

**DEPARTMENT OF
FIRE AND POLICE
PENSIONS**

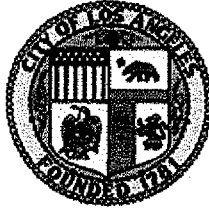
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CHIEF INVESTMENT OFFICER

April 26, 2012

Budget and Finance Committee
City Clerk, City Hall, Room 395
Los Angeles, CA 90012

ATTN: Erika Pulst, Legislative Assistant

Honorable Members of the Budget and Finance Committee:

In an April 19, 2012 correspondence, the Committee requested information on Best Practices within our respective field and how counterpart agencies have addressed common challenges. For pension systems, this information is not easily comparable since the Systems have various governing documents and may have different benefit levels. Further, this comparison is complicated by the fact that differences in funding levels lead to differences in the asset allocation plans, and to differences in expected investment returns.

Based on years of observations, however, I would offer the following as a best practice the City should follow when considering pension matters. The City should ensure that each of the involved entities (City Administrative Officer, Pension System, and Pension System actuary) independently confirms the estimated "savings" for a proposed pension change. This would allow the changes to be thoroughly vetted by each entity and for any differences to be either reconciled, or for the City Council to be aware of the differences prior to taking any action.

This up-front verification process should then be followed with a formal post implementation analysis, at a date certain time (i.e., one year after implementation). This will ensure information used by Council to make critical financial decisions is verified at a later date and, would allow the City to determine if improvements could be made to how savings are calculated.

This best practice process could be of tremendous value to the City going forward since recent changes to the pension benefits have projected significant savings, but these amounts may not have materialized as expected. For example, the Mayor and Council took significant actions in recent years to reduce payroll and the City contributions to the retirement Systems. These actions, the freezing of sworn health subsidies (CF 10-1868-S1) and the Early Retirement Incentive Program (CF 09-1320) both assumed savings that were used to justify actions in other areas. To my knowledge, there have not been formal "close-out" reports considered by Council of either action to quantify the actual savings. I



strongly encourage the Council to make it a policy, or law, to ensure projected pension savings are verified prior to finalizing any deal.

In terms of best practices within Los Angeles Fire and Police Pension (LAFPP), we regularly reviews operations to assess where improvements can be made. As such, the following are some of the more notable Best Practice efforts LAFPP has recently undertaken:

DEPARTMENTAL OPERATIONS:

1. Multi-year Strategic Plan developed and adopted annually by the Board of Fire and Police Pension Commissioners (Board);
2. Initiating a Governance Best Practices study in the 2012-13 Strategic Plan, approved by the Board on April 5, 2012;
3. Conducts an annual offsite educational Board meeting, within the downtown area, as recommended in the October 2007 Management Audit (Management Audit);
4. Regularly reviews and updates the Departmental Board Policies;
5. A Business Continuity Plan is underway to allow the department to continue providing vital services during a business disruption. This project was initiated several years ago and was also recommended in the Management Audit;
6. Regular participation at CALAPRS Roundtables, which allows LAFPP staff to meet with their counterparts from other California defined benefit retirement systems to share solutions to common issues and to discuss best practice solutions;
7. An Internal Audit Section was formed, consistent with the Management Audit and with professional standards for internal auditing, to review internal processes for efficiencies and ensure the proper management controls are in place throughout the department. An example of the value of this unit is demonstrated through a recent audit that will save approximately \$325K annually on DROP interest calculations; and,
8. Document imaging of all department records is underway and will lead to continued efficiencies in serving members and the costs of storing records offsite.

PENSION ADMINISTRATION:

1. Use of focus groups to evaluate existing Web-based member services with the goal to improve the website functionality and to reduce costs;
2. Regular audits of members over 90 years of age to ensure they are benefiting from their pension check as intended;
3. Triennial experience studies conducted to assess the reasonableness of the actuarial methods. This was also recommended in the Management Audit, but has been our policy for several years;
4. Point-of-Service surveys to track the satisfaction of member services, as recommended in the Management Audit; and,
5. A recent audit of L.A. Fire Relief demonstrated that the operational processes are effective, and identified some areas where efficiencies can be improved.

INVESTMENT PROGRAM:

1. Conducts an Asset Allocation study at least every three to five years, which results in an Asset Allocation Plan that provides adequate diversification and gives the expectation of the highest rate of return with an acceptable level of risk. This process was implemented prior to the Management Audit recommendation;
2. The Marketing Cessation policy stipulates that during the three months prior to the review of a contract with a firm currently under contract, the Board, Staff and General Consultant will cease communications with the contractor, other than those necessary to complete ongoing work;
3. Contractor Disclosure Policy was adopted in July 2007 with the purpose of preventing impropriety or the appearance of impropriety, to provide transparency and confidence in LAFPP's decision-making process, and to help ensure investment and procurement decisions are made solely on the merits of the goods or services proposed to be provided by Contractors to LAFPP. This Policy is in addition to, and is intended to supplement, any applicable state and city ethics, campaign finance, and lobbying laws at the State or local level; and,
4. Includes "Most Favored Nation Clauses" in investment contracts to negotiate fee reductions if an investment manager is hired by multiple City retirement systems for a similar mandate. This was also recommended in the Management Audit.

Please contact Bill Raggio at (213) 978-4553 if you should have any questions. Thank you.

Very truly yours,



Michael A. Perez
General Manager

c: President Robert von Voigt, LAFPP Board
Budget and Finance Committee:
Councilmember Paul Krekorian
Councilmember Mitchell Englander
Councilmember Tony Cardenas
Councilmember Paul Koretz
Councilmember Bill Rosendahl
Neil Guglielmo, Deputy Mayor
Miguel Santana, City Administrative Officer