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**OFFICE OF THE
CITY TREASURER**

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May 30, 1991
A00577MM.MWG

City Council
Sacramento, California

Honorable Members in Session:

**SUBJECT: ALTERNATIVE GENERAL FUND REDUCTION -
OFFICE OF THE CITY TREASURER**

SUMMARY

This report responds to the City Council's request during the budget hearing of May 8, 1991 for additional information regarding the alternative General Fund reduction proposed by the City Treasurer. The alternative General Fund reduction recommends the recovery of Sacramento City Employees Retirement System (SCERS) investment and other costs in lieu of the reductions recommended by the City Manager's FY 1991/92 and FY 1992/93 Proposed Budget. It is requested that the City Council adopt the alternative General Fund reductions proposed by the City Treasurer.

BACKGROUND

Pursuant to the City Manager's request on March 11, 1991 the City Treasurer identified budget cuts to provide General Fund reductions in the Office of the City Treasurer's budget exceeding 20% of the proposed budget (see Attachment 1).

The proposed budget reductions do achieve immediate General Fund relief which was the purpose of the City Manager's request. However, the savings achieved by the proposed reductions could be overshadowed by either potential revenue and service reductions or by significantly higher costs of hiring outside money managers or financial advisors. For example, the City's charge for investment management services of City and SHRA funds is less than the

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external managers' charges for SCERS investment management services (see Attachment 2).

During the process of identifying the budget cuts, the City Treasurer directed staff to review every available alternative. Pursuant to the City Treasurer's direction, staff examined new revenue sources, recovery of costs of services provided by the City Treasurer, and expenditure reductions. However, Treasury staff could not fully develop the feasibility of all the available options in time to meet the budget deadline.

Ultimately, the result of this effort was the identification of three direct services provided by the Office of the City Treasurer for which fees are not presently assessed to recover costs. These services are:

1. SCERS investment management
2. Ann Land/Bertha Henschel investment management
3. City debt management (including IRS arbitrage calculations)

The City Treasurer requested that the City Attorney review the City Treasurer's costs for SCERS investment management to determine which of the costs, if any, could be recovered. (The City Treasurer did not pursue assessing Ann Land/Bertha Henschel investment management costs because the income from these trusts is used to assist the indigent needy in the community.) The City Treasurer is reviewing the City debt management costs and may propose a fee for this service. Debt management is becoming increasingly complex and time consuming. As of June 1991, the City Treasurer manages outstanding debt exceeding \$800 million and performs arbitrage calculations for 24 issues. The average minimum annual fee for arbitrage calculations by external consultants is \$1,500 per issue (see Attachment 3).

During the budget hearing on May 8, 1991, the City Treasurer advised the City Council that according to a preliminary determination certain costs could be recovered from SCERS. The City Treasurer proposed that the City Council consider the recovery of these costs and the elimination of the funding for the annual staff seminar as an alternative to the reductions recommended in the Proposed Budget. The City Council directed the City Treasurer to report back on the details of the alternative.

FINANCIAL

The City Attorney's analysis dated May 9, 1991 (see Attachment 4) lists specific costs that may be allocated between SCERS and the City. The portion of the costs exclusively related to, and therefore allocable to investment and management of SCERS assets and funds, may be charged to the assets of SCERS. The allocation must be supported factually by accurate, articulated data and reasoning. The analysis clearly states that City Treasury staff time can not be charged against the assets of SCERS.

According to the City Attorney, the City Charter would have to be amended in order to allow recovery of administrative costs such as staff time. Several other departments, including the City Attorney, Finance and Personnel, have significant costs relating to SCERS administration. The City Treasurer has identified annual Treasury staff costs in excess of \$170,000 related to SCERS. A decision to propose to amend the City Charter is a policy matter which is in the purview of the City Manager.

