FALLBROOK PUBLIC UTILITY DISTRICT
MEETING OF THE FISCAL POLICY AND INSURANCE COMMITTEE

AGENDA

THURSDAY, APRIL 4, 2019
8:30 A.M.

FALLBROOK PUBLIC UTILITY DISTRICT
990 E. MISSION RD., FALLBROOK, CA 92028
PHONE: (760) 728-1125

If you have a disability and need an accommodation to participate in the meeting, please call the Secretary at (760) 999-2704 for assistance so the necessary arrangements can be made.

Writings that are public records and are distributed during a public meeting are available for public inspection at the meeting if prepared by the local agency or a member of its legislative body or after the meeting if prepared by some other person.

I. PRELIMINARY FUNCTIONS

CALL TO ORDER / ROLL CALL

PUBLIC COMMENT

II. ACTION / DISCUSSION -- (ITEMS A – D)

A. REVIEW PFM PORTFOLIO INVESTMENT STRATEGY
(Supplemental Materials)

B. PENSION AND OTHER POST EMPLOYMENT BENEFIT OBLIGATION LONG-TERM COST REDUCTION STRATEGY

C. POLICY FOR INTER FUND TRANSFERS

D. ARTICLE 15.1.1 OF ADMINISTRATIVE CODE

III. ADJOURNMENT OF MEETING

* * * * *

DECLARATION OF POSTING

I, Mary Lou West, Secretary of the Board of Directors of the Fallbrook Public Utility District, do hereby declare that I posted a copy of the foregoing agenda in the glass case at the entrance of the District Office located at 990 East Mission Road, Fallbrook, California, at least 72 hours prior to the meeting in accordance with Government Code § 54954.2.

I, Mary Lou West, further declare under penalty of perjury and under the laws of the State of California that the foregoing is true and correct.

April 1, 2019
Dated / Fallbrook, CA

Mary Lou West
Secretary, Board of Directors

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B

MEMO

TO: Fiscal Policy and Insurance Committee
FROM: Jack Bebee, General Manager, JRB
David Shank, Acting General Manager/CFO DS
DATE: April 4, 2019
SUBJECT: Pension and Other Post Employment Benefit Obligation Long-Term Cost Reduction Strategy

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Purpose

To update the District's strategy for offsetting costs associated with existing pension and other post-employment benefit (OPEB) obligations to help manage long-term cost of these benefits and the associated impacts on rates.

Summary

The District carries long-term obligations due to their existing pension and OPEB benefits. The OPEB benefit is associated with the retiree healthcare program. The District pension program is administered through the Public Employee Retirement System (PERS). PERS requires annual payments from the District to fund its pension obligation to employees. The PERS annual payment is made up of two parts 1) the cost of pension benefits earned by the active employees called the Annual Required Contribution (ARC); 2) a payment for benefits already earned but not fully funded by the District called the Unfunded Accrued Liability (UAL). In the past, PERS over-estimated expected returns on investments and didn't collect sufficient payment from participants for the benefits earned. This created a significant unfunded liability for participants. Due to pension reform and new pension reporting requirements, the District is making annual payments to fully fund its UAL in 30-years. The State also recognized the need to help reduce long-term pension costs and passed the Public Employee Pension Reform Act (PEPRA) in 2013. PEPRA reduced benefits for new employees that were not previously in PERS. 40% of District employees are now in PEPRA.

Due to concerns over the impact of these obligations on the District's expenses and fiscal sustainability, the District's Board of Directors has taken a progressive approach to evaluate alternatives to reduce these costs. The District evaluated the following options:

1. Transition out of PERS into a defined benefit program
2. Pay down the existing pension obligations to PERS
3. Set aside money in a trust to help off-set pension costs

In order to transition out of the PERS program, the District would have to fund all accrued current and future pension costs ($46 million as of 6/30/17) and create or pay for a pension administrator to manage the investments and payments to retirees vested in PERS. This was determined to not be financially viable at this time. The District determined that setting aside funds to help off-set the pension and OPEB obligations was the best path forward. Instead of just putting these funds into PERS, who has underperformed on returns in the past, the funds would be place into a third party trust held for the District's pension and OPEB costs. The District selected the Public Agency Retirement Services (PARS) to administer the trust. By utilizing PARS, the District can invest funds to achieve a higher rate of return to help off-set pension and OPEB costs. The District also elected to set-aside some funds from the sale of the Santa Margarita property to help off-set the pension obligations.

