



**TOWN OF LOS GATOS
FINANCE COMMITTEE REPORT**

MEETING DATE: 10/09/2017

ITEM NO: 2

DATE: OCTOBER 3, 2017

TO: COUNCIL FINANCE COMMITTEE

FROM: LAUREL PREVETTI, TOWN MANAGER

SUBJECT: REVIEW, DISCUSS, AND RECOMMEND THE TOWN COUNCIL ADOPT AN OVERSIGHT COMMITTEE, INVESTMENT POLICY AND ASSET ALLOCATION FOR THE TOWN OF LOS GATOS IRS SECTION 115 PENSION TRUST AND CALIFORNIA EMPLOYERS' RETIREE BENEFIT TRUST (CERBT)

RECOMMENDATION:

Staff recommends that the Council Finance Committee recommend to the Town Council:

1. Establishing the Town Council as the Oversight Committee for the Town of Los Gatos IRS Section 115 Pension Trust ("115 Pension Trust") and California Employers' Retiree Benefit Trust (CERBT);
2. Adopting an Investment Policy for the Town of Los Gatos IRS Section 115 Pension Trust and California Employers' Retiree Benefit Trust (CERBT);
3. Approving staff recommended asset allocations for both the Town of Los Gatos IRS Section 115 Pension Trust and California Employers' Retiree Benefit Trust (CERBT); and
4. Adopting the Investment Guidelines Document between the Town of Los Gatos and Highmark Capital Management

BACKGROUND:

Pursuant to Council direction, the Town issued a Request for Proposal in April 2017 for IRS Section 115 Pension Trust Services. On August 15, 2017, Town Council approved Public Agency Retirement Services (PARS) as the administrator of the Town's Section 115 Pension Trust. In addition, Town Council appointed the Town Manager/Director of Finance as the Town's Plan Administrator in order to execute legal and administrative documents and other actions

**PREPARED BY: STEPHEN CONWAY
 FINANCE DIRECTOR**

Reviewed by: Town Manager, Assistant Town Manager, and Town Attorney

PAGE 2 OF 8

SUBJECT: REVIEW AND DISCUSS OVERSIGHT BOARD, INVESTMENT POLICY AND ASSET ALLOCATION

DATE: OCTOBER 9, 2017

BACKGROUND (Cont'd):

necessary to initiate and maintain the Town's participation in the Public Agencies Post-Employment Benefits Trust.

The 115 Pension Trust acts as an additional investment vehicle for the overall funding of pension liabilities associated with the Town's Miscellaneous and Safety Pension Plans (the "Pension Plans"). In addition, in 2009, the Council approved participating in the California Employer's Retiree Benefit Trust (CERBT) Fund. The CERBT Fund is a Section 115 trust fund dedicated to the prefunding of other post-employment benefits ("OPEB"). The CERBT is the single investment vehicle for the Town's OPEB Plan ("OPEB Plan").

With the adoption of the 115 Pension Trust, it is now appropriate to establish the requisite governance and oversight controls reflective of the fiduciary responsibilities inherent in the management of pension and OPEB assets. Both Highmark Capital Management and the California Employers' Retiree Benefit Trust (CERBT) provide multiple options for investment of the Town's pension and healthcare assets. The differing investment options provided by the firms represent varying degrees of investment risk/return profiles. As such, staff recommends the establishment of an Oversight Committee and Investment Policy for the management of both the Town of Los Gatos IRS Section 115 Trust and California Employers' Retiree Benefit Trust (CERBT).

DISCUSSION:

The following discussion will follow the sequence of recommendations listed above:

Oversight Committee

The approval of PARS as the administrator of the Town's Section 115 Pension Trust established the operational structure necessary for the administration of pension assets. This structure includes PARS as the Trust Administrator with responsibilities for recordkeeping, reporting, servicing, compliance monitoring, and general program coordination. In addition, U.S. Bank serves as the Trustee and Custodian entrusted with a fiduciary role to safeguard the Town's assets. U.S. Bank has delegated the management of investments to Highmark Capital Management who provides active portfolio management for a series of portfolio options.

