MEMORANDUM

To: Board of Trustees

From: Paul Miller, Director of Finance
Renee Zysk, Accounting Manager

Date: November 19, 2024

Subject: 2025 Administrative and Capital Budget

Executive Summary

The Board reviews and approves an annual Administrative and Capital budget each year. This memorandum and accompanying presentation will summarize the budget position and assumptions for the remainder of the current year, review multi-year trends that inform each year's budgetary process, propose a 2025 budget, and highlight major drivers for next year. The proposed 2025 budget consists of:

Operating budget (excluding depreciation)	$14,793,100
Administrative budget (includes depreciation)	$16,567,900
Capital budget	$ 2,957,800

2024 Budget Update

The updated 2024 budget projection provides an estimated beginning fund reserve balance for 2025, and a baseline for expense comparisons for year over year changes. Our actual financial results through September are combined with estimated expenses and revenues for the fourth quarter to create an updated 2024 budget projection. The resulting fund reserve balance for the 2024 budget process is estimated to be $20.3 million, which is approximately 17.3 months of budgeted expenses at December 31, 2024. Some highlights and variances in the 2024 budget include:

- Ohio DC's primary source of revenue is administrative fees deducted from participant accounts[1]. As a result of increased participant account values, 2024 fee revenues are projected to be $16,416,400 or 6.5 percent higher than budgeted. Interest income will be about $240,000 more than budgeted due to higher than anticipated reserve levels. Combined, staff forecasts that 2024 revenues will exceed the budget by about $1,249,100 or about 7.6 percent.

[1] Ohio DC charges participants a uniform administrative fee. The fee of 0.14 percent is capped at $55 quarterly and is waived on account balances below $5,000.

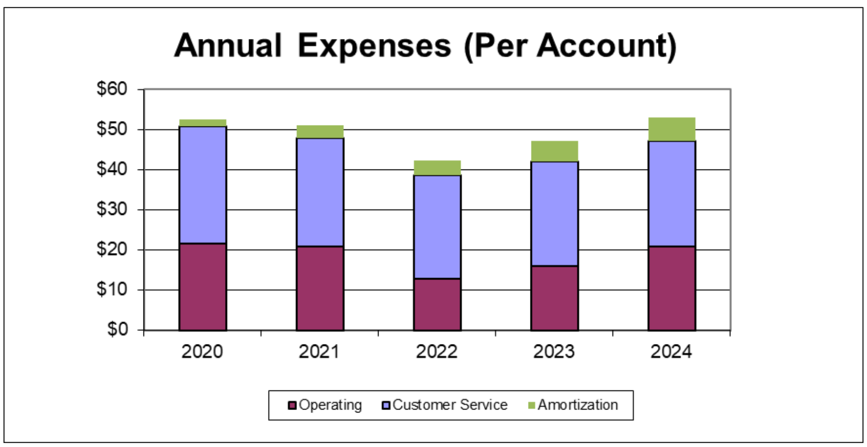
- Total 2024 administrative expenses are projected to be $14,486,600, which is $809,600 or 5.3 percent under the 2024 budget. The key budget variances were:

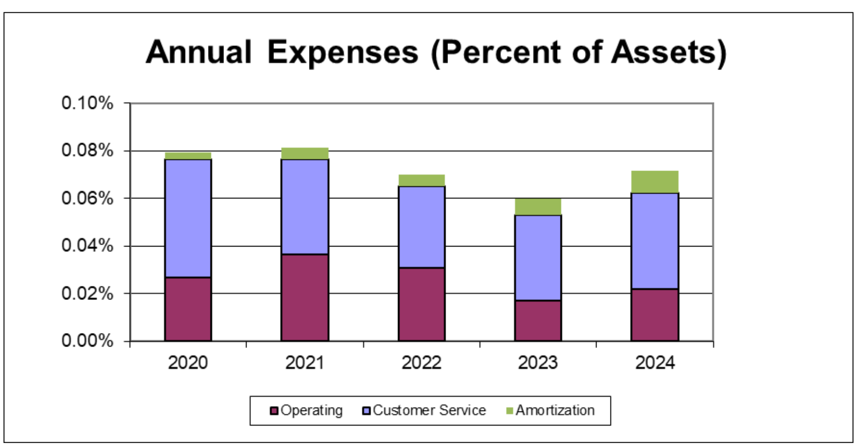
    - Employee salaries are $426,300 under budget due to various positions being budgeted, but not filled.
    - Customer service expense is $209,500 under budget due to higher-than-expected vacancies.
    - IT expenses are $110,600 under budget primarily due to the document management system project not being started in 2024.

