



**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT (METRO)  
FINANCE, BUDGET AND AUDIT STANDING COMMITTEE MEETING  
MINUTES  
NOVEMBER 8, 2019 – 8:00AM  
METRO ADMIN OFFICES  
110 VERNON STREET  
SANTA CRUZ, CA 95060**

A regular meeting of the Finance, Budget and Audit Standing Committee of the Santa Cruz Metropolitan Transit District (METRO) was convened on Friday, November 8, 2019 at the METRO Admin Offices, 110 Vernon Street, Santa Cruz, CA.

The Committee Meeting Agenda Packet can be found online at [www.SCMTD.com](http://www.SCMTD.com) and is available for inspection at Santa Cruz METRO's Administrative offices at 110 Vernon Street, Santa Cruz, California. \*Minutes are "summary" minutes, not verbatim minutes. Audio recordings of Board meeting open sessions are available to the public upon request.

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- 1 **CALL TO ORDER** at 8:05 AM by Board Vice Chair Rotkin.
- 2 **ROLL CALL:** The following Directors were **present**, representing a quorum:

**Director Trina Coffman-Gomez**  
**Director Donna Lind**  
**Director Donna Meyers**  
**Vice Chair Mike Rotkin**

**City of Watsonville** AR 9:10AM  
**City of Scotts Valley**  
**City of Santa Cruz**  
**County of Santa Cruz**

Alex Clifford  
Julie Sherman  
Angela Aitken

METRO CEO/General Manager  
METRO General Counsel  
METRO CFO

METRO EMPLOYEES AND MEMBERS OF THE PUBLIC WHO VOLUNTARILY INDICATED THEY WERE PRESENT (IN ALPHABETICAL ORDER) WERE:

Angela Aitken, SCMTD

Kristina Mihaylova, SCMTD

- 3 **ADDITIONS OR DELETIONS FROM AGENDA/ADDITIONAL DOCUMENTATION TO SUPPORT EXISTING AGENDA ITEMS – Distributed at the Meeting**  
Updated Agenda Item 6.1, FY19 Preliminary Schedule of Reserve Account Balances  
Updated Agenda Item 7, Consideration of Changes to the Reserve Fund Policy  
Updated Agenda Item 8, UAL and OPEB presentation on Recommendations to Reduce Unfunded Liabilities
- 4 **ORAL AND WRITTEN COMMUNICATIONS TO THE FINANCE, BUDGET AND AUDIT STANDING COMMITTEE**  
None.

**5 MONTHLY FINANCIAL UPDATE**

Angela Aitken, Chief Financial Officer, provided commentary to the presentation, adding that the numbers presented at the board meeting next Friday, 11/15/19, would be slightly different due to a more accurate representation of fuel expenses as a result of closing the month of September.

Director Lind asked if METRO knows why Highway 17 ridership hasn't improved. CEO Clifford provided a variety of reasons. Barrow Emerson, Planning and Development Director, added that transportation costs are becoming a smaller percentage of a family's overall budget; and, that a number of details are provided in the Board ridership quarterly report. The Directors offered to share any information with their respective agencies to support METRO in increasing ridership. Jayme Ackemann, Marketing, Communications and Customer Service Director, spoke briefly of the marketing efforts METRO will be undertaking.

There was no public comment.

**6 FY19 PRELIMINARY SCHEDULE OF RESERVE ACCOUNT BALANCES**

Angela Aitken, Chief Financial Officer, spoke briefly about the FY19 preliminary schedule.

There was no public comment.

**7 CONSIDERATION OF REVISIONS TO THE RESERVE FUND POLICY**

Angela Aitken, CFO, spoke to the staff report, bringing the assembly's attention to the changes delineated in the redline version of the policy. Directors present recommended that the operations sustainability reserve board-approved balance be increased from two months to three months.

There was no public comment.

**ACTION: MOTION TO RECOMMEND APPROVAL OF THE REVISIONS TO THE RESERVE FUND POLICY AS PRESENTED AND AN INCREASE IN THE OPERATIONS SUSTAINABILITY RESERVE FUND FROM TWO MONTHS TO THREE MONTHS**

**MOTION: DIRECTOR MEYERS**

**SECOND: DIRECTOR LIND**

**MOTION PASSED UNANIMOUSLY (Directors Lind, Meyers & Rotkin)**

**8 UAL AND OPEB PRESENTATION ON RECOMMENDATIONS TO REDUCE UNFUNDED LIABILITIES**

Angela Aitken, CFO, spoke to the presentation and elaborated on the cause, risks, etc. of the two types of liabilities with attending Directors contributed suggestions and experiences.

In response to Vice Chair Rotkin's question, CFO Aitken assured the assembly that staff would return with the estimated actuarial costs and timeline at the next board meeting.

There was no public comment.

**ACTION: MOTION TO RECOMMEND APPROVAL OF THE RECOMMENDATIONS TO ESTABLISH IN CONCEPT AN IRREVOCABLE SECTION 115 TRUST FOR PENSION (UAL) AND RETIREE MEDICAL (OPEB), BUT TO FIRST CONTRACT WITH AN ACTUARIAL TO RUN VARIOUS FINANCIAL SCENARIOS TO HELP REDUCE PENSION AND RETIREE**

**MEDICAL LIABILITIES BY IDENTIFYING VARIOUS CONCEPTS FOR THE BOARD TO CONSIDER**

**MOTION: DIRECTOR MEYERS**

**SECOND: DIRECTOR LIND**

**MOTION PASSED UNANIMOUSLY (Directors Lind, Meyers & Rotkin)**

*Director Coffman-Gomez arrived at 9:10AM*

**9 APPROVAL OF NEW CAPITAL PROJECTS AND UPDATED 10[YEAR UNFUNDED CAPITAL NEEDS LIST**

Barrow Emerson, Planning and Development Director, spoke to the staff report and elaborated on the continued pursuit of funding sources to replace our aging fleet. CEO Clifford provided an update on electric, CNG and hydrogen fueled options.

Referencing Table 1 in the staff report, CEO Clifford noted that the strategy has changed to focus METRO's funding efforts on fewer, larger opportunities.

There was no public comment.

**ACTION: MOTION TO RECOMMEND APPROVAL OF THE NEW CAPITAL PROJECTS AND UPDATED 10 YEAR UNFUNDED CAPITAL NEEDS LIST AS PRESENTED**

**MOTION: DIRECTOR MEYERS**

**SECOND: DIRECTOR**

**MOTION PASSED UNANIMOUSLY (Directors Coffman-Gomez, Lind, Meyers & Rotkin)**

**10 ADJOURNMENT**

Board Vice Chair Rotkin adjourned the meeting at 9:25 AM.

Pursuant to Section 54954.2(a)(1) of the Government Code of the State of California, this agenda was posted at least 72 hours in advance of the scheduled meeting at a public place freely accessible to the public 24 hours a day. The agenda packet and materials related to an item on this Agenda submitted after distribution of the agenda packet are available for public inspection in the Santa Cruz METRO Administrative Office (110 Vernon Street, Santa Cruz) during normal business hours. Such documents are also available on the Santa Cruz METRO website at [www.scmtd.com](http://www.scmtd.com) subject to staff's ability to post the document before the meeting.