In addition, The CERBT trust initially provided a single investment vehicle similar to the CalPERS pension fund; however, the CERBT has since established three investment strategies with varying degrees of risk/return profiles. Given that CERBT maintains all the assets of the OPEB Plan and with the addition of multiple asset allocation strategies; the CERBT should be included in this governance structure. The Town Council as the governing body is responsible for the

PAGE 3 OF 8

SUBJECT: REVIEW AND DISCUSS OVERSIGHT BOARD, INVESTMENT POLICY AND ASSET ALLOCATION

DATE: OCTOBER 9, 2017

DISCUSSION (Cont'd):

overall oversight of the pension and OPEB assets. This oversight includes ensuring compliance with the following:

- Federal laws and regulations (primarily those administered by the Internal Revenue Service and the US Treasury Department)
- State and local laws and regulations
- Industry standards, such as those set forth for accounting, financial reporting, and actuarial valuations, and
- The Pension and OPEB Plans' own strategic plan; policies, rules, and procedures.

Of note, Article XVI of the California State Constitution covers public finance. Section 17 of this article provides for the provision of pensions by a retirement board, who is vested with the responsibility of administering pension funds. Among other actions, Article XVI, Section 17, stipulates that investment of moneys and administration of the system are subject to the following:

"The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to, participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. A retirement board's duty to its participants and their beneficiaries shall take precedence over any other duty."

"The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system."

"The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims."

"The members of the retirement board of a public pension or retirement system shall diversify the investments of the system so as to minimize the risk of loss and maximize the rate of return, unless under the circumstances it is clearly not prudent to do so."

PAGE 4 OF 8

SUBJECT: REVIEW AND DISCUSS OVERSIGHT BOARD, INVESTMENT POLICY AND ASSET ALLOCATION

DATE: OCTOBER 9, 2017

DISCUSSION (Cont'd):

In addition to ensuring regulatory compliance, the Government Finance Officers Association opines that pension plan trustees and administrators carry out four primary functions in oversight of the investment process:

- Adopt an IRS 115 Pension Trust and OPEB Trust Assets Investment Policy
- Develop an asset allocation plan
- Assemble an investment team
- Monitor the investment program's implementation and performance

The establishment of a separate 115 Pension Trust and OPEB Trust Oversight Committee comprised of the entire Council will ensure that the oversight of pension and healthcare assets receives the requisite attention commensurate with the fiduciary responsibility as stated in a draft Investment Policy for the Trusts' Assets (Attachment 1). Additional training will be provided to the Council to prepare it for these responsibilities. The Finance Committee would retain its role as advisory to the Town Council/Trusts Oversight Committee.

IRS 115 Pension Trust and OPEB Trust Assets Investment Policy

The Government Finance Officers Association (GFOA) recommends that state and local entities establish a formal IRS 115 Pension Trust and OPEB Trust Assets Investment Policy that is approved by the governing board of the Pension and OPEB Plans (Attachment 1). This Investment Policy would govern the investments for the Town of Los Gatos IRS Section 115 Pension Trust and California Employers' Retiree Benefit Trust (CERBT). The purpose of the Investment Policy is to provide a framework for the management of the 115 trust assets. GFOA recommends that an investment policy contain the following elements:

- Statement of purpose – This section would articulate the rationale for the policy as well as the investment goals and objectives.
- Roles and Responsibilities – This section documents accountability for all stages of Investment Policy development and implementation.
- Standard of care – This section identifies the standard of prudence that the decision makers are expected to meet in carrying out their investment responsibilities.
- Asset Allocation – This section would summarize the long-term asset allocation strategy of the plan.
- Reporting and monitoring – This section will describe the frequency and manner in which external and internal parties report investment results.

