DAVID E. JANSSEN
Chief Administrative Officer

June 7, 2005

The Honorable Board of Supervisors
County of Los Angeles
383 Kenneth Hahn Hall of Administration
500 West Temple Street
Los Angeles, CA 90012

Dear Supervisors:

AMENDMENT TO EXTEND FOR THREE YEARS THE CONTRACT FOR THIRD PARTY ADMINISTRATION SERVICES FOR DEFERRED INCOME PLANS (ALL DISTRICTS) (3 VOTES)

IT IS RECOMMENDED THAT YOUR BOARD:

Approve a contract extension for a three year term with Great-West Life & Annuity Insurance Company and affiliates (known as GWRS) as Third Party Administrator (TPA) for the Deferred Compensation and Thrift (Horizons) Plan, Savings Plan, Deferred Earnings Plan and Termination Pay Pick Up Plan (collectively known as the County deferred income plans) with an option to renew for two additional one year terms. Direct the Chief Administrative Officer, as Chair of the Plan Administrative Committees (PACs), to execute the contract extension after review as to form by the County Counsel.

PURPOSE/JUSTIFICATION OF RECOMMENDED ACTION

The County deferred income plans require a qualified third party administrator to provide the contracted services because the County does not have the professional expertise, systems, and commercial experience to perform the services. As the result of an industry wide competition, the GWRS contract for TPA services was first approved in 1997 for a five year term expiring in June 2002. Based on GWRS' competent performance and low cost, the contract was extended by your Board for al three year term, expiring in June 2005.

GWRS continues to provide competent custom plan infrastructure services that would be costly to replace and, in our opinion, could not be replaced in today's market at an actual cost that would justify the cost of replacement. The respective County deferred income PACs, which include Local 660 and Coalition of County Unions representatives relative to the Hoirizons and Termination Pick Up Plans, evaluate GWRS performance at quarterly intervals. Each PAC has unanimously endorsed the recommendation to continue with GWRS as TPA for the County deferred income plans for an additional term[1]. With approval of this second GWRS contract extension, third party administration of the Los Angeles County deferred income plans will continue uninterrupted until June 30, 2008. The contract amendment before your Board also provides for two additional one year contract extension options.

FISCAL IMPACT/FINANCING

It has been Board policy, since the first deferred income plan was created, that all costs of deferred income plan services must be charged to plan participants. As a result, no County financing is required. Expenses are financed exclusively through charges to the plan participants.

FACTS AND PROVISIONS/LEGAL REQUIREMENTS

The County deferred income plan trusts are required by law to operate for exclusive benefit of the plan participants and their beneficiaries. The contract extension with GWRS for a three year term, ending on June 30, 2008, will benefit plan participants by providing continuity at reasonable cost for record keeping, financial administration, investment transaction processing and communication services for the County deferred income plans.

Custom infrastructure to support unique features, large plan size and scope. The County of Los Angeles deferred income plans, as a group, are among the largest government defined contribution arrangements in the nation in terms of plan population and assets. The County deferred income plans have unique features that other plans do not have, including, but not limited to, fully segregated accounting, custom payment and cash management of unallocated cash assets. To accommodate the County deferred income plans size, complexity, and evolving needs, GWRS has created an extensive customized infrastructure to support plan systems, record keeping, investment transactions and administration. This level of customization of day-to-day services would be difficult to obtain elsewhere in today's market. Further, GWRS has been prompt in bringing difficult operating issues to our attention and has cooperated with us to resolve them.

Advantages of current operating arrangement. With $4.5 billion in assets, the County deferred income plans have the financial leverage to realize low actual TPA costs, while simultaneously extracting substantial cost discounts from investment managers. Current plan management takes advantage of that leverage for the participants' benefit.

[1] Pursuant to Sections 5.18.250C and 5.25.090.C.3 of the County Code, the Board has reserved the sole authority to contract with the TPA for the Horizons and Termination Pay Pick Up Plans. While County Code provisions governing the Savings and Deferred Earnings Plans provide that the PACs may approve all contracts for services, your Board has directed in the past that the TPA agreement for all plans be sent to the Board for final approval prior to execution.

The contract with GWRS is fully unbundled, so the plans pay only the actual costs for services provided, and there are no hidden costs. For example, Savings and Deferred Earnings purchase communication services from GWRS, but Horizons contracts with another vendor for such services. Unlike most other government plans, the County plans contract directly with investment managers for investments to obtain lower investment costs or discounts. These lower costs are passed on directly to plan participants as increased investment yield. The plans' funds are fully invested at all times and the plans, not the TPA, realize the investment float on substantial plan funds sitting temporarily in plan bank accounts.