- Total 2024 capital expenditures were budgeted at $2,981,800, which is in line with current projections.

<u>Budget Trends and Policies</u>

While the current year's budget is informative and necessary for estimating the year-end reserve balance, staff also analyzes budget trends over several years to validate assumptions for the upcoming year's revenues and expenses. The following trend data was used in support of the proposed 2025 budget.





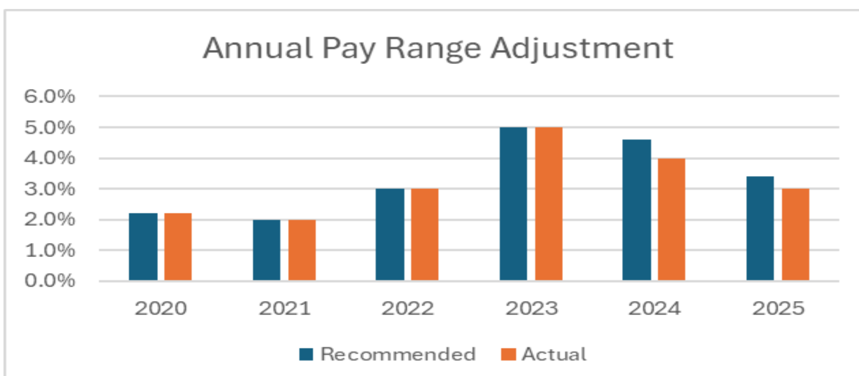
Budgeted Expenses—2025

The detailed expense budget for 2025 is based on past costs, trends, strategic objectives, contractual costs, and future operating plans, with expenses categorized monthly by category.

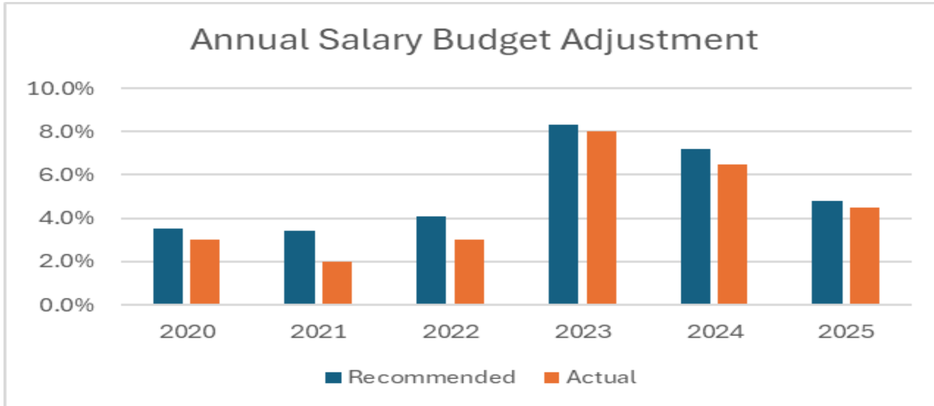
- Customer service expenses, primarily driven by the Nationwide contract, are our largest expense category. These costs are expected to rise by 4.3% due to scheduled increases in the contract being offset by some vacant positions. Total customer service expenses are budgeted at $7,876,900.

- Personnel and benefits, the next largest expense category, totals $3,912,600 in the 2025 budget. Three staff positions in the 2024 budget were eliminated, but four new positions have been added in 2025, plus the cost of executive leadership was moved from professional fees to this expense category. Health care costs/claims increased dramatically in early 2024, so this budget item was increased in 2025, in case this short-term trend continues.

