LAFPP
pension perspectives

January 2008

Newsletter for Active Members of Los Angeles Fire and Police Pensions

Inside

General Manager's **Message**

As you may know, there have been many articles in the press about the funding status of public pension funds. We are pleased to report that the Fire and Police Pension System had a return of 18.5% for the period ending June 30, 2007.

Due to these superior returns, and the returns of the last few years, the funded status of your pension system has improved from 94.7% to 99.2%.

With this funded status, we are in an elite group of public pension plans at or near 100% funding. In addition, we have prefunded our health benefits (since 1989), one of the few public pension systems in the country to do this.

For your own investments, staff has provided information in this newsletter to help you decide how to invest your assets, such as your investments in deferred compensation or DROP. I hope this information is useful as you continue to educate yourselves now and over the years in preparing for retirement from the City of Los Angeles.

Michael Perez
General Manager
Michael.Perez@lacity.org

Retirement Plan Fees and DROP

Comparing Investment Costs for DROP Rollovers

Submitted by: City of Los Angeles Deferred Compensation Plan

Note to Members: The following article was submitted for all participants of the Deferred Compensation Plan to provide some basic information on investing your assets and the costs and fees associated with investing. We hope you find the information useful. For any questions, you may contact a Deferred Compensation representative at (213) 978-1617.

Participants exiting DROP are faced with the challenge of deciding what to do with their DROP accounts. Leaving funds in DROP is not an option, and taking a full cash distribution generally won't make good tax sense. Many individuals roll their accounts to the City's Deferred Compensation Plan. Some may prefer to self-manage their accounts through an Individual Retirement Account (IRA), while others may seek professional investment management services. Regardless of your preference, it's important to understand how costs can vary depending on the type of investment vehicle chosen. This article will attempt to provide general information about potential costs in retirement investing so you can make informed choices.

Fees Matter. Some investors think certain investment choices or providers "don't have fees," or that investment fees are inconsequential because their investment will be growing in value. But evaluating fees should be as much a part of your decision-making process in retirement investing as it would be anywhere else. Just as if you were shopping for a new car or hiring a contractor, you need to know how much you will be charged before you can determine if the good or service is worth the price.

The Deferred Compensation Plan recognizes its obligation, as does any potential investment advisor or provider, to make this information clear so you can understand it in dollars and cents. If a potential financial services provider cannot do this and you continue to be confused, dig further. Here are some tips for asking the right questions.

1 Understand the Costs of Investment

Retirement plan fees and expenses can be described in different ways and using different terms. Let's break them down into three very broad categories:

- **Investment Cost**. Paying an expert to make investment decisions on your behalf. If you invest in a mutual fund, for example, you are paying a presumed expert, the fund manager, to invest your assets. Common terms associated with investment cost include "expense ratio" in a mutual fund or "investment management fee" for a

Retirement Plan Fees and DROP

Continued

personal investment advisor/ manager. Also included in this category are "early withdrawal penalties," common in certain mutual funds attempting to discourage frequent trading.

- **Administrative Cost.** The administrative (non-investment) costs of an investment; for example, issuing statements, operating a telephone service center or providing a Web Site. Common terms associated with administrative cost include "asset-based fee," "custodial fee," "trustee fee" or "record-keeping fee."
- **Sales Cost.** Fees paid to an investment provider or third-party broker to purchase, or exit, an investment. They are not part of all investment options but when present can be significant. Common terms associated with sales costs include "commissions," "front-end load," "back-end load," or "sales charge." Other charges may be applied if you transfer or withdraw your funds before a certain period of time — these include "contingent deferred sales charges," common in certain insurance company investments.

Not all investment vehicles will include all three types of costs or fees, and not all providers will communicate them to you in these terms. For example, a provider may not charge an explicit "administrative fee" but will pay its administrative costs out of revenue collected from its investment management fees. In addition, some fees are not "explicit" in the sense they are not discretely identified on an account statement. This is typical of a mutual fund, where its fee is collected out of your investment returns before those returns are paid to you. Sometimes a fee will appear at the front-end and be deducted from your initial deposit, and sometimes a fee will only appear later when you withdraw from an investment.

