NYSERDA'S PATH TO A 2040 NET ZERO INVESTMENT PORTFOLIO

Size and Description of Investment Portfolio

NYSERDA's Investment Portfolio as defined in the context of this initiative consists of two components: 1) a fund associated with health care benefits which is managed by NYSERDA, and 2) employee retirement funds housed in a combination of the State Retirement System and the Voluntary Defined Contribution plan.

1. <u>Health Care Benefits</u>

The New York Civil Service Law, Section 163(2) provides for health insurance coverage for retired employees of New York State including their spouses and dependent children. The law extends to public benefit corporations. Under this law, NYSERDA maintains a single-employer defined benefit plan to provide this benefit to eligible retirees and/or their spouses and dependent children. Eligibility is determined by membership in the System and New York State Voluntary Defined Contribution (VDC) Program, enrollment in the New York State Health Insurance Program at the time of retirement, and the completion of a minimum number of years of service.

Operationally, this plan is supported by a Trust, referred to as the Other Post-Employment Benefits (or OPEB) Trust, for the accumulation of funds to pay future benefit costs. Cash and investments of the OPEB Trust are held with a third-party trustee. The Trust is managed by the Officers of NYSERDA, in consultation with an independent Investment Consultant. **The OPEB trust, as of the end of last fiscal year had a net position of approximately $70 million.**

All OPEB Trust investments are made consistent with the investment policy based on target percentages established for each asset class. The Trust's risk tolerance is understood by the Plan Administrator such that achieving the Plan's investment objectives is not guaranteed and there will be time periods for which these objectives will not be met. The Plan Administrator also recognizes that some risk must be assumed to achieve the Trust's long-term investment objectives and accepts the inevitable fluctuations in returns that will occur. While it is understood that a certain level of risk is expected in the Trust's portfolio, the ability to withstand short and intermediate term variability was specifically considered in the development of the Investment Policy Statement risk tolerances. The OPEB Trust's investment policy places limitations on the concentration of investments in certain industries, with certain companies, and among asset classes and within investment policy ranges.

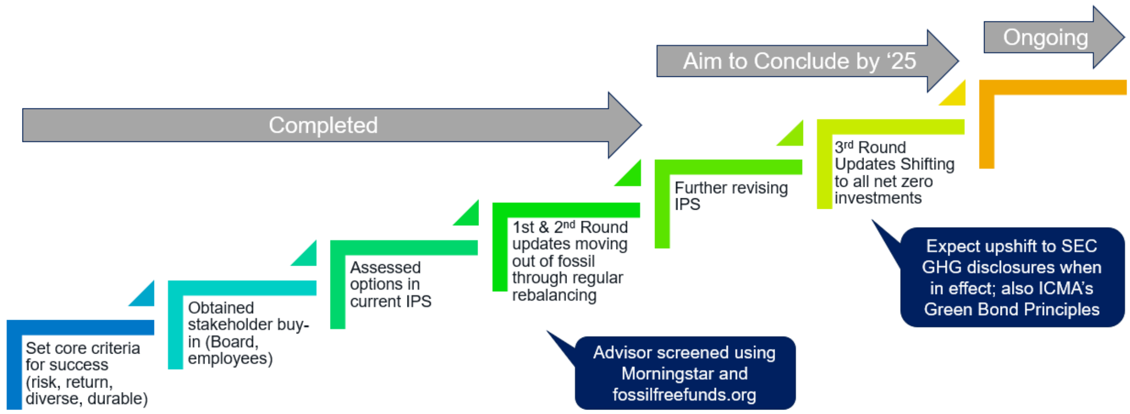
2. <u>Retirement Plans</u>

There are two retirement plans for NYSERDA employees: the New York State and Local Retirement System (the System), and the New York State Voluntary Defined Contribution Plan (VDC). Nearly all employees of NYSERDA participate in one of these two plans. As of the fiscal years ended March 31, 2022 and 2021, NYSERDA's proportionate share of the System's net pension liability was approximately 0.10% and 0.11%, respectively, determined based on the ratio of NYSERDA's total projected long-term contributions to the total System projected long-term contributions from all employers. As of the end of the last fiscal year, NYSERDA's share of the state System totaled a market value of approximately $292.1 million and NYSERDA's participant's share of the VDC market value was $6.8 million.

