual salary
   - costs and benefits of adding the employees currently in the defined contribution plan to the city's hybrid plan

To reduce pre-retirement leakage and increase long-term investment goals associated with participant accounts, the management committee should:

2. Discontinue retirement fund loans from the 401(a) plan

3. Review training efforts at least quarterly and develop strategies to target training

To improve governance of plan management, the chief financial officer should:

4. Coordinate the appointment and election of management committee members and convene meetings and facilitate the meetings in order to ensure the defined contribution plan is managed according to the intent of Ordinance 11-O-0672
5. Request that Voya report all compensation, direct and indirect, to the city on a monthly basis for monitoring and contract compliance
6. Request that Voya create an ERISA budget for excess revenue captured during the contract period

To manage oversight of the plan, the management committee should:

7. Create a separate plan document, referring to the city code and contract where relevant
8. Assess the advantages and disadvantages to participants of holding plan assets in a group annuity plan versus a mutual fund company prior to procuring plan management services when the current contract expires
9. Evaluate fund performance for all funds in the plan and consider substituting other assets that out-perform the current funds available in the plan

10. Review fees paid to ensure that they are reasonable
11. Determine whether the city should bear or share the plan administrative costs with the participants

To prevent manual processing errors with plan administration, the chief information officer, chief financial officer and the commissioner of human resources should:

12. Implement auto-enrollment as a part of the Oracle upgrade, which should eliminate the errors associated with the manual processes

Appendix

Management Review and Response to Audit Recommendations

Report # 16.01	Report Title: Retirement Administration - Defined Contribution Plan	Date: 7/5/2016

Recommendation Responses

Rec. #1	The chief financial officer and the commissioner of human resources should prepare for City Council consideration analysis estimating the costs associated with increasing the overall contribution rate to the defined contribution plan to the suggested level of 18% to 20% of annual salary, as well as the costs and benefits of adding the employees currently in the defined contribution plan to the city's hybrid plan.	**Agree**

Response:	DHR agrees to work with the Chief Financial Officer to prepare and analysis estimating the cost associated with increasing the overall City's contribution to the defined contribution plan.
Proposed Action:	Finance and HR will develop cost estimates for both increasing funding levels for employees who only have a 401a account and the cost to move these employees to the hybrid plan.
Implementation Timeframe:	September 2016
Responsible Person:	

Rec. #2	The management committee should discontinue retirement fund loans from the 401(a) plan.	

Response:	Did not seek a response. Management Committee not formed as of July 2016.
Proposed Action:	
Implementation Timeframe:	
Responsible Person:	

Rec. #3	The management committee should review training efforts at least quarterly and develop strategies to target training.	
Response:	Did not seek a response. Management Committee not formed as of July 2016.	
Proposed Action:		
Implementation Timeframe:		
Responsible Person:		
Rec. #4	The chief financial officer should coordinate the appointment and election of management committee members and facilitate the meetings in order to ensure the defined contribution plan is managed according to the intent of Ordinance 11-O-0672.	**Agree**
Response:		
Proposed Action:	The CFO will continue to prompt the formation of the management committee	
Implementation Timeframe:	June 2017	
Responsible Person:	CFO	
Rec. #5	The chief financial officer should request that Voya report all compensation, direct and indirect, to the city on a monthly basis for monitoring and contract compliance.	**Agree**
Response:		
Proposed Action:	The CFO will request that Voya provide all compensation data to the City on a monthly basis.	
Implementation Timeframe:	September 2016	
Responsible Person:	CFO	

Rec. #6	The chief financial officer should request that Voya create an ERISA budget for excess revenue captured during the contract period.	**Agree**

Response:	
Proposed Action:	The CFO will request that Voya provide all compensation data to the City on a monthly basis.
Implementation Timeframe:	September 2016
Responsible Person:	CFO

Rec. #7	The management committee should create a separate plan document, referring to the city code and contract where relevant.	

Response:	Did not seek a response. Management Committee not formed as of July 2016.
Proposed Action:	
Implementation Timeframe:	
Responsible Person:	

Rec. #8	The management committee should assess the advantages and disadvantages to participants of holding plan assets in a group annuity plan versus a mutual fund company prior to procuring plan management services when the current contract expires.	

Response:	Did not seek a response. Management Committee not formed as of July 2016.
Proposed Action:	
Implementation Timeframe:	
Responsible Person:	

Rec. #9	The management committee should evaluate fund performance for all funds in the plan and consider substituting other assets that out-perform the current funds available in the plan.	
Response:	Did not seek a response. Management Committee not formed as of July 2016.	
Proposed Action:		
Implementation Timeframe:		
Responsible Person:		
Rec. #10	The management committee should review fees paid to ensure that they are reasonable.	
Response:	Did not seek a response. Management Committee not formed as of July 2016.	
Proposed Action:		
Implementation Timeframe:		
Responsible Person:		
Rec. #11	The management committee should determine whether the city should bear or share the plan administrative costs with the participants.	
Response:	Did not seek a response. Management Committee not formed as of July 2016.	
Proposed Action:		
Implementation Timeframe:		
Responsible Person:		

Rec. #12	The chief information officer, chief financial officer and the commissioner of human resources should implement auto-enrollment as a part of the Oracle upgrade, which should eliminate the errors associated with the manual processes.	**Agree**

Response:	DHR agrees with the recommendation that an auto-enrollment process should be implemented as a part of the Oracle upgrade and that this change will help to eliminate the errors associated with our current manual processes.
Proposed Action:	The CFO and CHR will include auto-enrollment in the scope of work for the Oracle upgrade. AIM will investigate the feasibility of including auto-enrollment in the Oracle R12 upgrade. Auto-enrollment is heavily dependent on a defined business process for appropriate employee retirement plan assignment.
Implementation Timeframe:	October 2017 or Oracle upgrade go-live date
Responsible Person:	