2 Know Your Deferred Compensation Plan Fees

In the Deferred Compensation Plan every effort is made to be fully transparent with fees charged in the Plan. Administrative costs are detailed on every statement, and investment management fees are provided in every quarterly newsletter. At $2.6 billion in assets, the Plan has negotiated extremely competitive investment and administrative costs. In addition, the City's Plan has NO sales costs associated with any of its investment options.

Also, the firm providing administrative services for the Plan (Great-West Retirement Services) has no relationship to any of the investment funds chosen for the Plan. Great-West local counselors are salaried and will not profit based on any investment you select. As a result, there is absolutely no motivation for the counselor to steer you into any particular investment product.

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Above: Fire Drill Tower 81 – September 2007

This may not be the case when it comes to outside financial services providers, who may be compensated from investments they direct you to.

Compare in Dollars and Cents

Using the City's Deferred Compensation Plan as a point of comparison, it is suggested that you nail down the relative costs of other options you might be considering. There are a wide variety of potential products, providers and fees, so think of the following illustration as a very general example of what the cost differential might be.

Let's say you have $100,000 in DROP and are debating rolling the funds to the City's Deferred Compensation Plan verses rolling them to an IRA that will be managed by an investment advisor. The advisor indicates he will charge a 1% annual management fee (investment cost), an amount fairly typical for these types of services. Let's say he indicates your account will be invested in a variety of mutual funds which, on average, have fund management fees (investment costs) of 1%. This equates to a total of 2% in "investment cost." Let's also assume you will be charged a front-end load of 3% (sales cost). Finally, let's assume any administrative costs associated with this investment are recovered out of other revenue collected by the provider.

The City's Plan has an administrative fee of 0.11% (sometimes referred to as "11 basis points") that is waived for DROP accounts. You will, however, be charged a $25 annual custodial fee. If you invest your money in one of the City's broadly diversified asset allocation funds (for example the "Conservative Profile Fund") you will pay a fund management fee of 0.10% ("10 basis points," equal to 1/10th of one percent). Again, there are no sales costs associated with any of the City's investment options. Here is how the cost of these two investments would compare in the first year.

Retirement Plan Costs	Deferred Compensation Plan	IRA With Financial Advisor
Investment Cost	$100	$2,000
Administrative Cost	$25	$0
Sales Cost (first year only)	$0	$3,000
Total Cost	**$125**	**$5,000**

Get it in Writing

The illustration provides a fairly dramatic illustration of the potential cost differential. Of course, the actual costs of any potential alternative could be higher or lower. The only way to know for sure is to require that a potential financial services provider disclose ALL fees to you, direct or indirect, explicit or implicit, on your investment and investment earnings on an annual basis, and ask for an illustration based on a hypothetical dollar investment (for example, $100,000). The provider should be able to verify to you, in writing, that this illustration represents all of the direct or indirect fees which would be assessed out of your investment or investment earnings. A Great-West counselor will be happy to provide you a similar illustration for the City's Deferred Compensation Plan. With both in hand, you can make apples-to-apples comparisons.

Consider Your Objectives

Consider what you're trying to achieve with the investment provider. For many of us, a certain level of anxiety is associated with making investing decisions. This is why many investors are willing to hand over that decision-making to a perceived expert. The Deferred Compensation Plan likes to remind investors there are three basic keys to successful investing: (1) identifying the level of risk you are willing to take; (2) diversifying your investment in a manner consistent with your risk tolerance; and (3) managing the cost of investment so that it doesn't eat too deeply into your returns.

The City's Deferred Compensation Plan is a City-sponsored employee benefit program. The Plan provides four local counselors who can help you identify your risk tolerance and match your investments to that risk tolerance. The City's Plan also has a range of low-cost investment choices to help manage the cost of investment. Because neither the contractor nor City staff who work with the Plan are compensated based on your investment choices, they can provide you with objective information if you need help evaluating your options. If this service is consistent with your objectives, cost might be a deciding factor.