Pursuant to Public Authorities Law Section 1859(1), the Commissioner of the New York State Department of Taxation and Finance (Fiscal Agent) serves as fiscal agent for NYSERDA's cash and investments, maintaining such funds on NYSERDA's behalf and implementing investments subject to the Fiscal Agent's policies and with direction and authorization from NYSERDA. NYSERDA has a written investment policy that applies to all of its investments. The policy permits deposits with financial institutions approved by the Fiscal Agent and permits investments in certificates of deposit of bank or trust companies located in New York State, obligations of New York State and the United States government and certain of their agencies, repurchase agreements subject to certain limitations, and money market funds subject to certain limitations.

Strategy for Evolving Portfolio Construction and Supporting Short and Long Term Milestones, Metrics, and Targets

Focusing specifically on the long-term investment portfolio highlighted on the cover page, NYSERDA has shifted its investment portfolio out of fossil-fuel investments to date through a stepped process outlined below. These shifts have primarily leveraged regular periodic reviews and refreshes of investment policy statements (IPS) that guide the investment fund evaluation and selection process, followed by regular rebalancing of the portfolio to ensure alignment with target asset allocation ranges for different classes of investments as noted in the IPS.



Items Completed

The 2018 State of the State proposals included "a plan for divesting the New York State Common Retirement Fund from significant fossil fuel investments" guided by Comptroller Thomas DiNapoli and an advisory panel via a de-carbonization roadmap for the Common Retirement Fund to invest in opportunities to combat climate change and support the clean tech economy while assessing financial risks and protecting the Fund. Catalyzed by this action, NYSERDA began to investigate options to update its investment portfolio to reduce direct and indirect investment in companies in the fossil fuel industry.

NYSERDA's OPEB Plan Administrators worked with legal resources, its existing investment advisor, and internal staff to identify core criteria for success as shown above. NYSERDA then socialized a vision for updates to its investment portfolio, working closely with key stakeholders. Members of the Board's Audit and Finance Committee were requested to help oversee a review of the Authority's current Investment Policy Statement (IPS), with NYSERDA's then-Treasurer coordinating between the Board and an outside investment advisor to propose updates to that IPS. The purpose of those updates was to better reflect the risk-reducing value of additional diversification and expanded consideration of funds with very low or no investment in fossil fuel intensive businesses.

In March of 2018, NYSERDA board members adopted a resolution approving modifications to the IPS for the NYSERDA OPEB Trust, including changes to revise the asset allocation policy to add provisions for selection of funds to include consideration of funds which minimize investments in the fossil fuel industry. In this update, investment criteria were stated so as to clarify that the Plan Administrator's selection of fund investments must always put the economic interests of the Plan first but may also consider alternative investment options that minimize investments in the fossil fuel industry, provided they generally meet similar performance and risk criteria to investments considered without regard to their fossil fuel interests.

This IPS change was made in recognition that climate change represents one of the biggest economic challenges in the 21st century, one that presents significant risks and opportunities for investors. Fiduciary responsibilities require investors to analyze and understand risk exposure in a risk-constrained future. Consistent with changes being implemented by other prudent investors, and in recognition of investment products that were commercially available, management recommended that reasonably prudent strategies for investment of the Trust's assets may include a consideration of fossil fuel exposure of the funds considered for investment.

Items In Process

NYSERDA expects to continue to shift toward a fully zero-emissions portfolio primarily in three ways:

1. For the OPEB Trust, updating the criteria used to evaluate funds to incorporate climate risk reporting standards as discussed in the SEC's proposed Rules to Enhance and Standardize Climate-Related Disclosures for Investors. While it is our understanding that these rules focus primarily on climate risk and are not necessarily an optimal indicator of zero-emissions funds, we view them as a helpful complement to our overall approach to prudent evaluation of investment risks and anticipate that information from disclosures will feed into Morningstar or other ratings systems, and will update our fund evaluation sources accordingly.

