AGENDA: 5

Bay Area
Air Quality
Management
District

OPEB and Pension Funding Policy

Budget and Finance Committee Meeting
October 26, 2022

Stephanie Osaze
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Presentation Outcome

- The Committee will consider recommendation to approve the policy to the full Board of Directors.

Presentation Outline

- Plan Overview
- Policy Overview
- Recommendation

Requested Action

- The Committee will recommend that the Board of Directors approve the policy.

Plan Overview

1. Other Post-Employment Benefit Plan (OPEB) - Medical Retirement Benefits

2. California Pension Employers’ Retirement System (CalPERS)- Pension Retirement Benefits

Plan Overview
Other Post-Employment Benefits (OPEB)

To address the rising unfunded liabilities for OPEB, the Board approved:

- Target funding level of 90%.
- Invest $4 million (M) in annual discretionary funds.
- California Employers' Retirement Benefit Trust (CERBT) to invest discretionary funds.

Plan Overview
CalPERS Pension Plan

To address the rising unfunded liabilities for Pension, the Board approved:

- Target funding level of 90%.
- Set aside $1 million (M) in annual discretionary funds.
- California Employers' Pension Prefunding Trust (CEPPT) to invest discretionary funds.

Plan Overview
Funding of Retirement Liabilities

- **Medical Retirement (OPEB):**
  - Obligation: $73 M
  - Funded: $75 M (103%)
  - Surplus: ($2M)
- **Funding Policy:** 90% Funded Level
  - Current Funding Level at 103%*
  - **Redirect $4 M Annual Discretionary Funding to CalPERS Pension after reaching target funding level**

- **CalPERS Retirement (Pension):**
  - Obligation: $358 M
  - Funded: $258 M (72%)
  - Unfunded: $100 M (28%)
- **Funding Policy:** 90% Funded Level
  - 90% Target Date (FYE 2039)**
  - $1 M Annual Discretionary Funding
  - $4 M Redirect Discretionary Funding from OPEB

* Based on 2021 actuarial valuation

** Based on 2020 actuarial valuation

Policy Overview

PURPOSE:

- Formalize current practice of funding both the OPEB and Pension plans.
- Outline the overall funding goals and approach in achieving those goals.

Policy Overview
OPEB Medical Plan

OBJECTIVE: To accumulate sufficient assets to fully fund retiree healthcare benefits.

GOALS:

- Continue to make discretionary $4M contribution annually.
- Budget and pay the retiree healthcare premiums for current retirees.
- Strive to maintain minimum 90% funding level in the trust.

Policy Overview
OPEB Medical Plan (cont.)

GOALS Continue:

- If plan reaches 100% funding level; redirect the $4M discretionary contributions to the pension trust account.

- In case of a fiscal hardship or OPEB plan becomes super funded, Board may elect to use the funds in the OPEB trust to pay retiree health premiums.

Policy Overview
CalPERS Pension Plan

OBJECTIVE: To fund the actuarially determined contributions for employees and retirees to ensure benefits can be paid as promised.

GOALS:

- Budget and pay the annual required pension payments to CalPERS.
- Continue $1M annual discretionary contributions to the pension trust account.
- If applicable, redirect and invest up to $4M annual discretionary contributions designated for OPEB to the pension trust account.

Policy Overview
CalPERS Pension Plan (cont.)

GOALS Continue:

- Strive to maintain minimum 90% funding plan level.

- If CalPERS pension plan becomes 100% funded; redirect discretionary contributions at Board’s discretion.

- In case of a fiscal hardship or pension is super funded, Board may elect to use the funds in the trust to pay required pension payments to CalPERS.

Recommendation

The Committee will consider recommending the Board of Directors approve the Other Post Employment (OPEB) and Pension funding policy.

AGENDA: 6

California Employers' Pension Prefunding Trust (CEPPT) Investment Policy

Budget and Finance Committee Meeting
October 26, 2022

Leonid Bak
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Presentation Outcome

The Committee will consider recommending to the Board of Directors that the Board adopt a funding allocation and choose an investment strategy for the California Employers' Pension Prefunding Trust (CEPPT).

Presentation Outline

- Overview of CEPPT Investment Strategies
- Staff Recommendation and Discussion of Investment Policy
- Next Steps

Presentation Requested Action

Consider recommending to the Board of Directors to adopt an appropriate investment strategy for participation in CEPPT and decide on funds allocation.

