DATE: October 30, 2019
TO: Members of the Board of Retirement
FROM: Tracy Bowman, Director of Finance
SUBJECT: THIRD QUARTER 2019 BUDGET TO ACTUALS REPORT

Written Report

Highlights

Third Quarter Target: 75% Used / 25% Remaining

<table>
<thead>
<tr>
<th>Administrative Budget</th>
<th>Actuals to Date</th>
<th>Annual Budget</th>
<th>Budget $ Remaining</th>
<th>Budget % Remaining</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personnel Costs</td>
<td>$10,247,742</td>
<td>$14,764,600</td>
<td>$4,516,858</td>
<td>30.6%</td>
</tr>
<tr>
<td>Service and Supplies</td>
<td>5,831,343</td>
<td>11,298,230</td>
<td>5,466,887</td>
<td>48.4%</td>
</tr>
<tr>
<td>Capital Expenditures</td>
<td>52,264</td>
<td>370,000</td>
<td>317,736</td>
<td>85.9%</td>
</tr>
<tr>
<td>Grand Total</td>
<td>$16,131,349</td>
<td>$26,432,830</td>
<td>$10,301,481</td>
<td>39.0%</td>
</tr>
</tbody>
</table>

Background/Discussion

The Board of Retirement approved OCERS’ Administrative Budget for Fiscal Year 2019 (FY19) on November 19, 2018, in the amount of $26,432,830 for administration and investment related activities.

OCERS’ budgeting authority is regulated by California Government Code Sections 31580.2 and 31596.1, including a provision that OCERS’ budget for administrative expenses is limited to twenty-one hundredths of one percent of the accrued actuarial liability of the retirement system, excluding investment related costs and expenditures for computer software, hardware and related technology consulting services (commonly referred to as the 21 basis point test). The approved FY19 administrative budget represents 8.93 basis points of the projected actuarial accrued liability. The budget also meets OCERS’ Board policy limitation of 18 basis points of the projected actuarial value of total assets and represents 14.20 basis points of these assets for FY19.

The Chief Executive Officer, or the Assistant CEO, has the authority to transfer funds within the three broad categories of the budget: 1) Personnel Costs, 2) Services and Supplies, and 3) Capital Expenditures. Funds may not be moved from one category to another without approval from the Board of Retirement.

Administrative Summary

For the nine months ended September 30, 2019, year-to-date actual administrative expenses were $16,131,349 or 61.0% of the $26,432,830 administrative budget and below the 75% target set for the end of the third quarter budget by approximately $3.7 million. A summary of all administrative expenses and explanations of significant variances are provided below:
Personnel Costs

Personnel Costs as of September 30, 2019 were approximately $10.2 million or 69.4% of the annual budget for this category. These costs are slightly below budget due to the timing of hiring new staff. The newly created Training Manager position adopted in the 2019 Budget was filled during the second quarter. During the third quarter, four staff vacancies were filled; two Retirement Program Specialists, one Staff Attorney and one Investment Analyst. Also in the third quarter, the Director of Member Services position became vacant and the search for a replacement is currently underway.

Services and Supplies

Expenditures for services and supplies were approximately $5.8 million or 51.6% of the annual budget for this category. The positive variance of $2.6 million between the pro-rated budget and year-to-date actuals is primarily due to the following:

- Building Property Mgmt./Maintenance costs utilized 45.5% of the annual budget and were lower than the prorated budget by $200,701. Lower overall costs are related to timing of payments for property
tax and insurance premiums, as well as postponement of a planned roof repair that has not yet occurred as of the end of the third quarter.

- Due Diligence costs are at 16.4% of the annual budget and lower than the prorated budget by $46,905. This lower than anticipated cost is due to fewer visits than planned. Due diligence visits to investment managers tend to fluctuate throughout the year and are often done in conjunction with other investment conference/training travel. Due diligence costs are expected to remain under budget through the remainder of the year.

