PORT OF SEATTLE
MEMORANDUM

COMMISSION AGENDA
ACTION ITEM

Item No. 4C

Date of Meeting March 22, 2016

DATE: March 14, 2016

TO: Ted Fick, Chief Executive Officer

FROM: Tammy Woodard, Assistant Human Resources Director, Total Rewards
Paula Edelstein, Senior Director, Human Resources

SUBJECT: Contract to Provide Record Keeping, Investing, Reporting, and Educational Services to the Port's 457 and 401(a) Deferred Compensation Plan participants.

Amount of This Request: $4,250,000

Source of Funds: Plan Participants' Accounts ($2.65M) as well as the General Fund and the Airport Development Fund ($1.6M)

ACTION REQUESTED

Request Commission authorization for the Chief Executive Officer to execute a contract to provide record keeping, investing, reporting, and educational services for the Port's 457 and 401(a) deferred compensation plans. The contract will be a five-year contract with the option to extend, subject to fee negotiations, up to an additional five years. The maximum value of the contract over 10 years is estimated at $4.25 million.

SYNOPSIS

The Port of Seattle offers deferred compensation plans as an important element of the Total Rewards package. These plans contribute to the Port's ability to attract and retain employees with the skills and abilities essential to achieving the Port's mission and goals. The Port's deferred compensation plans include a 457 deferred compensation plan that all regular employees may participate in to set aside pre-tax funds for their retirement. In addition the Port has three 401(a) plans, one that holds the limited matching contributions the Port makes to non-represented employees' 457 plan contributions, one for sworn Police personnel that holds the Port's contributions that are made in lieu of contributions to Social Security, and one for Firefighters that also holds the Port's contributions that are in lieu of contributions to Social Security. These plans are in addition to the State and union trust pension plans that Port employees participate in.

The Port contracts with a vendor to provide record keeping services as well as reporting, investing, and education services associated with these plans. The current contract, which expires in March 2017, is a flat rate contract. The current contracted fee is $60 per participant account per year. The fees associated with the employees' 457 plan accounts as well as the Police and Fire Departments' 401(a) accounts are paid by plan participants. The fees associated with the non-represented employees' matching 401(a) plan accounts are paid by the Port.

We are requesting authorization for the CEO to execute a five-year contract with the option to extend for up to five additional years based on negotiated rates for the second five years and a maximum contract value of $4.25 million. Plan participants (employees and retirees with account balances) will pay an estimated 62.5% of these fees, or a maximum of $2.65 million over the course of the 10-year contract. The Port will pay an estimated 37.5% of the fees, or a maximum of about $1.6 million over the course of the 10-year contract.

BACKGROUND

The Port of Seattle has offered a 457 Deferred Compensation plan since 1975. This plan is available to nearly all Port employees. The 457 plan is a supplemental retirement savings plan and is in addition to the pension plans administered by the State Department of Retirement Systems or union trusts that employees participate in. The 457 plan provides a retirement savings opportunity for employees to supplement their Port pension and any other retirement or pension benefits they may receive when they retire.

In 2000, the Port implemented a 401(a) Supplemental Savings Plan for non-represented employees that provides limited Port matching contributions ($1000 to $2200 based on Port service) to employees' 457 plan contributions. This plan supports employees saving for their retirement with the matching contributions and recognizes employee service by increasing the Port's contribution as employee's length of service increases.

In 2002, 401(a) plans were negotiated to receive Port contributions in lieu of Social Security for Uniformed Services employees, Police Officers and Firefighters, who do not participate in Social Security. The 401(a) plans are incorporated into these employees' collective bargaining agreements.

These 401(a) plans are also supplemental retirement savings vehicles and are in addition to the Department of Retirement Systems (DRS) and union trust pension plans that most employees participate in.

The vendor contract currently in place provides a variety of services related to these plans. Record keeping is a significant portion of the service the vendor provides. The vendor tracks employee and Port contributions, employees' investment earnings, and disbursements from the plan when employees retire and begin withdrawing their savings. Employees select how to invest their plan contributions from a variety of available investment options. The vendor maintains a record of plan participants' investment options and also executes changes to employees' investment choices by moving funds at employees' request.