CEPPT Investment Strategies – Strategy 1

- The CEPPT Strategy 1 portfolio is invested in various asset classes that are passively managed to an index.
- CalPERS periodically adjusts the composition of the portfolio in order to match the target allocations.
- This portfolio has a higher allocation to equities than bonds, i.e., seeks higher returns, but assumes greater risk.

Asset Class	Target Allocation	Target Range	Benchmark
Global Equity	40%	± 5%	MSCI All Country World Index IMI (Net)
Fixed Income	47%	± 5%	Bloomberg US Aggregate Bond Index
Treasury Inflation-Protected Securities ("TIPS")	5%	± 3%	Bloomberg US TIPS Index, Series L
Real Estate Investment Trusts	8%	± 5%	FTSE EPRA/NAREIT Developed Index (Net)
Cash	-	± 2%	91-Day Treasury Bill

CEPPT Investment Strategies – Strategy 2

- Compared with CEPPT Strategy 1, this portfolio has a lower allocation to equities and a higher allocation to bonds.
- Historically, funds with a lower percentage of equities have displayed less price volatility and less fluctuation of value, i.e., lower risk.

Asset Class	Target Allocation	Target Range	Benchmark
Global Equity	14%	± 5%	MSCI All Country World Index IMI (Net)
Fixed Income	73%	± 5%	Bloomberg US Aggregate Bond Index
Treasury Inflation-Protected Securities ("TIPS")	5%	± 3%	Bloomber US TIPS Index, Series L
Real Estate Investment Trusts	8%	± 5%	FTSE EPRA/NAREIT Developed Index (Net)
Cash	-	± 2%	91-Day Treasury Bill

CalPERS Pension Retirement Plan

To address the rising unfunded liabilities for Pension, the Board approved:

Pension Policy:

- A funding target level of 90%.
- Set aside $1 million (M) in annual discretionary funds.
- As of Fiscal Year Ending (FYE) 2022, set aside is $5M (five years).

Recommended Funds Allocation

- Since 2008, the Air District has made payments up to $4 million to prefund OPEB.
- At present, OPEB prefunding status is at 103%.
  - As a result, the Board approved the $4 million in discretionary contributions for the FYE 2023 Budget to be redirected for pension purposes – to the CEPPT 115 Trust Account.
- Recommendation: transfer the accumulated $10 million to the CEPPT 115 Trust Account in 2 tranches:

  1. $5 million after the Committee approves the action – this is the amount set aside annually for pensions between FYE2018 and FYE2022, $1 million each year;
  2. $5 million at the end of FYE2023 – this is the amount approved in FYE 2023 for OPEB and pension.

Recommendation

Consider recommending the Board of Directors that the Board adopt the following for CEPPT 115 Trust:

1. Direct investments in the Air District’s CEPPT 115 Trust account to use strategy 2.
2. Allocate Air District’s funds to the CEPPT 115 Trust account in 2 tranches:
    1) Following adoption of the recommendation.
    2) At the end of FY2023.

AGENDA: 7

BAY AREA AIR QUALITY MANAGEMENT DISTRICT

Pathways to 100 Percent Cost Recovery

Budget and Finance Committee Meeting
October 26, 2022

Leonid Bak
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Presentation Outcome

The Committee will be updated on the Air District’s pathways to achieve 100 percent cost recovery based on the Matrix study proposals.

Presentation Outline

- Background
- Overview the main scenarios from the Matrix study
- Model assumptions
- Model results
- Summary and Conclusions

Presentation Requested Action

For information only.

Brief History
Fees and Cost Recovery Overview

Cost Recovery Policy Established in Fiscal Year Ending (FYE) 2012:

- Air District can recover 100% of costs through fees
- 85% minimum cost recovery target
- 6% average annual fee increase
- Regulated community gains predictable fees
- Established Budget Advisory Group in 2020

Summary of Matrix Study Options

Cost Recovery – Options Overview

- **Project objective:** Achieve 100% Overall Cost Recovery
- Four different options were evaluated based upon individual fee schedules and overall Air District cost recovery:

#	Option Description (Based on Individual Fee Schedule Cost Recovery)	# of Years to Overall 100% Cost Recovery
1	• Less than 110% = 15% Increase • 110%+ = 0% Increase	5
2	• Less than 100% = 15% Increase • 100%+ = 5% (CPI-W) Increase	5
3	• Less than 85% = 15% Increase • 85%+ = 5% (CPI-W) Increase	10+
4	• 15% Increase to All Fee Schedules	2

→ <u>**These scenarios assume no changes in staffing levels, priorities, workload, or reduction of existing backlog.**</u>

→ <u>**Some fee schedules still take 10+ years to get to 100%.**</u>

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matrix consulting group

- In April 2022, Committee recommended that the Air District analyze projected outcomes and impacts under Options 1 and 2.