DISCUSSION (Cont'd):

In addition to the GFOA suggested elements; the Certified Financial Analyst (CFA) Institute identifies the following elements of the Investment Policy:

- Scope and Purpose
- Governance
- Investment, return, and risk objectives
- Risk Management

Section 115 Pension and OPEB Trusts' Asset Allocations

The ultimate goal of a defined benefit (DB) plan is to provide retirement benefits to retirees. Historically, approximately two-thirds of pension assets are derived from investment earnings. In addition, research consistently shows that about 90% of the variation in portfolio returns is attributable to strategic asset allocation. The Town's Pension and OPEB Trusts were initially established with the following objectives in mind:

- Assets placed in the trusts remain controlled by the Town.
- The Trusts provide a mechanism for the Town to fund its pension and OPEB liabilities, as an additional way to reduce the amount of the Town's unfunded liabilities.
- The 115 Pension Trust can be "pre-funded" at a lower discount rate should there be flexibility in revenues available in the operating budget or with some portion of available year-end savings.
- Earnings in the 115 Pension Trust in the long term will very likely exceed the returns made on the Town's general portfolio because of a wider range of available investment choices and fewer restrictions such as the ability to invest in equities (stocks).
- 115 Pension Trust earnings can be used in future years to pay for increased pension costs as potential augmentation to the Town's operating budget revenues.
- The 115 Pension Trust provides a funding vehicle to accumulate assets that can be used in the future to pay down the unfunded pension liabilities in a variety of ways, including lump sum payments made to CalPERS to identified actuarial bases, or to make additional payments to CalPERS in each fiscal year cycle assuming a lower discount rate assumption of ongoing annual returns.
- Assets placed in the 115 Pension Trust can be invested strategically at a level of risk that provides a hedge against market downturns and volatility experienced by the fairly aggressive asset allocation utilized for the CalPERS portfolio.

SUBJECT: REVIEW AND DISCUSS OVERSIGHT BOARD, INVESTMENT POLICY AND ASSET ALLOCATION

DATE: OCTOBER 9, 2017

DISCUSSION (Cont'd):

115 Pension Trust: Highmark Capital Management currently provides the 115 Pension Trust with five different asset allocation options. Each asset allocation has varying degrees of exposure to equity, fixed income, and cash. The five asset allocations are intended to provide the Pension Plans with five distinct risk/reward profiles. The following are the asset allocations:

	Conservative	Moderately Conservative	Moderate	Balanced	Capital Appreciation
Equity	15%	30%	50%	60%	75%
Fixed Income	80%	65%	45%	35%	20%
Cash	5%	5%	5%	5%	5%
Expected Return	4.95%	5.68%	6.48%	6.85%	7.39%
Expected Standard Deviation	4.13%	5.26%	7.54%	8.84%	10.9%

OPEB Trust: The CalPERS managed CERBT provides three distinct asset allocations. Each asset allocation has varying degrees of exposure to equity, fixed income, TIPs, REITs, and commodities. Similar to Highmark each asset allocation provides different risk/return profiles. Currently the OPEB Plan is invested in Strategy 1. Following are the asset allocations:

	Strategy 1 Less conservative	Strategy 2 Balanced	Strategy 3 More Conservative
Equity	57%	40%	24%
Fixed Income	27%	39%	39%
TIPs	5%	10%	26%
REITs	8%	8%	8%
Commodities	3%	3%	3%
5 Year Return (net)	7.8%	6.4%	4.9%

Given the aforementioned prudent fiduciary principles, diversification mandate, uncertainty of timing of withdrawals, and recognizing that one of the primary goals of the 115 Pension Trust is to provide a steadily increasing level of funds, staff recommends choosing an asset allocation that maintains a relatively more conservative level of risk at this time. In the case of Highmark Capital Management, staff recommends the PARS Moderately Conservative allocation. For the

PAGE 7 OF 8

SUBJECT: REVIEW AND DISCUSS OVERSIGHT BOARD, INVESTMENT POLICY AND ASSET ALLOCATION

DATE: OCTOBER 9, 2017

CERBT asset allocation, staff recommends maintaining Strategy 1 due to the anticipated longer time horizon prior to any withdrawals. It should be noted that the expected return for

DISCUSSION (Cont'd):

PARS Moderately Conservative portfolio and the 5 year net return for CERBT Strategy 1 both exceed the return of the operating portfolio. In addition, staff believes that the recommended asset allocations are prudent pending an actuarial review by the Town's contracted actuary. A holistic review of the Town's existing and future pension and OPEB responsibilities will help inform the Committee and the Council as to: the maturity stage, future growth estimates, projected level of benefit payments, etc. A better understanding of the liabilities associated with the Town's future pension and OPEB obligations may dictate appropriate levels of risk and return for plan assets.