By contrast, in bundled plans TPAs typically provide all services, including recordkeeping, investments, communication and marketing, in a turnkey arrangement. In such arrangements, TPAs and investment managers, which are often divisions of the same company, work together to market investments; and investment discounts may be passed on to the TPA by the investment manager as additional compensation to the TPA. In some cases, part of this additional compensation is used by the TPA to lower the price to the customer. However, the part of any investment discount not passed on to the customer is an actual cost to the customer. The true cost to the customer is usually difficult, if not impossible, to assess in these arrangements.

Pricing. GWRS has offered to continue current pricing with future annual increases limited by the County's standard COLA policy. Current pricing has two principal elements: an annual basic service charge and fixed transaction fees for resource intensive services, such as loan processing. The annual basic service charge is subject to an annual COLA. The other charges are fixed for the life of the contract extension.

Given the variety of pricing arrangements offered in the market place for TPA services, the only practical way to evaluate them on a level field is to compare total actual TPA costs to total assets. The current TPA costs compared to projected costs under the proposed GWRS contract extension are shown in the attached table.

As seen in the attached table, total TPA costs are projected to be 0.075% of Plan assets per year. This is comparable to the actual TPA cost for similar size plans with fewer features and less customization. The price range for most government plans is 0.100% to 0.200%, or more for off the shelf plan administration of less complex plans.

Contract enhancements. The contract extension provides additional or recently adopted services such as the pick up of termination pay initiated by your Board in late 2004, and segregation of County deferred income plan accounts in a separate general ledger isolated from the transactions of other GWRS customers. The contract has been upgraded to include new County standard terms and conditions not required by the Board when the contract was last extended in 2002.

Cost of replacement. In view of the expected expense of replacement, which plan participants would bear as well, GWRS competent performance, and low current TPA cost, we are concerned that replacement costs might outweigh any potential gain to participants. Based on actual past benefit contractor procurement experience, the estimated minimum cost to the plans of replacing the current TPA (not including County staff time chargeable to plan expense) would be approximately $150,000 for RFP consulting, $150,000 for transition management consulting and $700,000 start up cost, for a total cost of $1 million.

IMPACT ON CURRENT SERVICES (OR PROJECTS)

Competent services will be provided at a reasonable cost to County deferred income plan participants. Based on our history with GWRS, we would expect to continue to receive accurate and timely record keeping, high quality administrative services and effective communications services.

Respectfully submitted,

DAVID E. JANSSEN
Chief Administrative Officer and
Chair of the County Deferred Income PACs

DEJ:SRH
WL:FF:DT:df

Attachment

c: County Counsel
Executive Officer, Board of Supervisors
Auditor-Controller
Treasurer and Tax Collector
Director of Personnel
Each Member of the Deferred Income Plan Administrative Committee

Attachment

Projected TPA Cost[1]

Plan → Data ↓	Horizons	Savings	Deferred Earnings*	Total [2]
Current Total Assets	$3,452,000,000	$971,000,000	$63,200,000	$4,486,200,000
Projected 2005-06 Assets	$3,797,000,000	$1,068,000,000	$65,700,000	$4,930,700,000
Participants	62,223	10,188	692	73,103
Current 2004-05 Total Annual Fee:	$3,017,000	$564,000	$43,000	$3,624,000
(Based on Current Monthly Participant Fee of)	*($4.04)*	*($4.61)*	*($5.22)*	
Projected Total Annual 2005-06 Fee:	$3,091,000	$577,000	$44,000	$3,712,000
(Based on Projected Monthly Participant Fee of)	*($4.14)*	*($4.72)*	*($5.35)*	
Current Fee as % of Assets	0.087%	0.058%	0.068%	0.081%
Projected Fee as % of Assets	0.081%	0.054%	0.067%	0.075%

* Deferred Earnings investment return estimated at 4 percent

[1] The projected cost assumes the FY 2005-06 COLA will be limited to 2.5% consistent with the FY 2004-05 salary adjustments granted to most County employees, static plan membership and plan assets will increase by 10% due to contributions, withdrawals and investment returns (except Deferred Earnings which is closed to contributions).

[2] The Termination Pay Plan is not included in this analysis because plan assets and membership are very low, the plan was initiated in late 2004, there is little contribution history and retired participants may take distribution immediately after assets are contributed. Accordingly, we do not have enough experience to accurately determine what a stable level of assets or actual costs will be. At this time assets are less than $3 million, there are fewer than 100 participants and monthly fees are $3 per month