A summary of the District's current UAL and OPEB and funds held to off-set these obligations is shown in Table 1:

Table 1 – Summary of Districts UAL and OPEB Liability and Offset Funds

Obligation	Pension (UAL component)	OPEB
Liability*	$12,649,005	$1,039,721
Funds Held**	$5,150,144	$935,700

*As of 6/30/17 – date of last PERS and OPEB valuation
**As of 12/31/18 – Includes funds held by PARS ($1.4M) and set aside in Pension Obligation Off-set Fund ($3.8M).

As shown in Table 1, the District is almost fully funded for OPEB obligations, but has a smaller percentage of funds set aside for pension obligations. The funds held for pension costs can be used to help off-set UAL costs or other pension costs. The UAL is driving an increase in annual pension costs for the District. The annual payment schedule to PERS is included in Attachment A. As shown on Attachment A, there is an option for a 30-year, 15-year, and 10-year schedule to pay down the UAL. The District has been paying down the UAL on a 30-year schedule.

The District has also been contributing an additional amount into PARS to help off-set future obligations. A payment of $500,000 into PARS for pension obligations and $150,000 in PARS for OPEB is scheduled this Fiscal Year. A long-term additional pension payment of $650,000 annually was included in the rate setting process.

<u>Pension and OPEB Alternatives</u>

A number of long-term strategies are available to help reduce long-term pension costs for the District. There are two ends of the spectrum on approaches to help stabilize long-term pension costs. At one end the District could reduce the amortization schedule and make larger payments to PERS and utilize funds from PARS to fund PERS. At the other end the District could make minimum payments to PERS and maximize payments and returns in PARS to diversify holding to off-set future payments.

Based on evaluation of numerous options with the FP&I Committee, it was determined that an approach to limit funds held by PERS and maintain control of funds under PARS was the preferred approach and utilize returns from PARS to help off-set long-term costs.

The District would continue on the 30-year schedule for PERS, which reduces the annual PERS payment and continue funding PARS and growing returns in PARS. Once the PARS account and Market Value of PERS assets covered 90% of the pension obligation, the PARS returns would then be used to off-set the annual pension costs. This approach leverages the PARS investment returns to hold down long-term pension costs; and over time, the returns could largely fund the pension obligation. This also keeps the money under the District control in PARS versus having it under control of the state in PERS. Since the District is already over 90% funded for PARS for OPEB, the District would fund the $650,000 budgeted for this year into PARS for pension obligations and the District would continue to fund PARS at $500,000 annually for the next six years and then would let returns grow until the pension obligation is 90% funded. Once this target is met, returns would be used to offset costs while maintaining a 90% funded target. Table 2 shows an example of what the payments would look like based on assumptions for future cost escalation and market returns.

Year	Total Annual Required PERS Payment[1]	PERS UAL Balance	Payment to PARS	PARS Balance[2]	% Funded[3]	Payment From PARS to PERS	Total Annual District Pension Payment
2019	$ 1,465,254	$ 12,668,951	$ 650,000	$ 5,150,144	76%	$ -	$ 2,115,254
2020	$ 1,590,270	$ 12,678,676	$ 500,000	$ 6,073,901	78%	$ -	$ 2,090,270
2021	$ 1,728,495	$ 12,590,766	$ 500,000	$ 6,890,096	80%	$ -	$ 2,228,495
2022	$ 1,786,143	$ 12,400,892	$ 500,000	$ 7,747,101	81%	$ -	$ 2,286,143
2023	$ 1,818,562	$ 12,142,793	$ 500,000	$ 8,646,956	83%	$ -	$ 2,318,562
2024	$ 1,853,695	$ 11,835,097	$ 500,000	$ 9,591,804	85%	$ -	$ 2,353,695
2025	$ 1,889,299	$ 11,470,938	$ 500,000	$ 10,583,894	86%	$ -	$ 2,389,299
2026	$ 1,925,376	$ 11,045,238	$ -	$ 11,625,589	88%	$ -	$ 1,925,376
2027	$ 1,961,918	$ 10,552,526	$ -	$ 12,206,868	89%	$ -	$ 1,961,918
2028	**$ 1,998,921**	**$ 9,986,906**	**$ -**	**$ 12,817,212**	**90%**	**$ 750,000**	**$ 1,248,921**
2029	$ 2,036,381	$ 9,342,020	$ -	$ 12,708,072	90%	$ 700,000	$ 1,336,381