    - Staff maintained the current 15-position pay range schedule with a 3.0% increase. While our smaller staff does not use every tier within the schedule, they have all been needed at some point in the past, and we expect they will be relevant for future hires and promotions. We suggest that a future compensation study can validate or revise the schedule for staffing needs at that time. Staff also consulted the prior compensation study and CBIZ recommendations regarding the historical pay range increases. Over the last several years, range adjustments have been equal to or lower than consultant recommendations:



    - Staff also reviewed historical salary budget increases and included a 4.5% increase in the 2025 budget. The increase to the salary budget is intended to fund cost of living raises, merit raises, and promotions. Historically, Ohio DC has tracked at or below the recommended salary budget increase provided by the compensation consultant. (See the next page for chart.)



- Information Technology (IT) expenses are budgeted to increase $397,000 in 2025 due to the addition of a $300,000 project to add a managed security operations center (SOC), which will increase our cyber security defenses. The budget was also increased for additional cloud services associated with 2025 projects.

- New IT projects completed in 2024 will lead to a $270,000 increase in depreciation expense in 2025, as we amortize their costs over the useful life of the project.

Overall operating expenses, excluding depreciation, are set to increase by 7.3% to $14,793,100, primarily due to the changes noted above.

Projected Revenues—2025

Most of Ohio DC's revenue comes from quarterly participant fees, which are based on participant account balances. Fees are designed to meet operating needs and are monitored closely to ensure that growing account values do not produce fees that outpace the cost of operating Ohio DC. Over time, any of the fee components can be adjusted by the Board to increase or decrease total fees, or to meet the changing administrative expenses, or capital needs of Ohio DC.

To project revenues for 2025, staff multiplied the estimated monthly values of participant accounts by the expected percent fee rate of 0.075 percent. This results in an estimated fee inflow of $16,477,600. This amount, together with existing cash reserves, should be sufficient to cover the estimated expenses for 2025, as well as provide funding for capital expenditures for ORIS and participant web portal enhancements and sustainability.

The projection includes a conservative net rate of return during 2025 of 3.50%. If the stock market underperforms this assumption, lower asset balances will produce less administrative fees. As a downside estimate, if we replace the slight projected growth in non-SVO assets with a loss of 20 percent, net assets would be about $3.4 billion lower, and annual administrative fees would decline by about $2.7 million. While the loss of this much revenue would be significant, it would only represent about 2 months of non-depreciation administrative expenses from Ohio DC reserves.

The 2025 administrative budget also includes $1,194,000 in interest income, a 17.8% increase over the 2024 budget due to the larger cash reserve balance.