The City Treasurer has carefully reviewed the FY 1990/91, FY 1991/92 and FY 1992/93 operating costs of the Office of the City Treasurer to determine costs recoverable from SCERS. These costs are detailed in Attachment 5. The basis of the allocation is the specific use of these services for the SCERS investments managed by the City Treasurer. These allocations do not materially differ from allocations used previously to calculate the City cost recovery rate. The difference is attributable to the careful scrutiny and allocation of the operating costs prompted by the current budget shortfall.

The following schedule summarizes the General Fund reduction that is achieved by the recovery of SCERS direct investment costs and the elimination of the annual staff seminar:

<u>Description</u>	<u>FY 1990/91</u>	<u>FY 1991/92</u>	<u>FY 1992/93</u>	<u>Total</u>
SCERS Cost Recovery	\$ 44,449	\$ 44,449	\$ 45,449	\$134,347
Staff Seminar	<u>-0-</u>	<u>4,000</u>	<u>4,000</u>	<u>8,000</u>
	\$ 44,449 =====	\$ 48,449 =====	\$ 49,449 =====	\$142,347 =====

The total General Fund cost reduction of \$142,347 exceeds the reduction recommended (approximately \$125,989) by \$16,358. In addition, the potential reduction may increase due to a delay in

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filling the vacant position and by hiring at a lower step and level than that of the prior Investment Officer.

This alternative produces a win/win situation. The City Treasurer is able to maintain the management team and expertise necessary for continued operation of the Office while actually exceeding the cost reductions proposed by the City Manager.

POLICY CONSIDERATION

It is the City's policy to recover costs of operations when providing services unless it is in the public interest to subsidize programs.

MBE/WBE EFFORTS

Not applicable.

RECOMMENDATION

The City Treasurer requests that the City Council amend the City Manager's Proposed Budget for the Office of the City Treasurer to restore the Investment Officer II position, reflect the recovery of certain SCERS direct investment costs for FY 1990/91, FY 1991/92, and FY 1992/93, and reduce the FY 1991/92 and FY 1992/93 operating budget by \$4,000 budgeted each year for the annual staff seminar.

Respectfully submitted,



4 THOMAS P. FRIERY
City Treasurer

RECOMMENDATION APPROVED:



WALTER J. SLUPE
City Manager

June 19, 1991
All Districts

Contact person:

Michael L. Medema, Assistant Treasurer
449-5168

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March 11, 1991
A00489TF.MWG

TO: Ken Nishimoto, Budget Manager

FROM: Thomas P. Friery, City Treasurer

RE: Budget Cuts

Per the City Manager's request, I have identified three budget cuts which exceed the 20% maximum target. Frankly, none of the cuts identified make practical or fiscal sense. This office needs adequate professional administrative and technical support in order to function at the level of responsibility and performance demanded by the City Council.

Cutting the position of Assistant treasurer would reduce administrative control of the banking and operations, financing and investment functions. The duties would have to be performed by me, which would detract from my ability to respond to the City Council, the City's financial needs and assist the other City Council appointees in carrying out their duties. In addition, the investment program would suffer. The Assistant Treasurer provides support and back-up to the Investment Officers and directs the management of the investment portfolios in compliance with the Treasurer's approved investment strategy in the absence of the City Treasurer. Last year, this office earned for the City over \$51 million on the monies managed. A one percent reduction in performance would result in a loss of \$510,000.00.

The elimination of the internal management of SCERS would permit the cutting of an Investment Officer I/II position. However, based on the agreements with the current external managers, the cost of external management would be approximately \$200,000 for the first \$50 million managed with the fee for the remaining \$110 million

Ken Nishimoto
March 11, 1991
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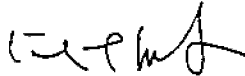
negotiable. This far exceeds the cost of the Investment Officer I/II. In addition, this would create a void in the management of Ann Land/Bertha Henschel Trusts and reduce the back-up coverage for the pooled portfolios. Finally, the Investment Officer I/II position provides the technical staff support to the SCERS Board to evaluate the external managers, research investment programs and to respond to inquiries regarding the Board's investment program and policies.