2. Also for the OPEB Trust, we will be working with our investment advisor in the coming year to integrate company climate/emission ratings as reported by the Climate Disclosure Project as a component of our fund evaluation.

3. For employee retirement funds, raising employee awareness about options that may be available to them to direct their portfolios to investments most aligned with our state's intended transition to a zero-emissions future.

Frameworks or Tools to Evaluate Investments and Inform our Strategy

Our investment strategy is founded on compliance, risk/return, and ESG designations.

1. <u>Legal compliance.</u> As a fiduciary, the Plan Administrator's purpose is to put the Trust's economic interests first for the payment of benefits. A methodical process is a predicate for the prudent consideration of the substantive considerations of an investment. A fiduciary that carefully considers the relevant criteria, and meaningfully deliberates the proposed investment decision, indicates procedural prudence. Fiduciaries cannot make decisions in the abstract but must undertake a process that reflects methods customarily used by other fiduciaries, such as pulling the requisite data and relying upon experts as appropriate in making an informed investment decision.

   To that end, we reviewed the proposed investment policy changes and the criteria and methodology used to identify low/no fossil fuel investments by the Investment Consultant and Plan Administrators with outside counsel, and they, as set forth in a legal analysis, advised that the proposed IPS amendments and investment decisions can meet all applicable fiduciary requirements under ERISA. (ERISA does not strictly apply but NYSERDA carefully considers ERISA provisions as a matter of policy). That evaluation also factored in U.S Department of Labor guidance regarding environmental, social and governance (ESG) investment decision-making, and the common law of trusts.

2. <u>Risk and return.</u> ERISA's prudence test calls for investment evaluations to prioritize return for a given level of risk/cost. To that end, when identifying appropriate investments, several key metrics that NYSERDA determines in consultation with its investment advisor are utilized to assess potential risk and return. In its evaluation of funds, NYSERDA also aims to control risk through reasonable and rational diversification of the assets into various asset classes. Complementing traditional portfolio diversification techniques to reduce exposure to a particular sector, geographic region, or company type, recent global events and price swings add weight to the argument that fossil investments may be riskier than others, shifting the risk/return balance in favor of alternatives.

3. <u>ESG and Low-Carbon designations</u>. NYSERDA's investment advisory consultant identified several suitable funds for each asset class that would, in their professional opinion and consistent with their responsibility established in the IPS, be consistent with the goals and objectives of the current IPS, without regard to whether the fund has fossil fuel related investments. Then, the investment consultant then identified a fund for each asset class with low fossil fuel exposure, using Morningstar's Low Carbon Designation™ or funds with Morningstar Portfolio Fossil Fuel Involvement™ of 0%, using Milliman's Fund Rating Reports or Morningstar ratings. The investment consultant identified and recommended funds which minimize investments in the fossil-fuel industry, providing that they generally meet performance and risk criteria where available and are appropriate low-carbon funds providing similar or better performance and risk ratings as the portfolio identified above.

Approach to Engagement and Advocacy with Portfolio Entities

Because of the nature of our investment portfolios, our stakeholders consist primarily of our Board and employees. Given NYSERDA's work scope, those bodies are supportive of the focus on moving to net zero. They also naturally have equally important foci on the prudent use of funds and longer-term risk management, to ensure we stay well-positioned to support obligations to current and former employees. With those dual themes in mind, we have focused on proactive outreach to gather perspectives before recommending changes in investment approach, and ensured that all our analysis is grounded in the regulatory underpinning of fiscal prudence, highlighting how a portfolio shift toward net zero is expected to maintain or improve returns relative to a given risk level.

From a procedural standpoint, we provide regular updates to the Audit and Finance Committee as well as the full Board on no less than an annual basis, through regular reports and verbal updates at Board meetings. The Audit and Finance Committee in particular serves as an essential sounding board; providing them draft plans and specific questions for their comment have been helpful techniques to elicit productive feedback and support. In these discussions, we have leveraged market benchmarks and direct input from both outside legal counsel and our investment advisor to build credibility.