- Equipment/Software expense utilized 26.3% of the annual budget, and is lower than the prorated budget by $343,809. The lower than expected expenditures is the result of several projects budgeted for the year which are either in process or have not been started as of the end of the third quarter, such as the manage file transfer solution, the board portal upgrade, rapid recovery appliance, patch management solution, change management solution and the anti-spam email solution. These expenses are expected to pick up later in the year. Additionally, miscellaneous hardware, software, and computer and printer supplies are running substantially below the prorated budget and are incurred on an as-needed basis.

- Infrastructure Maintenance costs are at 60.1% of the annual budget resulting in an unused prorated budget of $123,811. Various infrastructure maintenance costs associated with software and hardware support services did not incur costs until the third quarter, such as Microsoft Software Assurance and website hosting. Additionally, many hardware and software support services are currently lower than budgeted, including server and workstation hardware support, printer and computer room maintenance, other miscellaneous software and Oracle-V3 support.

- Legal Services are at 41.2% of the budget and are lower than the prorated budget by $499,201. Legal services for investments, litigation and tax counsel are utilized on an as-needed basis. Investment legal services are below budget by approximately $207,000. General board, tax counsel and other counsel services are under budget by approximately $292,000.

- Meetings & Mileage costs are slightly above the prorated budget for the quarter ended at 77.7%, or $1,645. The variance is primarily due to Board meeting costs including additional meetings for Personnel Committee and Disability Committee meetings that were added to the Board members meeting schedule, as well as travel to SACRS and legislative meetings by Board representatives. This category is expected to be within budget at year-end.

- Memberships/Periodical expense is at 90.1% of the annual budget which is above the prorated budget by $10,868. Memberships and periodical costs renew at different times throughout the year. In addition, membership costs have come in higher than expected. As the total amount expended under the Services and Supplies category remains under budget, an amendment is not required to cover the Membership budget shortfall at this time. The CEO or Assistant CEO has the authority to move budget dollars within the Services and Supplies category to cover the shortfall and as of the third quarter, there were sufficient dollars available in other Services and Supplies line items to offset this shortage.

- Postage is at 48.3% of the annual budget and lower than the prorated budget by $43,920. This is attributable to the timing of bulk mailings to members and the use of postage on an as-needed basis. In addition, the number of pages in the newsletter to members has been reduced resulting in a savings of postage, as more communication is done electronically. No additional mass mailings have been needed during 2019 to date.
• Printing costs are at 52.7% of the annual budget and lower than the prorated budget by $23,425. As with postage, printing costs are lower due to timing of mailings and a savings from the reduction in the number of pages in each mailing.

• Professional Services utilized 56.0% of the annual budget and are lower than the prorated budget by $1,205,932. The variance is primarily due to timing of expenses for various Information Security and IT related consulting such as Office 365 migration consulting and security penetration testing; cost savings in some areas such as Board election costs, actuarial services and investment risk reporting services; as well as costs used on an as-needed-basis, including internal audit consultants and services, CEO contingency and court reporter fees.

• Telephone expenses are at 59.1% of the annual budget, and currently below the prorated budget by $26,359. Telephone expenses are not expected to remain below budget as OCERS plans to switch to a new system during the fourth quarter.

• Training expense is at 48.7% of the annual budget and lower than the prorated budget by $127,797, primarily due to training costs that have been budgeted, but not yet incurred, including SACRS fall conference, investment-related conferences, employee tuition reimbursement, IT related training, and other various staff training and conferences.

**Capital Expenditures**

Capital Expenditures as of the third quarter total $52,264. Capital expenditures budgeted for the year are for building HVAC repair and board room audio visual improvements. The building HVAC has been partially serviced and additional capital expenditures have been incurred related to building assessment costs. The audio visual improvements for the board room are expected to be implemented later in the year or beginning of 2020.

**Conclusion:**

As of quarter-end, the Administrative budget based on preliminary actuals is at 61.0% of the annual budget. As actual administrative expenses are under the annual budget, OCERS is in compliance with the 21 basis point test and the 18 basis point test.

**Submitted by:**

Tracy Bowman
Director of Finance