The final reduction to meet the 20% target is the elimination of the Deputy Treasurer/Financing. This position co-ordinates the City's financing needs, serves as the City's financial advisor and supervises the use and reporting of the financing proceeds. This position was added in FY 1989/90 to support the implementation of the City's five year capital improvement program. It is unlikely that an external manager could be retained to perform these duties. Recently, SAFCA retained a firm to assist in the development of a \$10 million financing at a cost of \$34,500. I would be remiss in not pointing out that this is only a small part of the work performed by the Deputy Treasurer/Financing.

As I previously stated, these cuts do not make practical or fiscal sense. The Office of the City Treasurer is the single largest revenue producer for the City and needs to maintain adequately trained professionals and support in order to function properly. I have not assigned costs to the cuts since the exact impact is difficult to estimate. However, I assure you that the costs will likely far exceed the limited General Fund savings that would result.

For example, due to the efforts of the Assistant Treasurer and the Investment Officer I/II, I recently implemented a change in the payment of banking services that will result in an additional \$121,000 in revenue to the City (\$29,000 General Fund). The Deputy /Financing is working on a refunding project that may save the City over \$330,000 annually. If the positions were eliminated, such innovation would not be forthcoming.

I realize the need for all of us to evaluate our programs for potential belt-tightening methods during this difficult fiscal time. My conclusion is that the Office of the City Treasurer is currently operating with the absolute minimum of resources required to fulfill our obligations in an effective and efficient manner.


4 Thomas P. Friery
City Treasurer

CITY OF SACRAMENTO
OFFICE OF THE CITY TREASURER

Investment Cost Recovery Analysis
FY 1990/91
(\$s in thousands)

<u>ACTIVITY</u>	<u>FUNDS MANAGED</u>	<u>MANAGER</u>		<u>FEES</u>	
		<u>Treas</u>	<u>Extern</u>	<u>Earned</u>	<u>Paid</u>
<u>Investments</u>					
Pool A	\$ 132,744	X		\$ 240	\$
Pool B	24,474	X		44	
Pool C	1,829	X		3	
Pool D	16,907	X		30	
Pool E	11,707	X		21	
Pool F	4,948	X		9	
Pool G	35,263	X		37	
Pool H	<u>40,090</u>	X		<u>42</u>	
	<u>267,962</u>			<u>426</u>	<u>-0-</u>
Ann Land/Bertha Henschel	<u>1,076</u>	X		<u>-0-</u>	<u>-0-</u>
Bond Proceeds	<u>61,690</u>	X		<u>-0-</u>	<u>-0-</u>
SCERS City	179,352	X		-0-	
Axe-Houghton	8,956		X		53
Batterymarch	10,279		X		159
Delaware	26,133		X		206
Lexington	12,010		X		84
Newbolds	22,963		X		158
WJS & Associates	<u>22,600</u>		X		<u>52</u>
	<u>282,293</u>			<u>-0-</u>	<u>712</u>
Total	\$ 613,021			\$ 426	\$ 712
	=====			===	===