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**DATE:** November 8, 2019  
**TO:** Finance, Budget & Audit Committee  
**FROM:** Angela Aitken, CFO  
**SUBJECT: CONSIDERATION OF CHANGES TO THE RESERVE FUND POLICY**

**I. RECOMMENDED ACTION**

**That the Finance, Budget and Audit Standing Committee consider and recommend changes to the Board of Directors the proposed changes to the Reserve Fund Policy**

**II. SUMMARY**

- At the January 23, 2015 Board of Directors (Board) meeting, the Board gave staff direction to create a formal policy on Reserve Funds that would ensure strong fiscal management.
- Santa Cruz Metropolitan Transit District (METRO) has created an Administrative Code to codify policies enacted by the Board.
- At the October 23, 2015 Board meeting, the Board adopted the current Reserve Fund Policy within the Administrative Code.
- Staff recommends that the Board adopt the proposed clarifying changes to the Reserve Fund Policy within the Administrative Code, so that it reflects the current responsibilities and practices of the Finance Department in relation to the use and replenishment of the Reserve Funds.
- Staff recommends that the Board change the Operations Sustainability Reserve Fund target minimum balance from two (2) months to three (3) months.

**III. DISCUSSION/BACKGROUND**

During FY15, the METRO Board was presented with, and discussed, the impending “Fiscal Cliff” and Structural Deficit via numerous workshop presentations to the Board. At the November 14, 2014 meeting, the Board received recommendations on how each reserve “bucket” should be established and funded. CEO, Alex Clifford, and CFO, Angela Aitken, talked through the various reserve “buckets”, how they were each used, guidelines that were in place to follow, the funding status and deficit status of each “bucket”, industry policy or guidelines, and then presented a recommendation on how and to what level each reserve “bucket” should be funded.

The Board came to a consensus on these Reserve Funds and was presented with the individual fund agreements via a presentation to the Board at the January 23,

2015 meeting. Direction was also given during the November 14, 2014 meeting to create a formal Reserve Funds Policy, with an objective to establish sound formal, fiscal reserve guidelines that will ensure strong fiscal management, guide future agency decisions, maintain the fiscal stability of the organization, and place the agency in a position to better respond to unanticipated fiscal challenges and risk.

The purpose of the Reserve Fund Policy for METRO is to ensure the long-term economic stability of the agency. A key element of prudent financial planning is to ensure there are sufficient reserves to cover current operating and capital cash flows. Additionally, good fiscal responsibility requires anticipating the likelihood of, and preparing for, unforeseen disruptions in cash flow. METRO will, at all times, strive to have sufficient funding available to meet its operating and capital obligations.

Based on an analysis of “best practices” and quantitative standards, this policy strives to maintain a stable and positive financial position for the foreseeable future. Moreover, it provides guidelines to staff in planning and directing the day-to-day financial affairs and in developing recommendations to the Board.

Properly designed guidelines send a positive signal to the community, our customers, our stakeholders, rating agencies, and regulatory agencies that METRO’s Board is committed to the agency’s long-term financial health, stability and viability.

This policy has helped provide the agency with unrestricted funds with which to stabilize the agency’s finances and position it to better absorb economic downturns, unforeseen disruptions in cash flow, meet generally accepted financial practices, and fund the local match for state and federal capital grants.

The goal of this policy is to establish adequate reserve funds through sound fiscal reserve guiding principles that will guide agency staff when making financial recommendations to the Board. If the agency chooses to borrow funds in the future, a fiscally sound Reserve Fund Policy will contribute to a positive credit rating. A better credit rating results in a lower cost of borrowing.

Reporting of Fund Balances (defined as the excess of assets over liabilities) is guided by complying with Governmental Accounting Standards Board (GASB) Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions. GASB 54 defines five separate components of fund balance, each of which identifies the extent to which METRO is bound to honor constraints on the specific purposes for which amounts can be spent:

- a. **Nonspendable** fund balance (not in spendable form, such as inventories, prepaids, long-term receivables, or non-financial assets held for resale).



- b. **Restricted** fund balance (extremely enforceable limitations on use, such as debt covenants, grantors, contributors, or laws and regulations of other governments).
- c. **Committed** fund balance (constrained to specific purposes by a formal action of the Board, such as an ordinance, resolution, or policy).
- d. **Assigned** fund balance (limited to the Board's intent to be used for a specific purpose, but not Restricted or Committed).
- e. **Unassigned** fund balance (residual net resources, either positive or negative, in excess of the other four fund balance components). Unassigned amounts are available for any purpose with Board approval.

All of METRO's reserve funds are classified as committed fund balances and will be funded with surplus or "carryover" of unrestricted operating funds.

Adequate reserve funds are built over time. The goal of maintaining adequate reserves is to ensure that there are appropriate levels of working capital in the reserve funds for unanticipated situations such as a sudden increase in expenses, significant one-time unbudgeted expenses, unanticipated loss in funding, economic downturns, or uninsured losses, and to ensure continuity of service.

Reserve funds may also be used for one-time, nonrecurring expenses that will build long-term capacity, such as payment of grant funded expenses prior to being reimbursed by the awarding grant entity, matching dollars for grants, capital and operating expenditures that might not otherwise have a grant funding source or qualify for grant funding.

METRO's reserve funds are as follows currently:

- **Operations Sustainability Reserve Fund**
  - a. Classified as a committed fund balance
  - b. Sometimes referred to as the "rainy day fund"
  - c. Target minimum is equal to two months of average operating expenses for the most current fiscal year's budget
  - d. The target minimum is \$7.5M
  - e. Should not be used for recurring expenses

- **Cash Flow Reserve Fund**
  - a. Classified as a committed fund balance
  - b. Target minimum amount will be set annually through the budget process, and is calculated annually based on a review of all current reimbursable grants, a revenue flow analysis, and invoice payments.
  - c. The Cash Flow Reserve Fund target minimum is \$3M
  - d. Should not be used for recurring expenses
  
- **Operating and Capital Reserve Fund**
  - a. Classified as an unassigned fund balance
  - b. Funded by carryover, alternative fuel tax credits, excess sales tax revenue, and other fungible revenues
  - c. No target minimum amount designated
  - d. The Operating and Capital Reserve Fund has no target minimum
    - This fund would be a source for various Capital purchases and for use as local match for State and Federal grants
  - a. Should avoid using for recurring expenses
  
- **Workers' Compensation Reserve Fund**
  - a. Classified as a committed fund balance
  - b. Target minimum amount will be based on a bi-annual study of potential liability areas and risk
  - c. The Workers' Compensation Reserve Fund target minimum is \$2.1M
  - d. Should not be used for recurring expenses
  
- **Liability Insurance Reserve Fund**
  - a. Classified as a committed fund balance
  - b. Target minimum amount will be calculated annually based on the 5-year rolling average of outstanding claims at fiscal year-end, and an analysis of other potential risk considerations
  - c. The Liability Insurance Reserve Fund target minimum is \$767K
  - d. Should not be used for recurring expenses

All reserve funds will be recorded in the financial records as Board-designated reserves, included in the annual fiscal year budget, and broken out by the funds reflected in this policy. Reserve funds will be funded and available in cash or cash equivalent funds and will be maintained with the general cash accounts of the organization.

