

# Memorandum

**To:** Audit Committee of the ISO Board of Governors  
**From:** Ryan Seghesio, Chief Financial Officer & Treasurer  
**Date:** March 12, 2014  
**Re:** **Decision on modification to Retiree Medical Plan investment policy**

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*This memorandum requires Committee action.*

## EXECUTIVE SUMMARY

At its March 2013 meeting, the Audit Committee approved a new investment strategy for the assets associated with the ISO Retiree Medical Plan. The strategy was designed to better align the designated long-term assets of the plan to its long-term liabilities. In the months following the Committee meeting, the final investment policy was established and the investment strategy was executed. The new investment strategy has exceeded Management's expectations with regards to its impact on controlling the liabilities and expenses associated with administering the plan.

Upon the Chief Financial Officer's annual review of the investment policy, Management is proposing a minor modification to the terminology used to define the portfolio size. The current language uses the Accumulated Postretirement Benefit Obligation (APBO) to set the level of assets that will remain invested in this strategy. Although, it has been determined that it is more appropriate to use the Net Other Post-Employment Benefits (OPEB) Obligation, which represents the actual liability on the ISO balance sheet. The Net OPEB Obligation is a well-defined term within the ISO financial statements.

While these two defined numbers may be very similar, as they were last year, the APBO can be volatile and will quickly react to plan changes, assumptions, and investment performance. Those movements would cause corresponding increasing and decreasing of assets in the portfolio, which would be contrary to its long-term nature. In contrast, the Net OPEB Obligation stabilizes the impacts to the liability, allowing the portfolio to remain more constant.

Management recommends modifying the language in the Retiree Medical Plan Investment Policy as outlined below. The Employee Pension Benefit Committee has reviewed and approved these changes.

**Moved, that the Audit Committee of the ISO Board of Governors approves the modifications to the ISO Retiree Medical Plan Investment Policy as described in the memorandum dated March 12, 2014.**

## **POLICY LANGUAGE**

The first paragraph of Section VI-Appendices, of the investment policy will be modified as shown below:

Per the California Independent System Operator Corporation's Board of Governors approval at their March 20-21, 2013 meeting, and modified at their March 19-20, 2014 meeting, the designated assets associated with the ISO's balance sheet liability related to the Plan's present value of the Plan's liabilities, defined as the Net OPEB Obligation Accumulated Postretirement Benefit Obligation (APBO), will be invested in a manner similar to the Moderate Portfolio in the Pre-Mixed Portfolio Allocations defined in the ISO's Retirement Savings Benefits Plan (the 401(k)). The Net OPEB Obligation APBO is calculated annually by a third-party actuary and is described in detail in the contained within the ISO's audited financial statements. The designated assets are contained within two accounts at the Trustee/Custodian: 1) the Voluntary Employees Beneficiary Association (VEBA) Trust, which holds the assets, and any excess returns, associated with the liabilities of current retirees and employees who have reached the eligibility requirements of the Plan, and 2) the custody account, which holds the balance of the assets associated with the Net OPEB Obligation APBO but not yet transferred to the Trust. The ISO will annually adjust the assets contained in these accounts per the calculated Net OPEB Obligation APBO and the Trust's funding policy.