Another service the vendor provides is reporting on plan participants' account balances. Plan participants can access their account online at any time to view balances and investments and to conduct investment transactions. Account statements are produced on a quarterly basis showing contributions, investments, investment earnings, plan fees, account distributions, and changes in how funds are invested. The quarterly reports also show participants the rate of return on their account. The vendor also provides online and ad hoc reports to the Administrative Committee that oversees the plan showing overall contributions and disbursements, total plan balances, the number of plan participants, how employees are electing to invest their funds and other information useful to the Committee to ensure the plan is providing value to participants.

In addition, the vendor provides onsite education services to plan participants to help them understand the plan and optimize their savings through the plan. These services are provided through periodic group information sessions on a wide range of retirement savings topics, individual consultations with a Retirement Plan Specialist, and individual sessions with a Certified Financial Planner. Education services are also available online, through virtual appointments, and by using the vendor's mobile app.

Finally, the vendor also provides various other administrative support services to the plan including processing loans available through the plan, administering the Hardship Withdrawal process, distribution services when plan participants are ready to begin withdrawing their account balances, and required tax forms when participants withdraw funds from their account.

The contract with the current vendor will expire in early March, 2017. If a new vendor is selected through the competitive procurement process there will be significant work required to transfer data and funds to the new vendor and the timing of the transfer will need to be communicated well in advance to plan participants as there will be a period of time when investment changes cannot be made. Interfaces that permit electronic transmittal of data and funds from the Port to the vendor will need to be updated to reflect a new vendor's record keeping system. To provide sufficient time to transition to a new vendor, if one is selected, we will need to issue the Request for Proposal by the end of March, 2016.

The transition to a new deferred compensation plan vendor, or any benefit plan administrator, requires Port systems and process to be updated to reflect the new vendor's way of doing business. The change will impact Port employees who interact with the vendor to administer the plan, as well as all employees, and former employees, who have deferred compensation account balances. These changes require time not only for the transition of data and funds, but also for staff administering the plan to understand all the different ways of working with a new vendor but also for plan participants to set up new online accounts and understand how to access information about their accounts and who to contact when they need assistance. Because these transitions typically take two and a half to three years to be fully worked through we are requesting authorization for a five-year contract with the option to extend, following fee negotiations, for up to five additional years.

FINANCIAL IMPLICATIONS

Budget Status and Source of Funds

The Port paid fees associated with this contract are included in the Port's benefits budget each year. They are incorporated into the total budgeted amount and then allocated to departments along with other benefits items such as life insurance premium costs, disability insurance costs, and medical and dental plan costs.

ALTERNATIVES AND IMPLICATIONS CONSIDERED

Alternative 1) – Join the State of Washington's Deferred Compensation plan rather than administering the Port plans as unique Port of Seattle plans.

As a subset of the State of Washington, the Port has the option to join their deferred compensation plan rather than maintaining our own

Cost: Approximately $4.9 million consisting of about $2.1 million, paid by participants, for the 457 plan and an estimated $2.1 million paid by the Port and $715,000 paid by participants for the 401(a) plans.

Pros:

- The State plan is a well-run 457 plan.

Cons:

- The State plan does not offer the loan provision the Port's plan does which permit employees to take a loan against their deferred compensation balance, essentially borrowing and paying back with interest, their own funds. This is an often utilized option within the Port plan and an option that about 60% of all government deferred compensation plans offer.

- The State plan does not offer the onsite or virtual education services the Port plan offers. These services are well utilized by participants in the Port plans and are reported by employees as having a high value.

- Participants would not have as close a connection to the Administrative Committee and would need to funnel their requests for changes to investment options, and potentially other changes, to committee members they do not work with.

- Participants would need to research and understand new investment options and make different investment elections with the State plan.

- The fee the State plan charges is a percent of participants' account balance whereas the Port's plan charges a flat fee. Based on 2015 year-end account balances, participants' fees would initially be about the same with the State plan as with the Port administered plan but would increase as their account balances grow.

- The State plan can only administer 457 plans; they are not be able to administer the Port's three 401(a) plans. It would be possible to move the Port's 457 plan to the state and maintain administration of the 401(a) plans at the Port. This would still require the Port to contract with a vendor to provide administrative services (record keeping, investment, reporting and education) to the 401(a) plans. Having a smaller total deferred compensation plan value would likely result in higher fees charged by vendors offering the plan administration services. The deferred compensation plan's consultant estimates fees to administer the 401(a) plans would be at least 30% higher than the fees to administer the larger combined plan. This equates to approximately $165,000 in additional costs for members of the Police and Fire 401(a) plans and $480,000 in additional Port expense for administration of the non-represented 401(a) plan.