The CEO is responsible for assuring that the reserve funds are maintained and used only as described in this Reserve Fund Policy. The use of reserve funds will be reported to the Board annually through the annual fiscal year budget process, including a special notation reflecting any underfunded categories and a proposed recovery schedule.

If the reserve fund cannot be replenished by the next annual fiscal year budget, a repayment plan not to exceed three years will be proposed for Board consideration. The Finance Department shall maintain Board-approved policies which may contain provisions that affect the creation, sufficiency, and management of the reserve funds.

This Policy is reviewed every other year, at minimum, by the Finance Department, or sooner if warranted by internal or external events or changes. The following clarification modifications to the Reserve Fund Policy are recommended to the Board of Directors by Staff:

- 1.7.1010 - Additional Definitions and Acronyms
- 1.7.206 - Purpose and Applicability
- 1.7.401 - Operations Sustainability Reserve Fund
- 1.7.502 - Cash Flow Reserve Fund, Board Policy
- 1.7.1102 - Administration of Policy

Staff is also recommending changing the Operations Sustainability Reserve Fund target minimum balance from two months to three months. This would change the target minimum from \$7.5M to \$11.25M.

By a 2/3 vote of the Board, the Board may amend or revise the Reserve Fund Policy or temporarily waive the provisions of the Policy to allow reserve funds to be used to resolve an emergency funding situation not covered under this Policy, or to temporarily bridge an operating budget funding gap.

METRO has created an Administrative Code to codify policies enacted by the Board. Staff recommends that the Board adopt the revised Reserve Fund Policy within the Administrative Code, so that it reflects the current responsibilities and practices of the Finance Department, in relation to the use and replenishment of the reserve funds.

#### **IV. FINANCIAL CONSIDERATIONS/IMPACT**

Revising the Reserve Fund Policy, via the Administrative Code, will give guidance on how revenues above reoccurring expenses will be placed back into the reserve funds.

Maintaining solid reserves for the future is a key to METRO producing balanced budgets and being prepared for opportunities of growth, technological advancement in the future, and mitigation of financial risk.

#### **V. ALTERNATIVES CONSIDERED**

- Do nothing is an alternative but not recommended. These changes are needed so that the Reserve Fund Policy reflects the current responsibilities and practices of the Finance Department, in relation to the use and replenishment of the reserve funds.

#### **VI. ATTACHMENTS**

**Attachment A:** Resolution adopting Chapter 7 to Title I of the Santa Cruz METRO Administrative Code

**Exhibit A:** Reserve Fund Policy – Redline Version

**Exhibit B:** Reserve Fund Policy – Clean Version

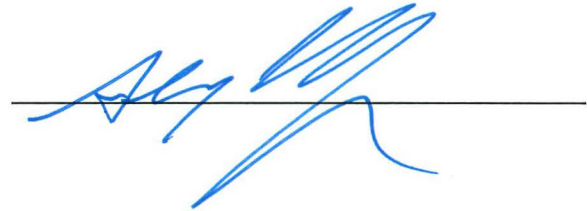
Prepared by: Angela Aitken, CFO

**VII. APPROVALS:**

Approved as to fiscal impact:  
Angela Aitken, CFO



Alex Clifford, CEO/General Manager



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**BEFORE THE BOARD OF DIRECTORS OF THE  
SANTA CRUZ METROPOLITAN TRANSIT DISTRICT**

Resolution No.  
On the Motion of Director:  
Duly Seconded by Director:  
The Following Resolution is Adopted:

**A RESOLUTION OF THE  
SANTA CRUZ METROPOLITAN TRANSIT DISTRICT ADOPTING  
CHAPTER 7 TO TITLE I OF THE SANTA CRUZ METRO  
ADMINISTRATIVE CODE**

**WHEREAS**, it is in the interest of the Santa Cruz Metropolitan Transit District to have a Reserve Fund Policy; and

**WHEREAS**, on October 23, 2015 meeting, the Board of Directors created a formal policy on Reserves that will ensure strong fiscal management; and

**WHEREAS**, the provisions of the policy reflect that it can be amended, revised, or temporarily waived by a Board vote of two-thirds, for an emergency funding situation or temporary operating budget funding gap,

**NOW, THEREFORE, BE IT RESOLVED BY THE BOARD OF DIRECTORS OF THE SANTA CRUZ METROPOLITAN TRANSIT DISTRICT**, that it hereby resolves, determines and orders as follows:

1. That the revised Reserve Fund policy attached hereto as Exhibit A, and presented to the Board of Directors is hereby adopted.

**PASSED AND ADOPTED** this 8<sup>th</sup> Day of November, 2019 by the following vote:

**AYES:** Directors -

**NOES:** Directors –

Resolution No. \_\_\_\_\_  
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**ABSTAIN:** Directors -

**ABSENT:** Directors -

\_\_\_\_\_  
ED BOTTORFF  
Chairperson

ATTEST:

\_\_\_\_\_  
ALEX CLIFFORD  
CEO/General Manager

APPROVED AS TO FORM:

\_\_\_\_\_  
JULIE SHERMAN  
District Counsel



SANTA CRUZ METROPOLITAN TRANSIT DISTRICT

ADMINISTRATIVE CODE

TITLE I – ADMINISTRATION

CHAPTER 7

RESERVE FUND POLICY

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Article 1

General Requirements

Definitions

**§1.7.101** Reporting of Fund Balances (defined as the excess of assets over liabilities) is guided by complying with Governmental Accounting Standards Board (GASB) Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions. GASB 54 defines five separate components of fund balance, each of which identifies the

extent to which Santa Cruz METRO is bound to honor constraints on the specific purposes for which amounts can be spent:

The following capitalized words and phrases whenever used in this Chapter shall be construed as defined below:

- §1.7.102** BOARD shall mean the Board of Directors of the Santa Cruz Metropolitan Transit District (Santa Cruz METRO).
- §1.7.103** GENERAL MANAGER shall mean the Chief Executive Officer (CEO) of Santa Cruz METRO appointed by the Board of Directors.
- §1.7.104** SANTA CRUZ METRO shall mean the Santa Cruz Metropolitan Transit District as established and operated under Part 10, Division 10 of the *California Public Utilities Code*.
- §1.7.105** NONSPENDABLE fund balance (not in spendable form such as inventories, prepaids, long-term receivables, or non-financial assets held for resale).
- §1.7.106** RESTRICTED fund balance (extremely enforceable limitations on use such as debt covenants, grantors, contributors, or laws and regulations of other governments).
- §1.7.107** COMMITTED fund balance (constrained to specific purposes by a formal action of the Board such as an ordinance, resolution, or policy).
- §1.7.108** ASSIGNED fund balance (limited to the Board's intent to be used for a specific purpose, but not Restricted or Committed).
- §1.7.109** UNASSIGNED fund balance (residual net resources, either positive or negative, in excess of the other four fund balance components). Unassigned amounts are available for any purpose with Board approval.