Take Your Time, Preserve Options

Because you have to roll funds out of your DROP account upon retirement, you may feel you're under some pressure as you approach your final retirement date. One way to ease the pressure is by rolling your funds to the lowest-cost option (which may be the Deferred Compensation Plan) and taking time to investigate.
If you happen to be considering rolling both your DROP as well as the Deferred Compensation Plan accounts to an outside provider, remember that once you roll out everything you don't have the option of rolling back in. So, to keep all options on the table, consider leaving at least a small balance in the Deferred Compensation Plan.

If you've decided to roll your money to the Deferred Compensation Plan, you can call (888) 466-0381 to request the DROP rollover packet. You're also welcome to complete the forms necessary in person by visiting City Hall, 200 N. Spring Street, Room 867, Monday through Friday from 8 a.m. to 5 p.m. and speaking with one of the Plan representatives in the City's Employee Benefits Division.

Value Matters

Perhaps the most important thing to keep in mind is that value matters in retirement investing as much as any other area of life. Many individuals will spend weeks or months debating the purchase of a $25,000 vehicle, but only a few minutes deciding how to invest $250,000. Don't be shy in looking out for this significant asset you've accumulated. As always, you are your best advocate.

Representatives of the City of Los Angeles Deferred Compensation Plan are not registered investment advisers, and cannot offer financial, legal or tax advice. Please consult with your financial planner, attorney and/or tax adviser as needed. Please consider the investment objectives, risks, fees and expenses of any prospective investment carefully before investing.

Attention: All Members Who Intend to Enter or Exit Deferred Retirement Option Plan (DROP)

It is important to schedule an appointment with the DROP Section when you are ready to enter or exit DROP. You should do so once you have obtained the Letter of Intent to enter or exit DROP from your department retirement counselor's office. By scheduling an appointment with us, it will allow you to take full advantage of our services.

If entering DROP, we recommend:

1. Ensuring that your marriage or domestic partnership has an effective date of at least one year before your DROP effective entry date. In order for a spouse or domestic partner to qualify for survivor benefits, you must be married or have your Declaration of Domestic Partnership with the Fire and Police Pensions for at least one year *prior* to entering DROP, unless you have registered with the California Secretary of State and have met its distinct eligibility requirements.

2. Purchasing your drill tower/basic training time *before* entering DROP. ALL time must be purchased *prior* to your participation in DROP. No purchase will be allowed after you join DROP.

3. For Tier 2 members only: If you intend to purchase your Lost Service Time, it must be purchased *before* you enter DROP. No purchase will be allowed after you join DROP.

4. For members of Tiers 3, 4 and 5: If you intend to purchase your Workers' Compensation Time, it must be purchased *before* you enter DROP. No purchases will be allowed after you join DROP.

In other words, all years of service purchases must be made prior to your effective DROP entry date.

If exiting DROP, we recommend:

1. You understand how your DROP funds may be distributed to you: as a lump sum cash payment, a rollover, or a combination of these two.

2. You research your tax liability and the consequences associated with each type of distribution, or consult a tax advisor before making your election.

In a lump–sum cash distribution of funds, you are taking a direct payment of monies. When you take a roll-over, your DROP funds are transferred from the Department pension fund to another fund or investment vehicle (a qualified plan). The tax benefit of rolling over your funds to a qualified plan is you can postpone your tax liability, whereas taking a lump–sum distribution will incur taxes for the tax year you take the distribution. Please consult your tax advisor for advice concerning your specific situation.

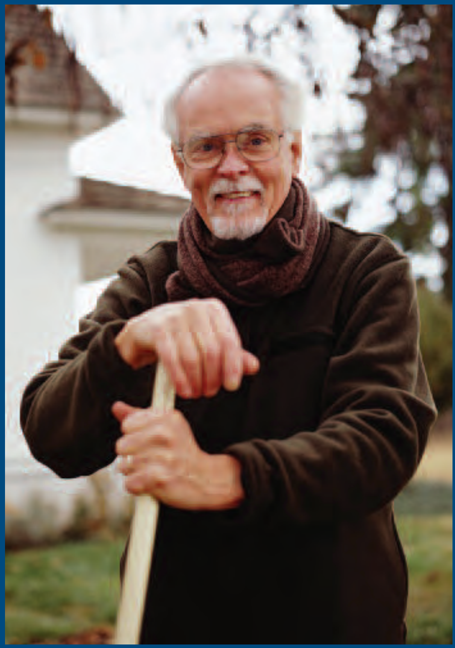
Important

Whether entering or exiting DROP, an appointment is necessary to meet with a DROP counselor.