1. Includes ARC and UAL. Assumes 3% annual payroll escalation and PERS Projections from 8/2017 Valuation Report

2. Based on 5% rate of return

3. % Total PERS+PARS ASSETTS to PERS Liability. Assume 4% Growth in Liability and 5% in Assetts

Table 2 – Projected Pension Payments and Utilization of PARS

The same approach would be utilized for the District's OPEB Liability. The District is currently over 90% funded for OPEB, so in the next budget year the District would make a payment from PARS to pay District OPEB costs. An example of a schedule for future OPEB payments is shown in Table 3.

Year	Total Annual Required OPEB Payment[1]	OPEB Liability[2]	Payment to PARS for OPEB	PARS Balance[2]	% Funded PARS to OPEB Liability	Payment From PARS for OPEB	Total Annual District Pension Payment
2019	$ 40,000	$ 1,039,721	$ -	$ 935,700	90%	$ -	$ 40,000
2020	$ 41,200	$ 1,070,913	$ -	$ 982,485	92%	$ 41,200	$ -
2021	$ 42,436	$ 1,103,040	$ -	$ 990,409	90%	$ 20,000	$ 22,436
2022	$ 43,709	$ 1,136,131	$ -	$ 1,019,930	90%	$ 20,000	$ 23,709
2023	$ 45,020	$ 1,170,215	$ -	$ 1,050,926	90%	$ 18,391	$ 26,629
2024	$ 46,371	$ 1,205,322	$ -	$ 1,085,081	90%	$ 18,989	$ 27,382
2025	$ 47,762	$ 1,241,481	$ -	$ 1,120,346	90%	$ 19,606	$ 28,156
2026	$ 49,195	$ 1,278,726	$ -	$ 1,156,758	90%	$ 23,135	$ 26,060
2027	$ 50,671	$ 1,317,087	$ -	$ 1,191,460	90%	$ 23,829	$ 26,842
2028	$ 52,191	$ 1,356,600	$ -	$ 1,227,204	90%	$ 24,544	$ 27,647
2029	$ 53,757	$ 1,397,298	$ -	$ 1,264,020	90%	$ 25,280	$ 28,476
1. District share of retiree health. Assumes 3% annual escalation							
2. From FY 2018 Audit. Assumes 3% annual escalation							
2. Based on 5% rate of return							

Table 3 – Projected OPEB Payments and Utilization of PARS

Recommended Action

Staff recommends using an approach to fund PARS and maintain a 90% funded status for both OPEB and Pension Obligations. Payments from PARS returns would be used once the fund has met the 90% funded target. The District has developed the attached policy (Attachment B) that memorialize the OPEB and Pension funding strategies.

Attachment A

Year	Total Annual Required PERS Payment[1]	PERS UAL Balance	Payment to PARS	PARS Balance[2]	% Funded[3]	Payment From PARS to PERS	Total Annual District Pension Payment
2019	$ 1,465,254	$ 12,668,951	$ 650,000	$ 5,150,144	76%	$ -	$ 2,115,254
2020	$ 1,590,270	$ 12,678,676	$ 500,000	$ 6,073,901	79%	$ -	$ 2,090,270
2021	$ 1,728,495	$ 12,590,766	$ 500,000	$ 6,890,096	81%	$ -	$ 2,228,495
2022	$ 1,786,143	$ 12,400,892	$ 500,000	$ 7,747,101	84%	$ -	$ 2,286,143
2023	$ 1,818,562	$ 12,142,793	$ 500,000	$ 8,646,956	86%	$ -	$ 2,318,562
2024	$ 1,853,695	$ 11,835,097	$ 500,000	$ 9,591,804	89%	$ 492,090	$ 1,861,604
2025	**$ 1,889,299**	**$ 11,470,938**	**$ 500,000**	**$ 10,091,804**	91%	**$ 517,090**	**$ 1,872,209**
2026	$ 1,925,376	$ 11,045,238	$ -	$ 10,591,804	93%	$ 529,590	$ 1,395,786
2027	$ 1,961,918	$ 10,552,526	$ -	$ 10,591,804	93%	$ 529,590	$ 1,432,327
2028	$ 1,998,921	$ 9,986,906	$ -	$ 10,591,804	94%	$ 529,590	$ 1,469,330
2029	$ 2,036,381	$ 9,342,020	$ -	$ 10,591,804	95%	$ 529,590	$ 1,506,791