**§1.7.1010 Additional Definitions and Acronyms**

CARRYOVER – End of Fiscal Year favorable variance

FTA - Federal Transit Agency Administration

GASB – Governmental Accounting Standards Board

STA – State Transit Assistance

STIC –Small Transit Intensive Cities Program (FTA)

STRUCTURAL DEFICIT - a fiscal budget situation in which recurring expenses exceed recurring revenues.

UNRESTRICTED FUNDS – funds available for any operating or capital expense use.

## Article II

### Purpose and Applicability

- §1.7.201** As a public agency, Santa Cruz METRO shall provide safe, reliable fiscally responsible service to our customers. To that end, a policy to fund and spend reserves is being presented. The purpose of the Reserve Fund Policy is to ensure the long-term economic stability of the agency.
- §1.7.202** This policy will establish formal fiscal reserve guidelines that will ensure strong fiscal management, guide future agency decisions, maintain the fiscal stability of the organization, and place the agency in a position to better respond to unanticipated fiscal challenges and risks as they occur.
- §1.7.203** A key element of prudent financial planning is to ensure there are sufficient reserves to cover current operating and capital cash flows. Additionally, good fiscal responsibility requires anticipating the likelihood of, and preparing for, unforeseen disruptions in cash flow. Santa Cruz METRO will at all times, strive to have sufficient funding available to meet its operating and capital obligations.
- §1.7.204** Based on an analysis of “best practices” and quantitative standards, this policy strives to maintain a stable and positive financial position for the foreseeable future. Moreover, it provides guidelines to staff in planning and directing the day-to-day financial affairs, and in developing the annual two-year budget.
- §1.7.205** Properly designed guidelines send a positive signal to the community, our customers, our stakeholders, rating agencies, and regulatory agencies, that the Board of Directors (Board) is committed to the agency’s long-term financial health, stability, and viability.
- §1.7.206** This policy will help provide the agency with unrestricted funds with which to stabilize the agency’s finances, and position it to better absorb economic downturns, unforeseen disruptions in cash flow, meet generally accepted financial practices, ~~and~~ fund the local match for state and federal capital grants- and miscellaneous emergency capital purchases.

## Article III

### Goals

- §1.7.301** The goal of this policy is to establish adequate Reserve Funds through sound fiscal reserve guiding principles that will guide agency staff when making financial recommendations to the Board.
- §1.7.302** If the agency chooses to borrow funds in the future, a fiscally sound Reserve Fund Policy will contribute to a positive credit rating. A better credit rating results in a lower cost of borrowing.

**Article IV****Operations Sustainability Reserve Fund**

- §1.7.401** The Operations Sustainability Reserve Fund is an unrestricted fund intended to provide an internal source of funds for unanticipated situations such as a sudden increase in expenses, significant one-time unbudgeted expenses, unanticipated loss in funding, economic downturns, or uninsured losses. This reserve fund ~~will ensure~~ intends to provide continuity of service (on a short-term basis), regardless of disruptions in cash flow, and is considered working capital to be used to fund current non-recurring expenses as needed without borrowing. This fund is sometimes referred to as a “rainy day fund”.
- §1.7.402** The Operations Sustainability Reserve Fund is not intended to replace a permanent loss of funds or fill an ongoing budget gap such as a structural deficit. It is the intention of Santa Cruz METRO that when the Operations Sustainability Reserve Fund is used, they be used on a short-term basis and replenished within a reasonably short period of time (i.e. one fiscal year).
- §1.7.403** **Board Policy** - The Operations Sustainability Reserve Fund is defined as a designated fund set aside by action of the Board of Directors, and is classified as a committed fund balance. The minimum amount to be designated as Operations Sustainability Reserve will be established in an amount sufficient to cover all operating expenses for a set period of time, measured in months. The minimum Operations Sustainability Reserve Fund shall be equal to two (2) months of the average operating expenses for the most current fiscal year’s budget, and will be adjusted annually through the budget process. The calculation of average monthly operating costs includes, but is not limited to all recurring, operating expenses such as salaries and benefits, overhead, travel and training, and ongoing professional services. Depreciation, in-kind, and other non-cash expenses are not included in the calculation. The Board will attempt to fully fund the Operations Sustainability Reserve Fund within three-years of the adoption of this policy. The Operations Sustainability Reserve Fund shall not be used to support recurring operating expenditures.

**Article V****Cash Flow Reserve Fund**

- §1.7.501** The Cash Flow Reserve Fund is an unrestricted fund intended to provide funds to protect the agency’s ability to meet payroll and pay its bills through the ebbs and flows of revenue flows. Since some grants are awarded on a reimbursable basis, this will also include payment of grant-funded expenses prior to being reimbursed by the awarding grant entity.

**§1.7.502** **Board Policy** - The Cash Flow Reserve Fund is defined as a designated fund set aside by action of the Board of Directors, and is classified as a committed fund balance. The target minimum amount ~~to be designated~~ to the as Cash Flow Reserve Fund will be ~~set reviewed~~ annually ~~through~~ during the budget process. Recommended changes to the target minimum will be communicated when the Schedule of Reserve Account Balances is presented to the Finance, Budget, and Audit Committee and the Board. ~~The target minimum amount and~~ is calculated ~~annually~~ based on a review of all current reimbursable grants, a revenue flow analysis, and invoice payments. In tight or difficult financial times, a fully funded Operations Sustainability Reserve Fund can double as the Cash Flow Fund. The Board will attempt to fully fund the Cash Flow Reserve Fund within three-years of the adoption of this policy. The Cash Flow Reserve Fund shall not be used to support recurring operating expenditures.

## Article VI

### Operating and Capital Reserve Fund

**§1.7.601** Maintaining the Santa Cruz METRO system in a state-of-good-repair is paramount to the stability and success of Santa Cruz METRO. A system is in a state-of-good-repair when all maintenance is performed at scheduled intervals; all facilities are properly maintained and without deferred maintenance; and all vehicles receive scheduled mid-life overhauls and are replaced when they reach the end of their useful life. The Operating and Capital Reserve Fund is intended to provide match for grants, used for capital and operating expenditures that might not otherwise have a grant-funding source or qualify for grant funding and to cover certain unanticipated operating expenses that cannot be capitalized. Use of the Operating and Capital Reserve Fund shall be limited to one-time expenditures and is not intended for recurring commitments.

**§1.7.602** **Board Policy** - The Operating and Capital Reserve Fund is defined as a designated fund set aside by action of the Board of Directors, and is classified as an unassigned fund balance. There is no target minimum amount to be designated for the Operating and Capital Reserve Fund since its funding source comes from what might generally be considered unanticipated surpluses such as fiscal year budget surplus (carryover) and unrestricted funds such as sales tax, farebox revenues, leases, advertising, and fuel tax credit, just to name a few examples. The Operating and Capital Reserve Fund shall not be used to support recurring operating expenditures.