For Police: Contact the DROP Section for an appointment once you have obtained a Letter of Intent to enter or exit DROP from your departmental retirement counselor's office.

For Fire: Contact a DROP counselor to obtain your Letter of Intent.

By scheduling an appointment with us, it will allow you to take full advantage of our services. If you do not have an appointment, staff will schedule one for you and you may return at that time. Please call the DROP Section at (213) 978-4495 or (800) 787-2489, ext. 84495# to schedule an appointment.



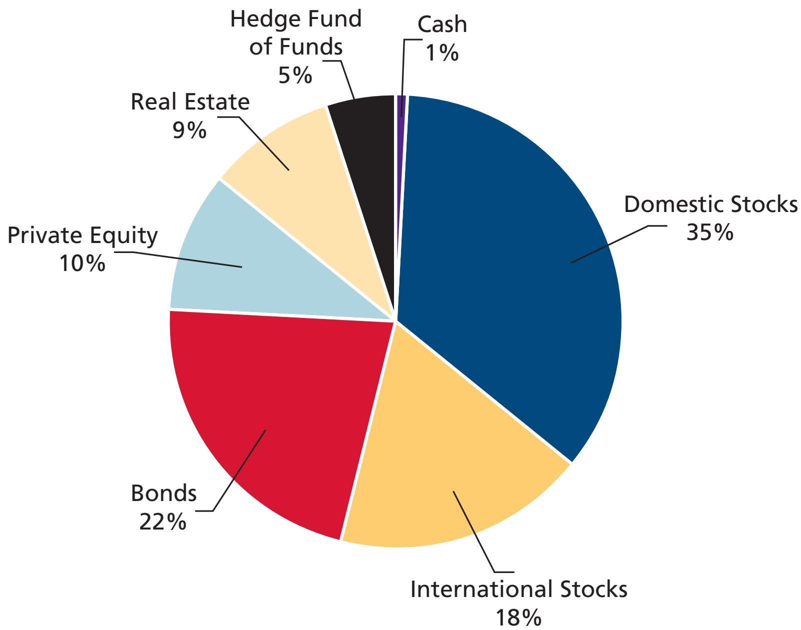
A Look at Our Current Asset Allocation Plan

At a recent meeting with delegates from the Police Protective League, we were asked about how Los Angeles Fire and Police Pensions (LAFPP) invests the assets of your pension system. In investing the funds of the Pension System, LAFPP follows the asset allocation plan recommended by a consultant and adopted by the Board of Fire and Police Pension Commissioners in 2006. Please note that the consultant recommending this plan to us does not have a monetary interest in where we actually invest our assets.

The asset allocation plan establishes the blueprint for investing the System's assets because it states how much of the System's assets may be invested in a particular asset class. This plan is primarily responsible for our long-range investment performance. In fact, over 90% of our performance can be attributed to this plan. The rest is based on the investments selected by our investment managers.

Assets are periodically re-balanced to achieve the target percent per asset class. All of the System's assets are managed by our 36 investment managers. As of the end of November 2007, the total assets of the Pension System totaled just over $16 billion.

Information on our current asset allocation plan is provided below.



Board of Fire and Police Pension Commissioners Active Fire Member Re-elected

Michael J. Carter was re-elected as the Active Fire Member to the Board of Fire and Police Pension Commissioners in an official election conducted on April 24, 2007. His term is for five years, which began July 1, 2007 and ends June 30, 2012. Please join us in congratulating Commissioner Carter!

Pre-Retirement Planning for Younger Members Getting Started Early on a Retirement Plan

"Very good information. Wish I had it ten years ago!"
"Should encourage younger employees to attend!"

These are just some of the comments submitted by LAFD and LAPD members who have attended a pre-retirement seminar as they neared retirement.