1. Includes ARC and UAL. Assumes 3% annual payroll escalation and PERS Projections from 8/2017 Valuation Report

2. Based on 5% rate of return

3. % Total PERS+PARS ASSETS to PERS Liability. Assume 3% Growth in Liability and 5% in Assets

Year	Total Annual Required OPEB Payment[1]	OPEB Liability[2]	Payment to PARS for OPEB	PARS Balance[2]	% Funded PARS to OPEB Liability	Payment From PARS for OPEB	Total Annual District Pension Payment
2019	$ 40,000	$ 1,039,721	$ -	$ 935,700	90%	$ -	$ 40,000
2020	$ 41,200	$ 1,070,913	$ -	$ 982,485	92%	$ 41,200	$ -
2021	$ 42,436	$ 1,103,040	$ -	$ 990,409	90%	$ 42,436	$ -
2022	$ 43,709	$ 1,136,131	$ -	$ 997,494	88%	$ 43,709	$ -
2023	$ 45,020	$ 1,170,215	$ -	$ 1,003,659	86%	$ 17,564	$ 27,456
2024	$ 46,371	$ 1,205,322	$ -	$ 1,036,278	86%	$ 18,135	$ 28,236
2025	$ 47,762	$ 1,241,481	$ -	$ 1,069,957	86%	$ 18,724	$ 29,038
2026	$ 49,195	$ 1,278,726	$ -	$ 1,104,731	86%	$ 19,333	$ 29,862
2027	$ 50,671	$ 1,317,087	$ -	$ 1,140,635	87%	$ 19,961	$ 30,710
2028	$ 52,191	$ 1,356,600	$ -	$ 1,177,705	87%	$ 20,610	$ 31,581
2029	$ 53,757	$ 1,397,298	$ -	$ 1,215,981	87%	$ 21,280	$ 32,477

1. District share of retiree health. Assumes 3% annual escalation

2. From FY 2018 Audit. Assumes 3% annual escalation

2. Based on 5% rate of return

Attachment B

<table>
<tr><td rowspan="4">FALLBROOK PUBLIC
UTILITY DISTRICT</td><td colspan="2">Standard Policy</td></tr>
<tr><td>Drafted by:</td><td>CFO/General Manager</td></tr>
<tr><td>Original Date:</td><td></td></tr>
<tr><td>Revision Date:</td><td></td></tr>
<tr><td rowspan="2">Management of the District's Other Post-Employment Benefits and Pension Trusts</td><td>Review by department:</td><td>1_____ 2_____ 3_____
4_____ 5_____ 6_____</td></tr>
<tr><td>Approved by:</td><td>General Manager</td></tr>
</table>

Purpose:

Establish the following guidelines related to the management of the District's Other Post-Employment Benefits (OPEB) Trust:

- *Set a funding target level for the District's OPEB liability as determined by actuarial reports.*
- *Establish guidelines for how the PARS OPEB Trust can be used to pay for District OPEB expenses.*

Establish the following guidelines related to the management of the District's Pension Trust:

- *Set a minimum funding target level for the District's pension liability as determined by actuarial reports.*
- *Establish guidelines for how the PARS Pension Trust can be used to pay for District pension expenses.*

Personnel:

Accounting and Supervisors

Policy:

General Policy

OPEB Trust:

The District has set a target OPEB funding level of 90%. The funding level is determined by dividing the assets held in the District's 115 OPEB Trust by the District's gross OPEB liability as determined by an actuary. If at the end of the fiscal year, the Districts funding level is below 90%, a deposit may be made by the District in the following fiscal year. If at the end of the fiscal year the funding level is over 90%, the funding level will be brought to the 90% level by budgeting a withdrawal from the OPEB Trust to fund retiree healthcare expenses in the following fiscal year.