**§1.7.603** The CEO is authorized to exercise the CEO Board authorized authority of up to \$50,000 to allocate these funds for the uses noted in this policy. All uses of this fund in excess of \$50,000 must be approved by the Board.

**Article VII****Workers' Compensation Reserve Fund**

- §1.7.701** The Workers' Compensation Reserve Fund is intended to provide funds to meet expenses associated with Santa Cruz METRO's self-insurance programs, losses that exceed insurance coverage, as well as deductible costs or losses not covered by insurance. The Workers' Compensation Reserve Fund shall be maintained at a level that will adequately indemnify the agency against loss. A bi-annual study of potential liability areas and risk shall be the basis for determining minimum reserves.
- §1.7.702** **Board Policy** - The Workers' Compensation Reserve Fund is defined as a designated fund set aside by action of the Board of Directors, and is classified as a committed fund balance. The Workers' Compensation Reserve Fund will be calculated bi-annually after an actuarial review has been performed. Annually, the Workers' Compensation Reserve Fund level will be included in the annual fiscal budget process. The Board will attempt to fully fund the Workers' Compensation Reserve Fund within two years of the adoption of this policy. The Workers' Compensation Reserve fund shall not be used to support recurring operating expenditures.

**Article VIII****Liability Insurance Reserve Fund**

- §1.7.801** The Liability Insurance Reserve Fund is intended to provide funds to meet Santa Cruz METRO's self-insurance programs, liability, insurance deductibles, self-insurance minimums, the first layer of a multi-layered insurance program, and to cover exposure where no insurance exists. This Fund is also used when exposure or losses exceed insurance coverage.
- §1.7.802** **Board Policy** - The Liability Insurance Reserve Fund is defined as a designated fund set aside by action of the Board of Directors, and is classified as a committed fund balance. The Liability Insurance Reserve Fund will be calculated annually based on the 5-year rolling average of outstanding claims at fiscal year end, and an analysis of other potential risk considerations. The Liability Insurance Reserve Fund balance will be approved by the Board through the annual fiscal budget process. The Board will attempt to fully fund the Liability Insurance Reserve Fund within the next fiscal year budget following the adoption of this policy. The Liability Insurance Reserve Fund shall not be used to support recurring operating expenditures.

**Article IX****Funding and Accounting for Reserve Funds**

- §1.7.901** All Reserve Funds are funded with surplus or “carryover” of unrestricted operating and capital funds.
- §1.7.902** Reserve Funds will be recorded in the financial records as Board-Designated reserves, included in the annual fiscal year budget, and broken out by the funds reflected in this policy. Reserve Funds will be funded and available in cash or cash equivalent funds. Reserve Funds will be maintained with the general cash accounts of the organization.

**Article X****Reporting, Monitoring and Replenishing of Reserves**

- §1.7.1001** The CEO is responsible for assuring that the Reserve funds are maintained and used only as described in this Reserve Fund Policy. The use of Reserve Funds will be reported to the Board annually through the annual fiscal year budget process, including a special notation reflecting any underfunded categories and a proposed recovery schedule.
- §1.7.1002** If the Reserve Fund cannot be replenished by the next annual Fiscal Year Budget, a repayment plan not to exceed three (3) years will be proposed for Board consideration.

**Article XI****Administration of Policy**

- §1.7.1101** The Finance Department shall maintain Board-approved policies, which may contain provisions that affect the creation, sufficiency, and management of the Reserve Funds.
- §1.7.1102** The Finance Department shall review this policy every other year, at a minimum, or sooner if warranted by internal or external events or changes. Modifications to the Reserve Fund Policy will be recommended by the Finance Department to the Finance, Budget and Audit Committee, and ultimately the Board, ~~of Directors.~~

**Article XII****Changes/Waivers to the Reserve Fund Policy**

- §1.7.1201** By a 2/3 vote of the Board, the Board may amend or revise the Reserve Fund Policy or temporarily waive the provisions of the policy to allow Reserve funds to be used to resolve an emergency funding situation not covered under this policy, or to temporarily bridge an Operating Budget funding gap.

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SANTA CRUZ METROPOLITAN TRANSIT DISTRICT

ADMINISTRATIVE CODE

TITLE I – ADMINISTRATION

CHAPTER 7

RESERVE FUND POLICY

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Article 1

General Requirements

Definitions

**§1.7.101** Reporting of Fund Balances (defined as the excess of assets over liabilities) is guided by complying with Governmental Accounting Standards Board (GASB) Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions. GASB 54 defines five separate components of fund balance, each of which identifies the

extent to which Santa Cruz METRO is bound to honor constraints on the specific purposes for which amounts can be spent:

The following capitalized words and phrases whenever used in this Chapter shall be construed as defined below:

- §1.7.102** BOARD shall mean the Board of Directors of the Santa Cruz Metropolitan Transit District (Santa Cruz METRO).
- §1.7.103** GENERAL MANAGER shall mean the Chief Executive Officer (CEO) of Santa Cruz METRO appointed by the Board of Directors.
- §1.7.104** SANTA CRUZ METRO shall mean the Santa Cruz Metropolitan Transit District as established and operated under Part 10, Division 10 of the *California Public Utilities Code*.
- §1.7.105** NONSPENDABLE fund balance (not in spendable form such as inventories, prepaids, long-term receivables, or non-financial assets held for resale).
- §1.7.106** RESTRICTED fund balance (extremely enforceable limitations on use such as debt covenants, grantors, contributors, or laws and regulations of other governments).
- §1.7.107** COMMITTED fund balance (constrained to specific purposes by a formal action of the Board such as an ordinance, resolution, or policy).
- §1.7.108** ASSIGNED fund balance (limited to the Board's intent to be used for a specific purpose, but not Restricted or Committed).
- §1.7.109** UNASSIGNED fund balance (residual net resources, either positive or negative, in excess of the other four fund balance components). Unassigned amounts are available for any purpose with Board approval.
- §1.7.1010 Additional Definitions and Acronyms**
- CARRYOVER – End of Fiscal Year favorable variance  
 FTA - Federal Transit Administration  
 GASB – Governmental Accounting Standards Board  
 STA – State Transit Assistance  
 STIC –Small Transit Intensive Cities Program (FTA)  
 STRUCTURAL DEFICIT - a fiscal budget situation in which recurring expenses exceed recurring revenues.  
 UNRESTRICTED FUNDS – funds available for any operating or capital expense use.