The "Planning for Your Future" seminar format—targeted for Tier 5 members with 10 years of service or less—has been updated to provide you with the tools to get started on a retirement plan. This new seminar format was presented to our first group and the ratings were excellent!

Here are just some of the topics covered:

- Tier 5 Pension Benefits
- Defining Your Retirement Goals
- Debt Management
- Estate Planning
- Investments
- Life Insurance

We encourage you to take advantage of the opportunity to attend this seminar. Retirement planning is something you must actively prepare for.

Here's how the process works:

- Invitations to the pre-retirement seminars are mailed to members according to seniority.
- If you get an invitation in the mail, send back the response and reserve your spot for that seminar.
- Confirmation letters are sent to members who are selected.

Don't wait until you are near retirement age to take advantage of this valuable information. The decisions you make now can make a big difference in how financially secure your retirement will be. Also, before you retire, there will be another opportunity to attend a seminar that will help you wrap up the details and ease you into retirement.

Check our Web site at www.lafpp.com for future dates. If you have any questions, please contact Communications and Special Projects at (213) 978-4530 or (800) 787-2489, ext. 84530#.

Taxability of Service Pensions!

Pension income is subject to federal income tax. However, part of your pension may not be taxed based on any after-tax contributions you may have made to the Pension Plan.

After-Tax verses Pre-Tax

From July 1, 1982 through November 21, 1996, mandatory member contributions were made on an "after-tax" basis. This means you paid withholding taxes on your income before contributions were deducted. Because this money was taxed when contributed to the Plan, it will be tax-free when received as part of your monthly pension benefit.

For all other periods, mandatory member contributions were made on a pre-tax basis. This means your contributions were deducted from your paycheck before income tax withholding was calculated. These amounts are "tax-free" when you contribute them. Therefore, the pension benefits provided by these contributions are taxable when you receive them at retirement.

For members who have contributed on both a pre-tax and post-tax basis, your pension check will reflect the combination. You will be advised of the breakdown of what portion is free of federal income taxes and what portion is taxable. The combination will continue until you have recovered all of the after-tax dollars you contributed to the Plan. Thereafter, your entire pension payment will be taxable as ordinary income.

Determining Taxability

For pensions effective on or after January 1, 1998, the formula we use to determine the amount of your benefit that is taxable verses the amount that is tax-free, is the "Simplified Method" formula developed by the IRS. The tax-free portion is based on the amount of your after-tax contributions at retirement, and your age (plus your spouse's age, if applicable) when you begin to receive pension benefits.

The formula determines the amount of your pension that will not be taxed and the length of time for that exclusion. By subtracting the tax-free amount from your gross pension for a fixed number of months, your already-taxed contributions will be recovered. Cost-of-living pension increases will not change or have any effect on the tax-free amount since the calculation is based upon your original retirement allowance.

For more information on the Simplified Method formula, please visit our Web site at www.lafpp.com. If you have any questions, contact the Retired Member Services Section at (213) 978-4495 or (800) 787-2489, ext. 84495#.

Register Your Domestic Partner With Los Angeles Fire and Police Pensions

If you want your domestic partner to be eligible to qualify for survivor benefits, you *must* file a Declaration of Domestic Partnership with Los Angeles Fire and Police Pensions (LAFPP), unless you have registered with the State of California having met its distinct eligibility requirements. Registering your domestic partnership with the Personnel Department does NOT make your domestic partner eligible for survivor benefits from the LAFPP.

To file with the LAFPP, same-sex couples and opposite-sex couples must meet our domestic partnership requirements, complete a Declaration of Domestic Partnership form and submit it with any requested documentation to the Active Member Services Section of LAFPP. Please note that registration of your domestic partnership with LAFPP does not create community property rights in your pension benefits.

Upon receipt, Active Member Services will send a confirmation letter to you with the effective date of your Declaration. The effective date is used to meet various survivor eligibility requirements.

For example, you must have a Declaration of Domestic Partnership on file with LAFPP *at least one year prior* to:

- the effective date of a service pension; or,
- the effective date of DROP entry

These and other domestic partner benefit eligibility requirements and information are posted on our Web site at www.lafpp.com under "Plan Details," then "Domestic Partnerships." To download the Declaration from our Web site, select the "Forms" icon.