CITY OF SACRAMENTO
TREASURER'S OFFICE
BONDS ISSUED SUBJECT TO REBATE CALCULATION

CITY OF SACRAMENTO	PAR BONDS	REBATE "FEE"
1987 COPs (Public Facilities Project)	\$41,650,000	\$1,500
1989 COPs (Community Center & Executive Airport)	96,540,000	1,500
1991 Refunding COPs (Light Rail)	32,040,000	1,500
1991 Refunding COPs (1987 Public Facilities)	44,865,000	1,500
	-----	-----
Subtotal City bond issues	215,095,000	6,000
ASSESSMENT DISTRICT 1915 ACT BONDS		
New Ramona Colony	2,580,095	1,500
South Land Park Hills Unit #24	39,207	1,500
Bell Avenue	3,566,864	1,500
G,H, 25th & 26th Street Alley	49,098	1,500
Robla Viejo	4,517,182	1,500
North Natomas	38,446,534	1,500
T, U, 18th & 19th Street Alley	47,735	1,500
Willow Rancho Street Lighting	41,278	1,500
Laguna Creek	10,357,745	1,500
Pocket Road/Greenhaven Drive	2,077,461	1,500
Main Avenue Sanitary Sewer	142,875	1,500
Freeport Village Street #3	66,212	1,500
Dreher Tract Street Lighting	8,384	1,500
Norwood/I-80 Business Park	462,955	1,500
Bruceville Road	369,992	1,500
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Subtotal assessment bond issues	62,773,617	22,500
SHRA TAX ALLOCATION BOND ISSUES		
1987 Merged Downtown Redevelopment Area	33,925,000	1,500
1989 Alkali Redevelopment Area	2,370,000	1,500
1989 Del Paso Redevelopment Area	2,275,000	1,500
1989 Oak Park Redevelopment Area	5,300,000	1,500
1990 Merged Downtown Redevelopment Area	78,435,000	1,500
	-----	-----
Subtotal SHRA tax allocation bonds	122,305,000	7,500
TOTAL ALL BONDS	----- \$400,173,617 =====	----- \$36,000 =====



MAY 13 1991

CITY
TREASUREROFFICE OF THE
CITY ATTORNEYSHARON SIEDORF CARDENAS
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ASSISTANT CITY ATTORNEYSR. DEPUTY CITY ATTORNEYS:
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WILLIAM P. CARNAZZOCITY OF SACRAMENTO
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May 9, 1991

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TIMOTHY N. WASHBURN
SABRINA M. THOMPSON
JOSEPH MCINERNEY
JOE ROBINSON
LESLIE R. LOPEZMEMORANDUM

TO: Michael Medema, Assistant City Treasurer

FROM: William P. Carnazzo, Senior Deputy City Attorney

RE: Recovery of SCERS Investment Costs

ISSUE

In your memorandum dated April 9, 1991, you asked for clarification as to whether certain of the actual, incurred costs of the Treasurer's Office are chargeable to the assets of SCERS under City Charter §393, or whether they are properly classified as "administration" costs and must therefore be absorbed by the City.

ANSWER

Consistent with the several opinions we have issued on this subject in the past, any item relating to staff costs of the Treasurer's Office falls on the "administration of the system" cost side of the line; other direct costs of managing and investing the assets and funds of the system are properly charged to the assets of SCERS. Where an item of cost has dual functions, an apportionment of the cost, based upon a reasonable and articulated factual analysis, must be utilized to segregate the cost, and allocate it between the City and SCERS.

ANALYSIS

We have issued a number of opinions on this subject in the past. Copies of these opinions, listed below, are attached for your reference and future use.

1. October 21, 1986--"Expense of Pension Plan Increment to LGFS". Here it was concluded that an allocable portion of the cost of developing the system was chargeable to SCERS assets. We cautioned, however, that care must be taken to exclude that portion of the cost which was allocable to "...staff time savings for the Treasurer in more efficiently performing the same tasks as he has always undertaken for the Board."

2. June 10, 1986 and May 12, 1986--"Expenses of the Utility Bond Substitute Program". Here it was concluded that the Treasurer's staff costs related to this program were administrative expenses not chargeable to the assets of SCERS.

3. November 18, 1982--"Custody Fees on S.C.E.R.S. Securities". Here it was concluded that fees paid to custodial agents as compensation for trust custodial services related to SCERS securities are chargeable to the assets of SCERS.

4. October 20, 1982--"Telegram Expense Associated With Gold And Silver Investment". Here it was concluded that the cost of telegrams sent by the Treasurer confirming authority in gold and silver investment transactions is an expense chargeable against the assets of SCERS.