Pension Trust:

The District has set a target pension funding level of 90%. The pension funding level is determined by dividing the assets held in the District's 115 Pension Trust and the District's assets held by CalPERS by the District's gross pension liability as determined by an actuary. If at the end of the fiscal year the Districts funding level is below 90%, a deposit may be made by the District in the following fiscal year. If at the end of the fiscal year the funding level is over 90%, the funding level will be brought to the 90% level by budgeting a withdrawal from the Pension Trust to fund permitted pension expenses in the following fiscal year.

Definitions

***CalPERS**: CalPERS is the California Public Employees" Retirement System. The District has contracted CalPERS to administer its defined benefit retirement plan.*

***OPEB Trust**: The 115 Trust established by the District with PARS to fund the District's OPEB liability.*

***Pension Trust**: The 115 Trust established by the District with PARS to help the District's fund and manage its CalPERS pension liability.*

***District's Retiree Healthcare Cost**: The District's share of a retirees' healthcare costs. This is limited to the payment of 50% of the retiree's healthcare costs and excludes any spouse or dependent healthcare costs.*

C

MEMO

TO: Fiscal Policy & Insurance Committee
FROM: David Shank, Assistant General Manager/CFO DS
DATE: April 4, 2019
SUBJECT: Policy for Inter Fund Transfers

Purpose

Discuss the draft policy governing the transfer or funds from one enterprise to another.

Summary

Cost of service principles require that each enterprise (i.e., Water) be managed separately and that rates and charges recover only the costs of that enterprise. Transferring funds from one enterprise to another for any reason other than for cost of service would violate this construct. Therefore, the District's policy is to not allow these kinds of transfers to occur unless they are structured like an inter fund loan. Under these conditions the Board would approve the loan amount and repayment terms.

Recommended Action

That the Committee review the attached (Attachment A) Inter Fund Transfer Policy.

Attachment A

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<tr><td rowspan="2">Inter Fund Transfer Policy</td><td>Review by department:</td><td>1________ 2________ 3________
4________ 5________ 6________</td></tr>
<tr><td>Approved by:</td><td>General Manager</td></tr>
</table>

Purpose:

Establish the restriction on the transfer of funds from one enterprise to another.

- *Ensures that cost of service principles are met by eliminating any cross subsidization of costs by another Enterprise.*

Personnel:

Accounting and Supervisors

Policy:

General Policy

The goal of this policy is to conform to cost of service principles and restrict the fund transfers from one enterprise to another for non-cost of service reasons. No transfers of funds across enterprises shall be made in accordance with Article 15 of the District's Administrative Code. With Board approval a loan from one enterprise to another will be permitted provided a repayment schedule is developed and adhered to. The terms of the loan will be determined at the time the loan is made.

Definitions

Enterprise: *This refers to the District's distinct services and includes Water, Recycled Water and Wastewater.*

Cost of Service Transfers: *Cost of service transfers are related to expenses incurred by one Enterprise but are shared by another Enterprise. For example debt service on the reclamation plant is paid out of the Wastewater Fund but the Recycled Water Fund pays a portion of the debt service.*

Inter Fund Transfer: *This refers to the transfer from one Enterprise to another Enterprise. For example a transfer of funds from Water to Wastewater.*

DRAFT

D

MEMO

TO: Fiscal Policy & Insurance Committee
FROM: Jack Bebee, General Manager, JRB
DATE: April 4, 2019
SUBJECT: Article 15.1.1 of Administrative Code

Purpose

Discuss the revised language to Article 15.1.1 of the Administrative Code regarding the Annual Budget Resolution.

Summary

At the February Regular Board Meeting, the Board approved revised language to the Administrative Code relative to the annual budget resolution process and annual allocation of an annual Liquidity Fund level. After the meeting, there was some further concerns expressed about the lack of clear language relative to the prohibition of use of any funds established as long-term investments without Board approval. While the language does identify language relative to use of reserves, it does not specifically state a Board action for use of long-term investments. The current language is attached as Attachment A, with a proposed addition to add language that states:

"Any withdrawal of funds from long-term investments shall require prior board approval." Since the overall updates to this Section were also developed and approved during the meeting, an additional review of the language should be done by the Committee.