To request a Declaration by mail or for more information about filing a Declaration of Domestic Partnership with LAFPP, please contact Active Member Services at (213) 978-4522, (800) 787-2489, ext. 84522#, or email us at pen.pensions@lacity.org.

Above: Graduate from Fire Drill Tower 81

CONTACT INFORMATION

Department of Fire and Police Pensions

Our staff is available to assist you Monday through Friday (except Holidays) from 8 a.m. to 5 p.m. Please refer to the following directory so that the right staff member can address your specific need. When calling on the toll-free number, use the extension number provided for each section, followed by the pound sign.

Active Member Services
(213) 978-4522 (or 84522#)

- Annual Member Statements
- Beneficiary Statements
- Contribution Accounts
- Dissolution-of-Marriage Information
- Domestic Partnership Forms
- Service Credit and Bad Time (Lost Service Time) Purchases

Communications and Special Projects
(213) 978-4530 (or 84530#)

- Benefit Presentations
- Newsletters
- Pre-Retirement Seminars
- Department Web Site

Medical and Dental Plans (for Pensioners Only)
(213) 978-4560 (or 84560#)

- Health Insurance Subsidy
- Dental Insurance Subsidy
- Health Insurance Premium Reimbursement Program

Disability Pensions
(213) 978-4500 (or 84500#)

- Active Member Deaths/Survivor Pensions
- Disability Application Processing
- Disability Pension Reviews
- Review of Dependent Children/ Dependent Parent Qualifications

Service Pensions
(213) 978-4575 (or 84575#)

- Service and Survivor Pension Processing and Inquiries
- Retired Member Records and Information
- Change of Address (for Pensioners Only)
- Discontinuance of Benefits (Upon Death or Other Ineligibility)

Retired Member Services (for Pensioners Only)
(213) 978-4495 (or 84495#)

- Direct Deposit
- Tax Withholding
- Cost-of-Living Adjustments

DROP Administration
(213) 978-4568 (or 84495#)

- Information on the Deferred Retirement Option Program

Other Ways to Contact Us

Toll-Free: (800) 787-CITY (2489)
Fax: (213) 978-4450
TDD: (213) 978-4455
Email: pen.pensions@lacity.org
Web Site: www.lafpp.com
Address: 360 E. Second Street
Suite 400
Los Angeles, CA 90012
Mail Stop: 390

For your convenience, the following forms can be printed from our Web site: Beneficiary Form, Deferred Compensation Incoming Transfer/Direct Rollover Form, Domestic Partnership Declaration Form, Notice of Termination of Domestic Partnership Form, DROP Beneficiary Form, DROP Distribution and Election Form, and Request to Purchase Service Credit Form.

Millennium Bill Emergency Care
For Veterans

The Department of Veteran Affairs (VA) has the authority to pay for emergency care in non-VA facilities for eligible veterans who are enrolled in the VA health care system. The VA will pay 70 percent of the rates that Medicare considers "allowable" and the non-VA facility will accept VA payment as payment in full.

Eligibility

This benefit does not apply to all veterans.

You qualify if you answer "yes" to the following:

- Are you enrolled in VA health care?
- Have you been seen by a VA health care professional within the preceding 24 months?

And, you answer "no" to the following:

- Do you carry any form of health insurance coverage, including Medicare, Medicaid or workers' compensation?

  This benefit was established as a safety net for veterans who have no other health insurance. The VA strongly encourages veterans to retain any current health care coverage for the following reasons:

- Not all care provided in an emergency room may be considered emergency care;
- Spouses generally do not qualify for VA health care and if insurance is cancelled, the spouse may lose coverage too.
- Veterans could be personally liable for medical bills if they decided to drop their Medicare Part B coverage or their personal health insurance coverage.

Veterans, who have any questions concerning eligibility, should contact their local VA medical center. To locate your local medical center, call VA's health Benefit Service Center at (877) 222-VETS (8387).

LAFPP

Los Angeles Fire and Police Pensions
Mail Stop #390
360 East Second Street
Suite 400
Los Angeles, CA 90012

Return Service Requested