5. May 4, 1982--"Expense of Telerate Financial System Display of Gold And Silver Trading Markets". Here it was concluded that because the Treasurer is the named manager for this portion of the portfolio, the allocable portion of the expense associated with the program is chargeable against the assets of SCERS.

6. December 8, 1981--"Audit of Retirement System Assets". Here it was concluded that the cost of the audit was an administration expense not chargeable to the assets of SCERS, since it does not relate to the investment of the funds or assets.

7. February 3, 1981--"Investment Cost Recovery Fee as Applied to Gross Income Earned by SCERS Assets Participating in 'Pool A'". Here it was concluded that this fee was not chargeable to the income from Pool A attributable to SCERS assets, since the fee represents the cost of providing the services and general overhead necessary to generate the income.¹

¹On page two of this opinion, there is a reference to the "Moneymax" system, but this cost is not separately dealt with in the opinion. If indeed the cost of that system could be broken out, and allocated as between SCERS and City funds in a reasonable, factually supportable and articulated manner, an allocable portion of the Moneymax system's actual cost could be charged to the assets of SCERS. Nothing in the February 3, 1981 opinion should be read to preclude that result.

Re: Recovery of SCERS Investment Costs

May 9, 1991

Page 3

8. December 12, 1980--"Administration Expenses of Retirement System". Here it was concluded that staff costs of the Treasurer's Office are not chargeable to the assets of SCERS, since they are properly classified as costs of "administration" of the system itself.

There is no need to repeat here the reasoning used in arriving at the conclusions contained in these opinions, since the analysis and application of Charter §393 is consistent throughout them. Applying that same analysis to your April 9, 1991 memorandum, we have reached the following conclusions:


1. The cost of Telerate Service, Moody's Investment Service, telephone charges and bank charges may be allocated between SCERS and the City. The portion exclusively to, and therefore allocable to investment and management of SCERS assets and funds may be charged to the assets of SCERS. This allocation must be supported factually by accurate, articulated data and reasoning, which should in turn be embodied in a report to the Board, for its approval. As I recall, this was done in connection with the expense for the creation of the LGFS system.

2. The expense attributable to City staff time making direct SCERS investments and in making buy and sell investments for professional financial advisors cannot be charged against the assets of SCERS.

3. In the event that there are other expenses which you wish to have charged against SCERS assets, we should review the item in each instance.

CONCLUSION

Consistent with the several opinions we have issued on this subject in the past, any item relating to staff costs of the Treasurer's Office falls on the "administration of the system" cost side of the line; other direct costs of managing and investing the assets and funds of the system are properly charged to the assets of SCERS. Where an item of cost has dual functions, an apportionment of the cost, based upon a reasonable and articulated factual analysis, must be utilized to segregate the cost, and allocate it between the City and SCERS.



WILLIAM P. CARNAZZO
Senior Deputy City Attorney

Att.

cc: Yvonne Berdan, Retirement Officer

ATTACHMENT 5

CITY OF SACRAMENTO
OFFICE OF THE CITY TREASURER

Direct SCERS Investment Costs
FY 1990/91, FY 1991/92 and FY 1992/93

<u>DESCRIPTION</u>	<u>FY 1990/91</u>	<u>FY 1991/92</u>	<u>FY 1992/93</u>
<u>Telephone & Telegraph</u> (23.2% SCERS)	\$ 1,369	\$ 1,369	\$ 1,369
<u>Rental Equipment</u>			
Telerate (50%)	17,400	17,400	18,400
Telerate Market News (50%)	1,680	1,680	1,680
<u>Data Processing</u>			
IDC Market Pricing (100%)	7,200	7,200	7,200
Telerate Pages (50%)	1,800	1,800	1,800
<u>Subscriptions</u>			
Moody's Public Utility (100%)	2,400	2,400	2,400
Moody's Investor Service (100%)	<u>12,600</u>	<u>12,600</u>	<u>12,600</u>
	\$44,449 =====	\$44,449 =====	\$45,449 =====