To educate employees, we leverage annual benefits enrollment windows to provide education about the State's commitment to net zero investments and how we are working to support that. We also use regular employee newsletters to highlight available information about the System and the VDC, so that where options exist for employee and retiree choice of investment funds they are well apprised of how to identify those that better support emissions reduction.
Our communications strategy with employees includes acknowledging the concerns employees may have and addressing those head on to reassure them that our focus remains on risk and return, and we leverage success stories to build confidence.

Governance and Oversight

NYSERDA investments in the context of this plan consist of retirement and long-term health care benefit plans. On the former, we are a participating employer of the NYSLRS and follow the requirements of that plan. On the latter, the investments are overseen primarily by the Audit and Finance Committee of our Board, supported by the Chief Financial Officer and the Finance and Accounting team. NYSERDA is subject to the provisions of Public Authorities Law Section 2925, the Office of the State Comptroller's "Investment Guidelines for Public Authorities," the provisions of NYSERDA's enabling legislation concerning NYSERDA investments, and NYSERDA's own "Investment Guidelines, Operative Policy and Instructions." At least annually, the Audit and Finance Committee of NYSERDA's Board reviews and evaluates NYSERDA's investment program results and approves any revisions to the Guidelines.

Internal Zero-Emission Investments Team

Rather than assemble a separate team to advance our efforts in this area, we are intentionally weaving our focus on zero-emissions into ongoing activities. The table below reflects the primary teams engaged - not just in the long-term investments, but our focus on moving to zero emission business practices across the board - and some key metrics we will be tracking and working to improve over time. Of note, the zero-emission goal is being embedded not just in Finance team goals, but is also being incorporated into the individual goals set for the managers of each of these areas, to foster both accountability and achievement recognition.

Team	Role	Draft Metrics
Finance	Work with Board, Audit and Finance Committee, and investment advisor to continue to refine and update ratings systems to evaluate investments, ensuring the IPS statement is reviewed at least annually and, as needed, updated for emerging guidance regarding identification of funds that align with both risk/return plan objectives and support progress toward emission-free goals.	% of OPEB Trust portfolio invested in funds of entities that are emission free or making demonstrable, verified progress on a timeline consistent with NYS goals.
Green Bank	Support NYSERDA's efforts to migrate working capital over time to options that support a shift to emissions-free operations.	Working capital metrics TBD by 2025.
Human Resources	Educate employees regarding retirement fund plan options.	Number of employees attending annual information sessions.
Contracts	Integrate sustainability and emissions considerations into RFI's, RFP's, and contract terms and conditions.	Tentative: % w/verifiable net zero pledges
Facilities and Fleet	Ensure compliance with all executive orders pertaining to buildings and fleet. Update HVAC systems as soon as practically possible to electrify heating and continue to improve efficiency and environmentally sustainable practices.	% Building Systems on Electric % EV's
Sustainability Coordinator	Coordinate with departmental representatives across the organization to ensure alignment with state guidance regarding sustainability and shift to emissions-free solutions.	TBD pending potential new executive orders regarding government sustainability practices; currently guided by EO4

In sum, we have:

- Completed initial steps successfully to move out of fossil fuel investments based on existing ratings systems.
- Through a recent RFP, worked to identify and select investment advisors skilled in the area of ESG funds identification and evaluation, with plans to further revise our IPS within the next year and rebalance to it.
- Identified additional data sources to incorporate into our fund evaluations for improved understanding of emissions profile and climate risk.
- Mapped out a transition timeline.
- Identified internal point people accountable to advance the next phases of our plan.

Complementing the investment portfolio as defined in the context of this plan, we continue to advance also on the three other fronts of our net zero journey – capital investments, program spend, and working capital – aligning all with state guidance and wherever possible leveraging emerging evaluation criteria. The overall timeline on all four fronts we are pursuing is shown below, and we are happy to provide additional details as requested.