## Article II

### Purpose and Applicability

- §1.7.201** As a public agency, Santa Cruz METRO shall provide safe, reliable fiscally responsible service to our customers. To that end, a policy to fund and spend reserves is being presented. The purpose of the Reserve Fund Policy is to ensure the long-term economic stability of the agency.
- §1.7.202** This policy will establish formal fiscal reserve guidelines that will ensure strong fiscal management, guide future agency decisions, maintain the fiscal stability of the organization, and place the agency in a position to better respond to unanticipated fiscal challenges and risks as they occur.
- §1.7.203** A key element of prudent financial planning is to ensure there are sufficient reserves to cover current operating and capital cash flows. Additionally, good fiscal responsibility requires anticipating the likelihood of, and preparing for, unforeseen disruptions in cash flow. Santa Cruz METRO will at all times, strive to have sufficient funding available to meet its operating and capital obligations.
- §1.7.204** Based on an analysis of “best practices” and quantitative standards, this policy strives to maintain a stable and positive financial position for the foreseeable future. Moreover, it provides guidelines to staff in planning and directing the day-to-day financial affairs, and in developing the annual two-year budget.
- §1.7.205** Properly designed guidelines send a positive signal to the community, our customers, our stakeholders, rating agencies, and regulatory agencies, that the Board of Directors (Board) is committed to the agency’s long-term financial health, stability, and viability.
- §1.7.206** This policy will help provide the agency with unrestricted funds with which to stabilize the agency’s finances, and position it to better absorb economic downturns, unforeseen disruptions in cash flow, meet generally accepted financial practices, fund the local match for state and federal capital grants and miscellaneous emergency capital purchases.

## Article III

### Goals

- §1.7.301** The goal of this policy is to establish adequate Reserve Funds through sound fiscal reserve guiding principles that will guide agency staff when making financial recommendations to the Board.
- §1.7.302** If the agency chooses to borrow funds in the future, a fiscally sound Reserve Fund Policy will contribute to a positive credit rating. A better credit rating results in a lower cost of borrowing.

**Article IV****Operations Sustainability Reserve Fund**

- §1.7.401** The Operations Sustainability Reserve Fund is an unrestricted fund intended to provide an internal source of funds for unanticipated situations such as a sudden increase in expenses, significant one-time unbudgeted expenses, unanticipated loss in funding, economic downturns, or uninsured losses. This reserve fund intends to provide continuity of service (on a short-term basis) regardless of disruptions in cash flow, and is considered working capital to be used to fund current non-recurring expenses as needed without borrowing. This fund is sometimes referred to as a “rainy day fund”.
- §1.7.402** The Operations Sustainability Reserve Fund is not intended to replace a permanent loss of funds or fill an ongoing budget gap such as a structural deficit. It is the intention of Santa Cruz METRO that when the Operations Sustainability Reserve Fund is used, they be used on a short-term basis and replenished within a reasonably short period of time (i.e. one fiscal year).
- §1.7.403** **Board Policy** - The Operations Sustainability Reserve Fund is defined as a designated fund set aside by action of the Board of Directors, and is classified as a committed fund balance. The minimum amount to be designated as Operations Sustainability Reserve will be established in an amount sufficient to cover all operating expenses for a set period of time, measured in months. The minimum Operations Sustainability Reserve Fund shall be equal to two (2) months of the average operating expenses for the most current fiscal year’s budget, and will be adjusted annually through the budget process. The calculation of average monthly operating costs includes, but is not limited to all recurring, operating expenses such as salaries and benefits, overhead, travel and training, and ongoing professional services. Depreciation, in-kind, and other non-cash expenses are not included in the calculation. The Board will attempt to fully fund the Operations Sustainability Reserve Fund within three-years of the adoption of this policy. The Operations Sustainability Reserve Fund shall not be used to support recurring operating expenditures.

**Article V****Cash Flow Reserve Fund**

- §1.7.501** The Cash Flow Reserve Fund is an unrestricted fund intended to provide funds to protect the agency’s ability to meet payroll and pay its bills through the ebbs and flows of revenue flows. Since some grants are awarded on a reimbursable basis, this will also include payment of grant-funded expenses prior to being reimbursed by the awarding grant entity.

**§1.7.502** **Board Policy** - The Cash Flow Reserve Fund is defined as a designated fund set aside by action of the Board of Directors, and is classified as a committed fund balance. The target minimum amount designated to the Cash Flow Reserve Fund will be reviewed annually during the budget process. Recommended changes to the target minimum will be communicated when the Schedule of Reserve Account Balances is presented to the Finance, Budget, and Audit Committee and the Board. The target minimum amount is calculated based on a review of all current reimbursable grants, a revenue flow analysis, and invoice payments. In tight or difficult financial times, a fully funded Operations Sustainability Reserve Fund can double as the Cash Flow Fund. The Board will attempt to fully fund the Cash Flow Reserve Fund within three-years of the adoption of this policy. The Cash Flow Reserve Fund shall not be used to support recurring operating expenditures.

## Article VI

### Operating and Capital Reserve Fund

**§1.7.601** Maintaining the Santa Cruz METRO system in a state-of-good-repair is paramount to the stability and success of Santa Cruz METRO. A system is in a state-of-good-repair when all maintenance is performed at scheduled intervals; all facilities are properly maintained and without deferred maintenance; and all vehicles receive scheduled mid-life overhauls and are replaced when they reach the end of their useful life. The Operating and Capital Reserve Fund is intended to provide match for grants, used for capital and operating expenditures that might not otherwise have a grant-funding source or qualify for grant funding and to cover certain unanticipated operating expenses that cannot be capitalized. Use of the Operating and Capital Reserve Fund shall be limited to one-time expenditures and is not intended for recurring commitments.

**§1.7.602** **Board Policy** - The Operating and Capital Reserve Fund is defined as a designated fund set aside by action of the Board of Directors, and is classified as an unassigned fund balance. There is no target minimum amount to be designated for the Operating and Capital Reserve Fund since its funding source comes from what might generally be considered unanticipated surpluses such as fiscal year budget surplus (carryover) and unrestricted funds such as sales tax, farebox revenues, leases, advertising, and fuel tax credit, just to name a few examples. The Operating and Capital Reserve Fund shall not be used to support recurring operating expenditures.

**§1.7.603** The CEO is authorized to exercise the CEO Board authorized authority of up to \$50,000 to allocate these funds for the uses noted in this policy. All uses of this fund in excess of \$50,000 must be approved by the Board.

**Article VII****Workers' Compensation Reserve Fund**

- §1.7.701** The Workers' Compensation Reserve Fund is intended to provide funds to meet expenses associated with Santa Cruz METRO's self-insurance programs, losses that exceed insurance coverage, as well as deductible costs or losses not covered by insurance. The Workers' Compensation Reserve Fund shall be maintained at a level that will adequately indemnify the agency against loss. A bi-annual study of potential liability areas and risk shall be the basis for determining minimum reserves.
- §1.7.702** **Board Policy** - The Workers' Compensation Reserve Fund is defined as a designated fund set aside by action of the Board of Directors, and is classified as a committed fund balance. The Workers' Compensation Reserve Fund will be calculated bi-annually after an actuarial review has been performed. Annually, the Workers' Compensation Reserve Fund level will be included in the annual fiscal budget process. The Board will attempt to fully fund the Workers' Compensation Reserve Fund within two years of the adoption of this policy. The Workers' Compensation Reserve fund shall not be used to support recurring operating expenditures.