- Matrix's conclusions on years to 100% CR under all options are crucially based on a few basic, but rigid assumptions – fixed spending, fixed staff count, fixed workload, fixed priorities.

Summary of Assumptions

When modelling our cost recovery, Air District made every effort to maintain the same parameters as in the Matrix study. The result was broadly similar, with some adjustments to account for new data.

In order for the model to work, 3 broad groups of assumptions were made:

1. ***Impacts*** to the Air District's budget and operations from ***macroeconomic shifts*** – e.g., higher inflation/COLA for FYE2024-26, vacancy savings, stable property tax revenue;

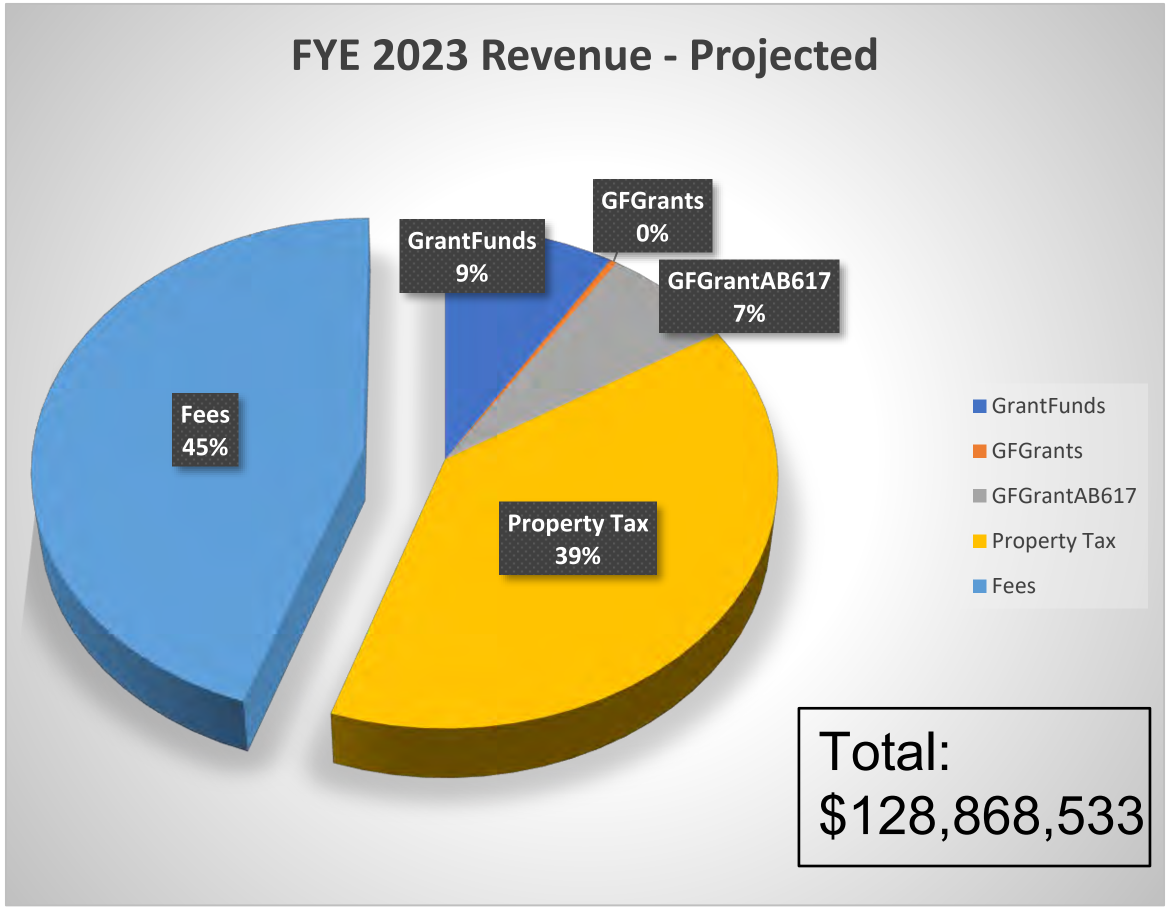
2. ***Impacts*** to the Air District's budget and operations from the regulated community, i.e., ***industrial plant shifts*** (closures, idling, etc.);