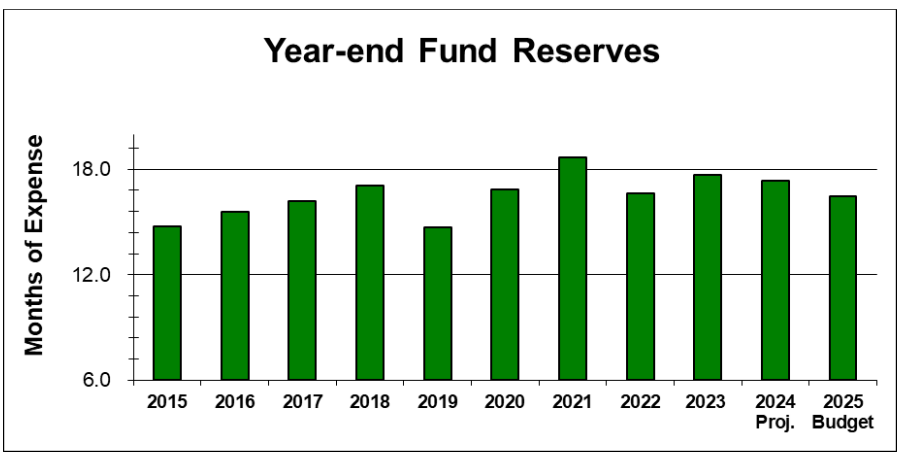
Capital Expenditure Budget—2025

Regular and ongoing Ohio DC capital expenditures include funds to purchase replacement computers, printers, copiers, office furniture, and a computer firewall. The 2025 budget for these items is $100,500. Capital expenditures in 2025 also will include the $225,000 cost of a document management system project, set up costs for a new managed SOC of $50,000, and $2,582,300 for system enhancements, cyber security and support from Peraton. Staff annually reviews all IT expenditures to determine how costs are expensed in the normal course of business or capitalized into the recordkeeping modernization project (and subsequently expensed/depreciated over the expected life of the enhancement).

Fund Reserves

The Ohio DC fund reserve policy targets six to 18 months of annual expenses (excluding depreciation) in reserve. Fund reserves are invested in short-term interest-bearing products such as money market funds or certificates of deposit until the funds are needed.

The chart below shows year-end fund reserves over the past decade. During this period, the stock markets have generally shown gains, resulting in increased revenues and increased fund reserves over the period. Ohio DC began the recordkeeping modernization project in 2015 and has generally maintained the same reserve levels during this period of higher capital expenditures. Our reserves in 2025 will maintain similar levels as 2024, near the top end of the reserve policy. If volume and performance of participant investments exceeds our expectations, staff may need to evaluate the need for a quarterly fee holiday or fee restructuring in 2025.



2025 PROPOSED BUDGET SUMMARY

DESCRIPTION	2025 PROPOSED	2024 APPROVED	24 TO 25 $ CHANGE	24 TO 25 % CHANGE
REVENUES:				
PARTICIPANT FEES	**$16,477,600**	$15,412,264	$1,065,336	**6.9%**
INTEREST INCOME	**1,194,000**	1,013,916	180,084	**17.8%**
OVERNIGHT FEE INCOME	**24,000**	19,200	$4,800	**25.0%**
TOTAL REVENUES	**17,695,672**	16,445,380	1,245,420	**7.6%**
CUSTOMER SERVICE	**7,876,900**	7,552,503	324,397	**4.3%**
PERSONNEL AND BENEFITS	**3,912,600**	3,594,015	318,585	**8.9%**
INFORMATION TECHNOLOGY (IT)	**1,147,400**	749,963	397,437	**53.0%**
COMMUNICATIONS	**606,700**	580,516	26,184	**4.5%**
PROFESSIONAL FEES	**540,000**	625,311	-85,310	**-13.6%**
OFFICE OPERATING COSTS	**472,800**	473,955	-1,155	**-0.2%**
INSURANCE	**236,700**	215,200	21,500	**10.0%**
TOTAL OPERATING BUDGET	**14,793,100**	13,791,464	1,001,636	**7.3%**
DEPRECIATION	**1,774,800**	1,504,752	270,048	**17.9%**
TOTAL ADMINISTRATIVE BUDGET	**16,567,900**	15,296,216	1,271,684	**8.3%**
NET REVENUES OVER EXPENSES	**$1,127,772**	$1,149,164	-$21,392	**-1.9%**
TOTAL CAPITAL BUDGET	**$2,957,800**	$2,981,800	-$24,000	**-0.8%**

Summary and Recommendations

Total administrative expenses are budgeted at $16,567,900 for 2025. This is an increase of $1,271,700 or 8.3% percent compared to the 2024 budget.

During 2025, Ohio DC will continue to build a document management system, engage a managed SOC partner, and perform routine enhancements to the recordkeeping system and participant website. These capital expenditures are budgeted at $2,957,800 in 2025.

Fund reserves are projected to be 17.3 months of 2024 budgeted expenses on December 31, 2024, which is nearing the high end of the funding policy six- to 18-month target range. Revenues over expenses of $1,127,700 are budgeted for 2025, which will result in an increase to our fund reserves, while capital expenditures will decrease our fund reserves. Our projected fund reserves will decrease slightly and be 16.4 months of 2025 budgeted expenses on December 31, 2025.

In conclusion, staff recommends approving the 2025 Administrative and Capital budget as presented.