



# Other Post Employment Benefits

Finance and Insurance Committee

Item 8-1

July 8, 2013

# OPEB Presentation

- **What is OPEB and what is Metropolitan's unfunded OPEB liability?**
- **What is a Section 115 Trust?**
- **Third Party Providers**
- **Evaluation Criteria**
- **Conclusion**
- **Board Options**
- **Staff Recommendation**

# What is OPEB?

- Other Post Employment Benefits – medical premiums for Metropolitan’s retirees.
- Metropolitan’s unfunded OPEB liability is \$545 million.
- Current biennial budget includes OPEB pre-funding payments of \$5 million and \$10 million for fiscal years 2012 – 2013 and 2013 – 2014.
- Pre-funding payments to a Section 115 Trust can reduce the OPEB liability.

# What is a Section 115 Trust?

- Government sponsored and controlled trust
- Advantages of Section 115 Trust:
  - More predictable costs.
  - Tax exemption for investment earnings.
  - Earnings on assets reduce employer contributions.
  - Investment return assumptions will be higher making the annual required contribution and unfunded liability lower.

# What is a Section 115 Trust? - cont'd

- Advantages of Section 115 Trust continued:
  - Governmental Accounting Standard Board Statement 45 allows for reduction of the OPEB liability for assets held in a Section 115 Trust.
- Disadvantage of Section 115 Trust:
  - Once funds are contributed, they may not be used for other purposes.

# Third Party OPEB Providers

- **California Employer's Retiree Benefit Trust.**
  - CERBT was established on January 1, 2008, and is managed by CalPERS.
  - Service offices are in Sacramento.
  - \$2.5 billion of assets under management.
  - Nonprofit, multi-employer trust.
  - Approximately 345 municipal agencies, including six of Metropolitan's member agencies and the Association of California Water Agencies participate in the CERBT.

# Third Party OPEB Providers

- **Public Agency Retirement Services (PARS).**
  - PARS has been managing OPEB trust funds since 1996.
  - Service offices are in Los Angeles.
  - Utilizes the services of U.S. Bank as trustee and Highmark as investment advisor and manager.
  - Using Highmark, approximately \$500 million of assets under management.
  - For-profit, private entity that manages both multi-employer and single employer trusts for approximately 100 clients.

# Third Party OPEB Providers

- **PFM Asset Management (PFMAM).**
  - PFMAM is the asset management company within the PFM Group and has been managing OPEB trust funds since 2007.
  - Service offices in Los Angeles and San Francisco with investment management staff in Harrisburg, Pennsylvania.
  - \$1.8 billion of assets under management.
  - For-profit entity that provides single employer trusts on behalf of 48 clients.



# Evaluation Criteria

- The three OPEB Trust providers were evaluated based on the following criteria:
  - **Fees.** Investment management, administration and mutual fund fees.
  - **Structure.** Various parties to the agreement(s), such as the trustee and investment manager, as well as the legal structure of the trust (e.g., multi-employer or single-employer).
  - **Investment options.** Spectrum of investment options available to Metropolitan (e.g., customized vs. model portfolios).

# Evaluation Criteria Cont'd

- **Returns/Performance.** Investment performance of the different providers over different periods of time.
- **Start-up costs and effort.** Staff time, legal and other costs necessary to establish or join the trust.
- **Ongoing administration.** Effort required to maintain the trust, ensure that the program functions properly, monitor funding levels and investment performance.

# Evaluation Criteria Cont'd

- **Portability.** Ease in which Metropolitan would be able to move trust assets to another OPEB Trust provider.
- **Fiduciary risk.** Protection provided to Metropolitan. Each of the providers takes on a different level of fiduciary responsibility for managing the trust.

# Conclusion

- CERBT, PARS, and PFMAM have the necessary investment options, experience, and expertise to assist Metropolitan with establishing or joining a Section 115 Trust and to administer and invest the OPEB pre-funding payments.

# Conclusion

- Fees are the main difference among the three providers, with CERBT having the lowest overall fees for administration and investment management.
  - Assuming an initial \$40 million of assets under management, approximate annual costs are:
    - CERBT - \$60,000 (15 basis points)
    - PARS - \$392,000 (98 basis points)
    - PFMAM - \$244,000 (61 basis points)

# Board Options

- **Option 1:**
- Adopt the CEQA determination that the project is not subject to CEQA and authorize the General Manager, with approval of the General Counsel, to execute a contract with CERBT to administer and invest Metropolitan's pre-funding of OPEB benefits.
- **Fiscal Impact:** Reduces unfunded OPEB liability by approximately \$40 million for the current biennial budget. The unfunded OPEB liability will be further reduced if the Board continues to approve these payments and increases the funding over time to begin paying the full ARC.

# Board Options

- **Option 2:**
- Adopt the CEQA determination that the project is not subject to CEQA, direct staff to select PFMAM or PARS for the administration and investment of amounts contributed to pre-funding of OPEB benefits, and authorize the General Manager, with approval of the General Counsel, to execute the necessary contracts with the selected OPEB Trust provider.
- **Fiscal Impact:** Same as Option #1, except the annual fees paid to the provider will be approximately \$180,000 to \$330,000 higher than the cost of CERBT.

# Staff Recommendation

- **Option 1**



# End of Presentation