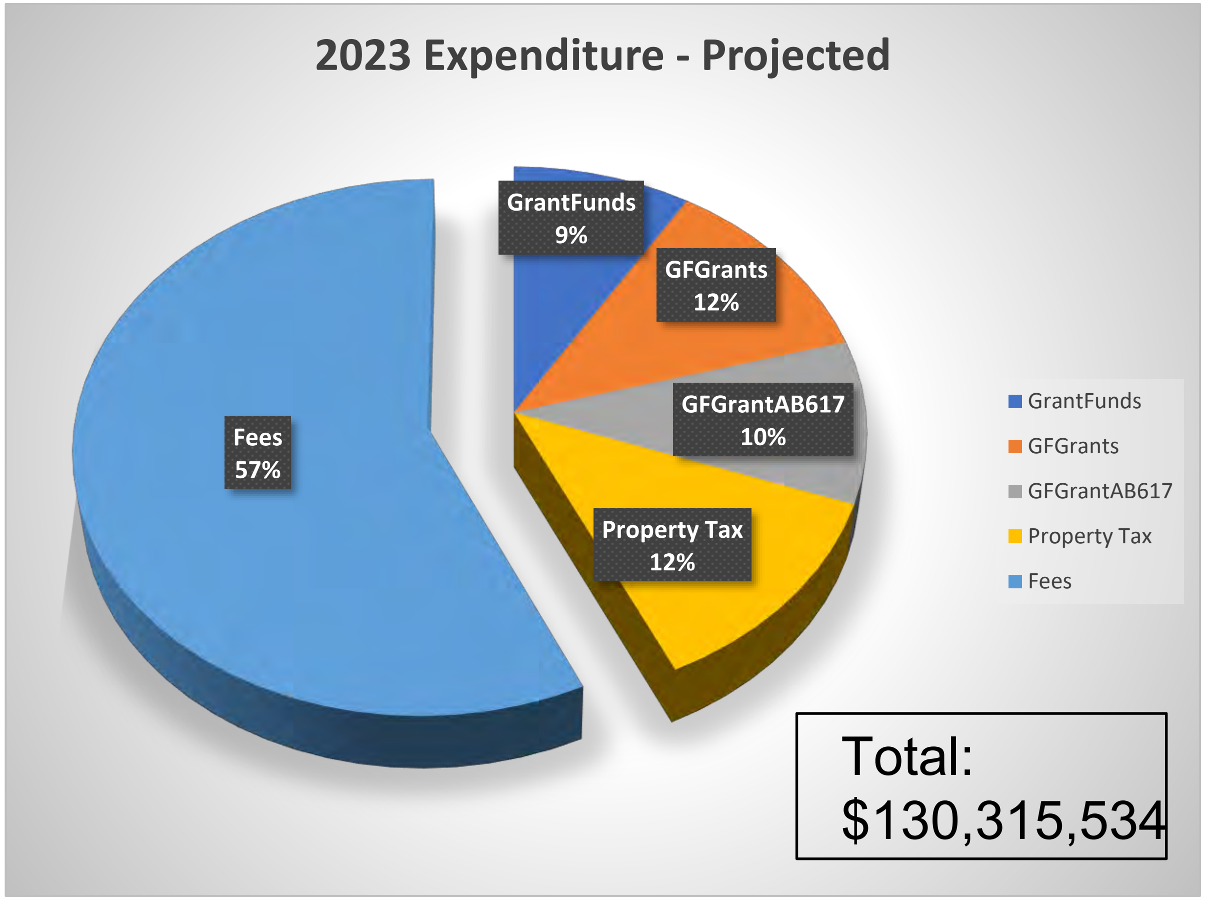
3. ***Fixed spending*** by the Air District – no increases in hiring beyond 20 approved positions, no changes in the programs, no reduction of backlog – for the entire projected period (2022 – 2032), to stay in line with Matrix key assumptions.