The section also discusses the establishment of a liquidity fund level annually. Staff developed a District policy (Attachment B) to describe the basis for establishing the amount of funds to hold in this fund.

Recommended Action

That the Committee review the language in Section 15.1.1 of the Administrative Code and approve the addition of the language relative to use of long-term investments.

Attachment A

Article 15. Budget and Fund Management

Sec. 15.1 District's Annual Budget.

Preparation of the District Budget is directed by the Assistant General Manager/CFO. Working with the Fiscal Policy and Insurance Committee the General Managers develops annual financial goals and objectives for the budget in February. A first preliminary Budget is presented to the Board of Directors and public in May and a second preliminary Budget in June. The final Budget is presented in July for adoption, along with a resolution adopting a tax rate for Bonded Indebtedness.

The budgeting process is intended to create a transparent process that enables the Board of Directors to estimate the Districts revenues and expenses including employee compensation arising from negotiations and changes in other costs of operations.

15.1.1 Annual Budget Resolution.

The Board shall approve an annual budget resolution that establishes the total appropriation for the fiscal year based on the following budget categories:

1. Administration, operations, and maintenance
2. Water purchases and contingencies
3. Capital improvements and equipment
4. Revenue Bonds, State Revolving Fund, interest, and principal
5. Established annual Liquidity Fund level

In addition, the budget resolution shall identify any anticipated net withdrawal of District reserves for the Fiscal Year. Any unanticipated net withdrawal of District reserves shall be a separate board action. Any withdrawal of funds from long-term investments shall require prior Board approval.

Any spending above the established appropriations or additional withdrawal of reserves shall require Board approval. As part of the annual budget process, the Board will review and approve the District's liquidity fund level.

Sec. 15.2 Treasurer's Fund.

The Treasurer's Fund is established primarily to account for all District cash and investments and also to record detailed accounting for fringe benefits. Revenues are obtained from a budgeted mark-up on District labor. Revenue and Expense accounts in this fund are closed to the Utility fund annually.

Sec. 15.3 General Fund.

The General Fund shall consist of accounts for property tax revenues and appropriations to other funds as determined by the Board.

Sec. 15.4 Utility Funds.

The Utility Funds consists of three separate funds reflecting the operating departments of Water, Wastewater and Recycled Water. The funds reflect the revenues from water sales, monthly service charges and other recurring fees and all expenses, including Operating and Maintenance (O&M) and General & Administrative (G&A).

Attachment B

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<tr><td>Revision Date:</td><td></td></tr>
<tr><td rowspan="2">Management of the District's Liquidity Fund Balance</td><td>Review by department:</td><td>1_____ 2_____ 3_____
4_____ 5_____ 6_____</td></tr>
<tr><td>Approved by:</td><td>General Manager</td></tr>
</table>

Purpose:

Establish the following guidelines related to the management and utilization of the District's Liquidity Fund:

- *Annually reset the balance of the fund to a level calculated using the sum of the following amounts:*
    1. *The amount equivalent of one month of operating expenses.*
    2. *The net capital funding requirement for the fiscal year.*
- *Require Board approval for the transfer of any additional funds to the Liquidity Fund.*

Personnel:

Accounting and Supervisors

Policy:

General Policy

To enable the District to maximize the yield of its investment portfolio, the District has separated its long-term investments from its short-term investments. The short-term investments are maintained to provide working capital/Liquidity to the District. In accordance with Article 15 of the Administrative Code, each fiscal year the beginning balance of the Liquidity Fund shall be set equal to the sum of 1) one month of operating expenses and 2) the projected net capital funding needs. One month of operating expenses shall be determined by taking the budgeted operating expenses including the cost of water and dividing by 12. The net capital funding requirement for the fiscal year will be calculated by subtracting projected capital restricted revenues (i.e. Capital Improvement Charges) from the budgeted capital expenditures. The sum of these two amounts equals the Liquidity Fund fiscal year beginning balance.

Definitions

***Liquidity Fund**: The funds held in the District's Liquidity Account in the CAMP investment pool.*

***Net Capital Funding Need**: The net capital funding need is the difference between the annual budgeted capital expenditures and the projected capital restricted revenues. Capital restricted revenues include property tax, water standby availability charges, and Capital Improvements Charges.*