**Article VIII****Liability Insurance Reserve Fund**

- §1.7.801** The Liability Insurance Reserve Fund is intended to provide funds to meet Santa Cruz METRO's self-insurance programs, liability, insurance deductibles, self-insurance minimums, the first layer of a multi-layered insurance program, and to cover exposure where no insurance exists. This Fund is also used when exposure or losses exceed insurance coverage.
- §1.7.802** **Board Policy** - The Liability Insurance Reserve Fund is defined as a designated fund set aside by action of the Board of Directors, and is classified as a committed fund balance. The Liability Insurance Reserve Fund will be calculated annually based on the 5-year rolling average of outstanding claims at fiscal year end, and an analysis of other potential risk considerations. The Liability Insurance Reserve Fund balance will be approved by the Board through the annual fiscal budget process. The Board will attempt to fully fund the Liability Insurance Reserve Fund within the next fiscal year budget following the adoption of this policy. The Liability Insurance Reserve Fund shall not be used to support recurring operating expenditures.

**Article IX****Funding and Accounting for Reserve Funds**

- §1.7.901** All Reserve Funds are funded with surplus or “carryover” of unrestricted operating and capital funds.
- §1.7.902** Reserve Funds will be recorded in the financial records as Board-Designated reserves, included in the annual fiscal year budget, and broken out by the funds reflected in this policy. Reserve Funds will be funded and available in cash or cash equivalent funds. Reserve Funds will be maintained with the general cash accounts of the organization.

**Article X****Reporting, Monitoring and Replenishing of Reserves**

- §1.7.1001** The CEO is responsible for assuring that the Reserve funds are maintained and used only as described in this Reserve Fund Policy. The use of Reserve Funds will be reported to the Board annually through the annual fiscal year budget process, including a special notation reflecting any underfunded categories and a proposed recovery schedule.
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**Pension (UAL)  
and  
Retiree Medical (OPEB)  
Liabilities  
Recommendations to Reduce Liabilities**

Santa Cruz METRO Board of Directors

*November 8, 2019*

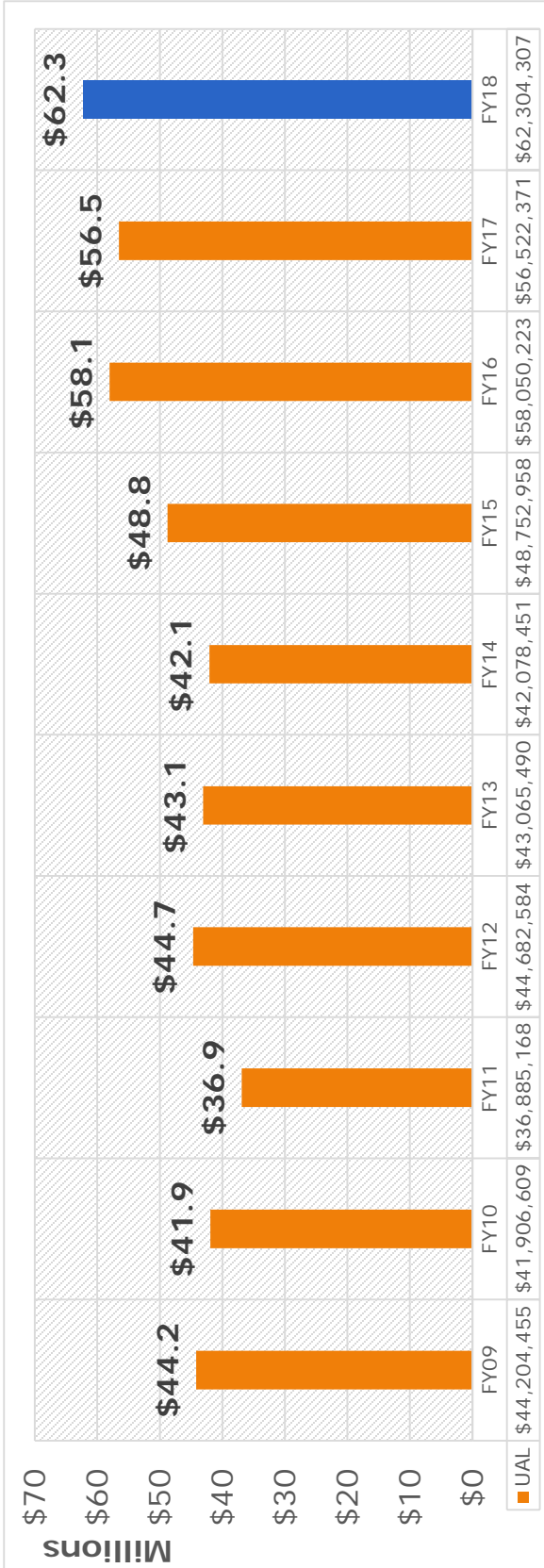
Angela Aitken, Chief Financial Officer

# Overview of Today's Presentation

- Pension Liability (UAL): Overview and Updates
- Retiree Medical Liability (OPEB): Overview and Updates
- What can we do to reduce the liabilities?
- What have we done so far to reduce the liabilities?
- What do we recommend to further reduce the liabilities?
- Questions

# Pension Liability (UAL): Overview & Updates

(as per CalPERS Actuarial Valuation Report as of June 30, 2018)



	June 30, 2017	June 30, 2018
1. Present Value of Projected Benefits	\$197,740,176	\$211,046,469
2. Entry Age Normal Accrued Liability	\$173,211,950	\$185,503,758
3. Market Value of Assets (MVA)	\$116,689,579	\$123,199,451
4. Pension Liability (UAL) (2-3) *	\$56,522,371	<b>\$62,304,307</b>
5. Funding Ratio ( 3/2 )	<b>67.4%</b>	<b>66.4%</b>

\* UAL is the gap between funds available and funds needed for retiree benefits.