For Context: FYE 2023 Budget Overview

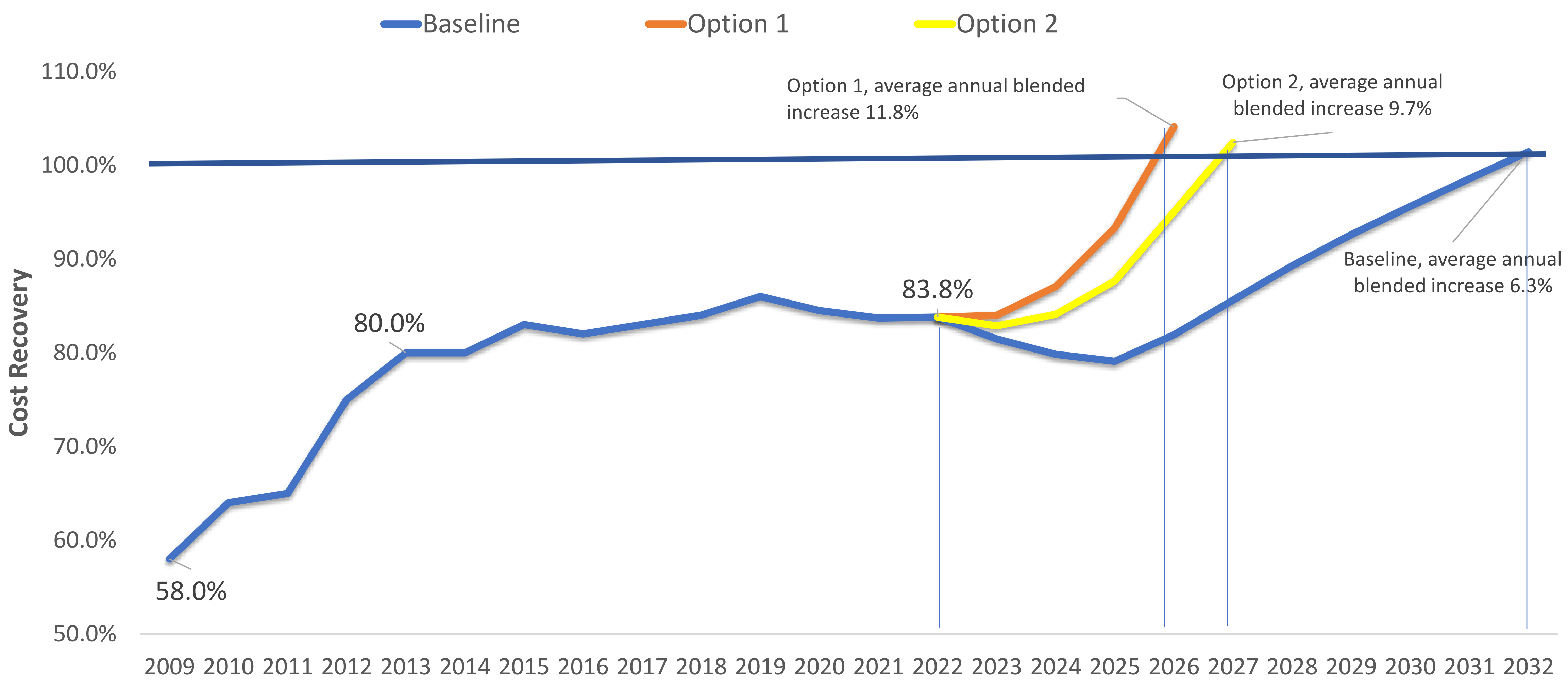
Why focus on full cost recovery? The Air District does not have a budget problem: healthy revenues and reserves. But property tax revenue, which currently subsidizes the shortfall in fee revenue (about $8M) may be used for other priorities.

- ***Stable budget projections also critically assume continuation of the AB617 funding.***





Options to Reach 100% Cost Recovery Model Output



Summary and Conclusions

Goal 1: Reaching 100% Cost Recovery Quickly

Options 1 and 2 may allow the Air District to reach 100% cost recovery relatively quickly (although both assume spending restraint – no new spending before reaching full cost recovery).

Goal 2: Least Disruption

Baseline (status quo) scenario will take longer to achieve full cost recovery. Also critically assumes that the Air District's fee recoverable spending will be lower than fee revenue.

Goal 3: Stable Operation

Focus on maintaining Air District's operations sustainably. Emphasis on very gradual sustainable incremental changes over time while not neglecting fundamental cost recovery issues. Timeline commitment to achieve incremental and sustainable cost recovery, e.g., 90% by 2026.

Goal 4: Air District's Program Integrity

Focus on the Air District's priorities and programs while maintaining and increasing gradually cost recovery over time without strict deadlines. This will require a strategic staffing plan to address needs and deficiencies in line with Board priorities and demands.

Feedback Requested/Prompt

Questions?