<u>This is not the recommended alternative.</u>

Alternative 2) – Administer the Deferred Compensation plans in house.
Rather than contracting with a vendor to provide plan administration services the Port could self-administer this program.

<u>Cost:</u> See Below

Pros:
- Port staff would not need to complete a competitive procurement process every five to ten years or change vendors following a procurement process which would mean staff time could be devoted to other activities.

Cons:
- We are unable to estimate the cost of self-administering this program in hours as we are unable to identify any self-administered plans that we can consult with to estimate costs. The Plan's consultant is not familiar with any self-administered plans and the State of Washington utilizes a specialized vendor to administer their plan. We researched the plan offered by the State of New York, the largest deferred compensation plan in the nation, and they utilize a specialized vendor to administer their plan and were unable to assist us in estimating costs of self-administering the plan.

- Research through the National Association of Government Defined Contribution Administrators (NAGCDA), the industry association for governments offering plans like the Port's deferred compensation plans, reports using specialized vendors for plan administration as a best practice.

- As well as hiring additional staff to ensure employees with the knowledge and experience necessary to perform the services the vendor currently performs, the Port would also need to invest in a robust record keeping system that would accurately track the transactions and investments of participants' accounts. A very high level estimate from ICT is that the initial investment would be between $200,000 and $300,000.

- Self-administering the plan would expose the Port to the potential liability associated with investment or record keeping errors. In the rare situations when a vendor makes these errors, they correct them and absorb the associated costs.

This is not the recommended alternative.

Alternative 3) – Discontinue the Deferred Compensation plans.
The Port could opt to discontinue the deferred compensation plans and require that participants liquidate their accounts.

Cost: There would be some cost associated with closing down the plans, costs would depend on how the Port approached closing down the plans.

Pros:
- Port staff would not need to complete a competitive procurement process every five to ten years or change vendors following a procurement process which would mean staff time could be devoted to other activities.

Cons:
- Eliminating the deferred compensation plans would eliminate a valued element of the Port's Total Rewards Package and diminish the value of the Port's overall Total Rewards Package. This in turn would jeopardize our ability to attract and retain employees with the talents necessary to achieve the Port's goals and objectives.

- Many collective bargaining agreements list the 457 plan among the benefits offered to employees and both the Police and Fire 401(a) plans are part of the respective departments' collective bargaining agreements.

- We believe that if the Port were to eliminate the deferred compensation plans it might be possible to require all account balances be transferred to Individual Retirement Accounts (IRAs). This would preserve the tax-deferred status of participants' accounts. Simply eliminating the plan and paying out employees' account balances would subject employees to tax liabilities on their balances and potentially tax penalties as well.

This is not the recommended alternative.

Alternative 4) – Contract with a specialized vendor to provide record keeping, reporting, and education services to the Port and plan participants.

Cost: $1,600,000 in Port expense plus $2,650,000 in participant costs for a total of $4,250,000 over 10 years.

Pros:
- Contracting with a vendor specializing in deferred compensation plan record keeping, investing, reporting and education services will permit participants and the Port to receive an array of services at a reasonable cost.

- Utilizing a specialty vendor will ensure appropriate investing practices, accurate record keeping and reporting, compliant tax handling of the various types of money contributed to participants' accounts, as well as high quality education services that can help employees manage their accounts wisely and contribute to realizing their retirement goals.

- The Port currently contracts with a firm on the Small Contractors and Suppliers (SCS) roster to provide consulting and investment advising services to all of the deferred compensation plans. The need for this contract will continue as long as the Port continues to offer the deferred compensation plans.

Cons:
- Conducting a competitive selection procurement for a deferred compensation plan vendor will require about 300 hours of staff time to complete.
- If a new vendor is selected through the procurement, about 300 hours of staff time will be necessary to complete the transition to a new vendor.

This is the recommended alternative.

ATTACHMENTS TO THIS REQUEST

- None.

PREVIOUS COMMISSION ACTIONS OR BRIEFINGS

- None.