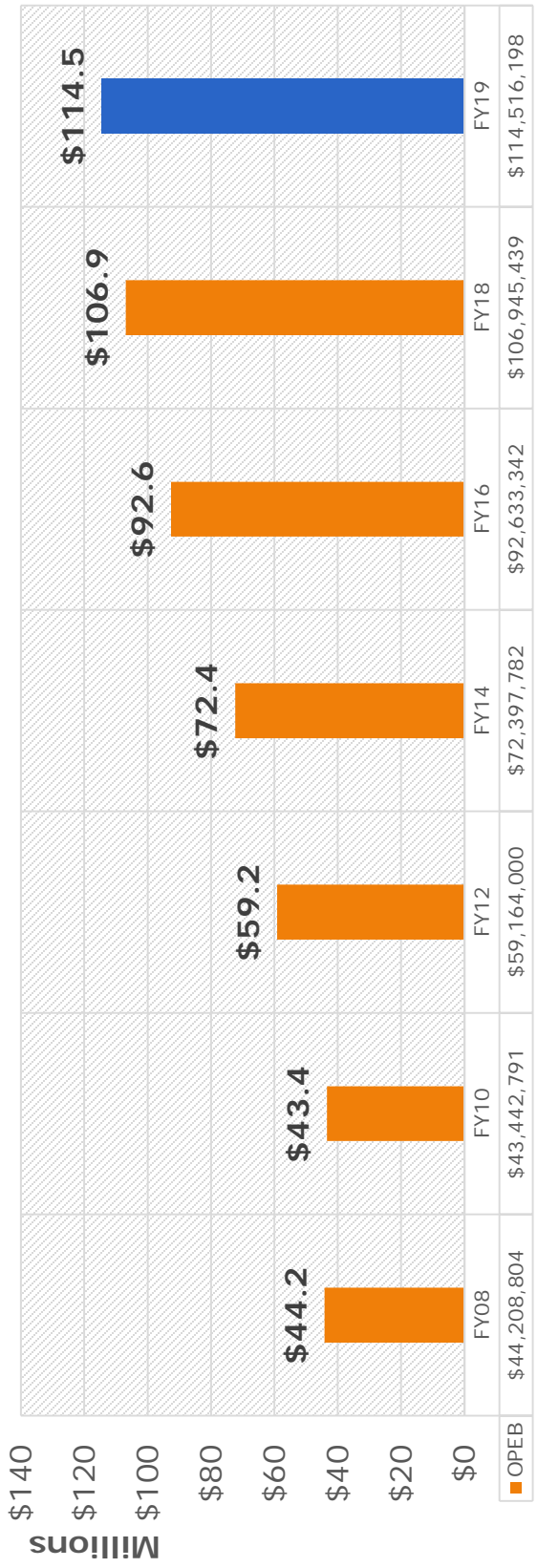
**Employer Contributions: Normal Cost & UAL**  
**Santa Cruz METRO: Projections FY21 – FY26**  
 (as per CalPERS Actuarial Valuation Report as of June 30, 2018)

	Required Contribution	Projected Future Employer Contributions (Assumes 7.00% Return for Fiscal FY19) *				
Fiscal Year	FY21	FY22	FY23	FY24	FY25	FY26
Normal Cost (% of Payroll)	10.448%	10.4%	10.4%	10.4%	10.4%	10.4%
Normal Cost \$ Payment (A)	\$2,071,638	\$2,118,829	\$2,177,097	\$2,236,967	\$2,298,484	\$2,361,692
UAL Payment (B)	\$4,586,794	\$5,052,000	\$5,437,000	\$5,674,000	\$5,955,000	\$5,837,000
Projected Payroll (2.75% growth)	\$19,828,082	\$20,373,354	\$20,933,622	\$21,509,297	\$22,100,803	\$22,708,574
Total Contribution (Illustrative only based on projected payroll ) (A+B)	\$6,658,432	\$7,170,829	\$7,614,097	\$7,910,967	\$8,253,484	\$8,198,692
Total Contribution as a % of Payroll	33.6%	35.2%	36.4%	36.8%	37.4%	36.2%

\*The Preliminary Rate of Return for FY19 is **6.7%**.

# Retiree Medical Liability (OPEB): Overview & Updates

(as of June 30, 2019)



METRO – OPEB Funding Status:	as of June 30, 2018	as of June 30, 2019
1. Total OPEB Liability (TOL)	\$106,945,439	\$114,516,198
2. Fiduciary Net Position (Value of Trust Assets) (Create an Irrevocable Trust)	\$0	\$0
3. Net Retiree Medical Liability OPEB Liability * (NOL) (1- 2)	\$106,945,439	\$114,516,198

\* Net OPEB Liability is the gap between funds available and funds needed for retiree benefits.



# What can we do to reduce the liabilities?

- Things we have done so far to reduce the liabilities:
  - 😊 Understand the two liabilities and make them visible to the public: **DONE**
  - 😊 Approve budget plans to set aside funds to reduce the liabilities: **DONE**
  - 😊 Prepay the Pension (UAL) portion for the Fiscal Year, before July 31<sup>st</sup>: **DONE**
  - 😊 Closely monitor and control personnel costs: **DONE**
- What do we recommend to further reduce our liabilities:
  - Make Additional Discretionary Payments (ADPs) toward paying down UAL
  - Work with CalPERS to establish Fresh Start UAL Amortization
  - Establish and prefund an Irrevocable Section 115 Trust for UAL and OPEB
  - Contract with an actuarial to run various financial scenarios

# What have we done, so far?

Understand the Liabilities and Make them Visible to the Public: Presentations to Board Members, Staff and Public at Finance Committee and Board Meetings in 2019

Approve Budget Plans to Set Aside Funds to Reduce the Liabilities: Board Approved (June 2019) transfers of \$2M\*/Year to a dedicated reserve fund

(\*The exact amount of the transfers depends on the availability of excess funds in the operating budget at year-end, unplanned / unbudgeted expense could reduce /eliminate the transfers)

Prepay the Pension Liability UAL Portion for the Year in FY20:  
\$4,044,788 Paid in July 2019  
= \$144,064 Savings for the Year

Closely Monitor and Control

Personnel Costs:

Average Labor Cost Increase for the last 5 Years (FY15-FY19) = **0.4%**;

As of Fall Negotiations with Unions:

- Negotiated **5% employee contribution for any medical plan** for SEIU and SMART FR, effective Jan 2021; **3%** for SMART PC, effective Jan 2022;
- Negotiated **increase in the quarterly payments** for those METRO employees **waiving our medical insurance program** (from \$300 to \$1,000/Qtr.)



# What Do We Recommend?

## Make Additional Discretionary Pension Liability (UAL) Payments:

- ✓ Payments can be made at a dedicated amount
- ✓ Allows for budgeting flexibility
- ✓ Can dedicate one-time funding or new revenue
- ✓ **Any additional payments made to the principal reduces the amount of interest paid in the future**

**\$1M** paid today reduces the amount of total interest paid by **\$1.6M**

**\$1M** paid every year for the next five years = **\$6.8M** of saved interest payments (as per CalPERS actuarial estimate based on our 2017 Valuation Report)

**OR**

## Fresh Start (Full or Partial) Pension Liability (UAL) Amortization:

- ✓ Must pay off faster than existing amortization schedule
- ✓ Create new minimum payment
- ✓ Significant long-term savings
- ✓ **Irrevocable (Full)**
- ✓ No Irrevocable election (Partial)

**15 Year Amortization = \$16M Estimated Savings**

**10 Year Amortization = \$32M Estimated Savings**  
(as per CalPERS Annual Valuation Report as of June 30, 2018)





# What Do We Recommend?

## Establish and Pre-Fund Irrevocable Section 115 Trusts for Pension (UAL) and Retiree Medical (OPEB):

- ✓ Contributions are restricted and cannot be used for other purposes
- ✓ Improved Credit Rating
- ✓ Reduction of Net Pension and Retiree Medical Liabilities
- ✓ There are costs associated with funding and managing a trust

## Contract with an Actuarial to Run Various Financial Scenarios to Help Reduce Pension and Retiree Medical Liabilities:

- ✓ They would incorporate changes to our Employee medical benefits currently offered
- ✓ They would analyze:
  - ✓ benefits of additional contributions to both liabilities
  - ✓ how those contributions are implemented to achieve maximum savings
  - ✓ benefits of creating the Trusts to pay towards both liabilities

# Questions