Highmark Capital Management Investment Guidelines Document (115 Pension Trust)

As part of Highmark Capital Managements fiduciary role, it has provided the Town with an Investment Guidelines Document (IGD) which establishes the Investment Policy between Highmark and the Town. Similar to the draft Investment Policy for the Trusts, it is prudent to have a formal documented investment understanding between the Town and our Investment Manager. The purpose of the IDG is to:

- Reflect the 115 Pension Trust goals including which investment allocation strategy best aligns with the Town's approved Investment Policy for the Trusts.
- Facilitate the process of ongoing communication between the Plan Sponsor (Town Council) and its plan fiduciaries (Union Bank as trustee, PARS acting as Administrator, and Highmark Capital Management as a designated investment manager).
- Confirm the 115 Pension Trust's investment goals and objectives and investment management policies applicable to the investment portfolio identified below and obtained from the Town.
- Provide a framework to construct a well-diversified asset mix that can potentially be expected to meet the 115 Pension Trust's short- and long-term needs that is consistent with the overall Pension Plan's investment objectives, liquidity considerations and risk tolerance.
- Identify any unique considerations that may restrict or limit the investment discretion of its designated investment managers.
- Help maintain a long-term perspective when market volatility is caused by short-term market movements.

PAGE 8 OF 8

SUBJECT: REVIEW AND DISCUSS OVERSIGHT BOARD, INVESTMENT POLICY AND ASSET ALLOCATION

DATE: OCTOBER 9, 2017

Staff has provided a sample IDF as Attachment 2 of this report which provides sample details of the investment policy and procedures and assumes the recommendation of the Moderately Conservative. Staff has reviewed the document and concurs with the Moderately Conservative

DISCUSSION (Cont'd):

recommendation with modest revisions, including more specificity regarding investment discretion. If this is also the recommendation of the Finance Committee, then this IDF will be prepared for Council consideration.

CONCLUSION AND STAFF RECOMMENDATION:

Staff recommends that the Council Finance Committee recommend to the Town Council:

1. Establishing the Town Council as the Oversight Committee for the Town of Los Gatos IRS Section 115 Pension Trust and California Employers' Retiree Benefit Trust (CERBT);
2. Adopting an Investment Policy for the Town of Los Gatos IRS Section 115 Pension Trust and California Employers' Retiree Benefit Trust (CERBT);
3. Approving staff recommended asset allocations for both the Town of Los Gatos IRS Section 115 Pension Trust and California Employers' Retiree Benefit Trust (CERBT); and
4. Adopting the Investment Guidelines Document between the Town of Los Gatos and Highmark Capital Management for the 115 Pension Trust.

Attachments:

1. Draft IRS 115 Pension and OPEB Trust Assets Investment Policy
2. Highmark Investment Guidelines Document

Draft
Town of Los Gatos IRS Section 115 Pension Trust and
California Employers' Retiree Benefit Trust (CERBT)
Investment Policy

Purpose

The Town of Los Gatos (the "Town") has established the Town of Los Gatos IRS Section 115 Pension Trust (the "115 Pension Trust") and the California Employers' Retiree Benefit Trust (the "CERBT"), collectively the "115 Trusts", in order to provide for funding of pension, retiree health and other post-employment benefits for the City's eligible retirees. The 115 Pension Trust acts as an additional investment vehicle for the overall funding of pension liabilities associated with the Town's Miscellaneous and Safety Pension Plans (the "Pension Plans"). The CERBT is the single investment vehicle for the Town's OPEB Plan ("OPEB Plan"). The Town has established the 115 Trusts Oversight Committee (the "Oversight Committee") to oversee the assets of the 115 Trusts and to perform the duties and responsibilities set forth in this Investment Policy (IP).

Composition

The membership of the Oversight Committee is composed of the entire Town Council.

Fiduciary Duties and Responsibilities

The Oversight Committee has the following fiduciary duties and responsibilities:

1. The Oversight Committee has exclusive control of the investments of the 115 Trusts. The Oversight Committee will manage the funds under the Trusts:
 - a) solely in the interest of, and for the exclusive purposes of providing for funding of benefits for participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the Trusts;
 - b) with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims; and
 - c) by diversifying the investments of the Trusts so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly prudent not to do so.

2. The work of the Oversight Committee shall be consistent with a written statement of Investment Policy (i.e., this Investment Policy for the Trusts). At least once every three years, the Oversight Committee will evaluate the appropriateness of the Investment Policy and, based on such evaluation, either confirm the tenets of the Investment Policy as then in effect, or amend the 115 Trusts Investment Policy as appropriate. The Investment Policy must include the following:
 - a) document investment objectives, performance expectations and investment guidelines for assets under the Trusts;
 - b) establish an appropriate investment strategy for managing all assets under the Trusts, including an investment time horizon, risk tolerance ranges and asset allocation to provide sufficient diversification and overall return over the long-term time horizon of the Trusts; and
 - d) establish periodic performance reporting requirements that will effectively monitor investment results and ensure that the investment policy is being followed.

Investment Objectives

1. The primary objective of the 115 Trusts investment portfolios is to satisfy the Pension Plans and OPEB Plan obligations to pay benefits to members and their beneficiaries. To do so, the 115 Trusts will seek to achieve long-term net returns in excess of the actuarial investment return assumption while maintaining a reasonable level of investment risk.
2. The funds will be managed as an ongoing concern with a long-term investment horizon, consistent with demographic profile of the members and beneficiaries of the plans.
3. A range of risks will be managed in connection with the trusts, with an emphasis on the following:
 - a) The impact of the investment decisions on the funded status of the plans and the resulting volatility of contributions.
 - b) Risk of loss of plan assets.
4. In determining the investment strategies of the 115 Trusts, various factors will be considered including, but not limited to:
 - a) The structure and duration of the Pension Plans and OPEB Plan liabilities.
 - b) Modern Portfolio Theory.

c) The liquidity needs of Pension Plans and OPEB Plan.

Investment Strategy/Asset Allocation

The Oversight Committee has delegated the investment management function to third parties. These third parties offer multiple asset allocation options with varying degrees of risk return profiles. The Oversight Committee will select the asset allocation which best aligns with the aforementioned fiduciary standards and investment objectives.

The Oversight Committee will review the selected asset allocations annually. However, the Oversight Committee can review the current asset allocation selections at any time in light of market conditions.

Monitoring and Reporting

The Oversight Committee will do all of the following:

1. Monitor the 115 Trusts investment managers on an ongoing basis and may be terminated by Oversight Committee at any time due to performance or other developments that call into question the investment manager's ability to continue to effectively manage assets of the 115 Trusts.
2. Review and assess the performance of any Investment Manager(s) appointed by the Oversight Committee to perform services related to the Trusts quarterly.
3. Measure and evaluate the quarterly performance of investment managers relative to appropriate long-term performance benchmark.
4. Review the actuarial evaluations annually.
5. Monitor compliance with this Investment Policy for the Trusts.



Investment Guidelines Document

Town of Los Gatos

Employee Benefits Fund Pension Plan

September 2017

Investment Guidelines Document

Scope and Purpose

The purpose of this Investment Guidelines Document is to:

- Facilitate the process of ongoing communication between the Plan Sponsor and its plan fiduciaries;
- Confirm the Plan's investment goals and objectives and management policies applicable to the investment portfolio identified below and obtained from the Plan Sponsor;
- Provide a framework to construct a well-diversified asset mix that can potentially be expected to meet the account's short- and long-term needs that is consistent with the account's investment objectives, liquidity considerations and risk tolerance;
- Identify any unique considerations that may restrict or limit the investment discretion of its designated investment managers;
- Help maintain a long-term perspective when market volatility is caused by short-term market movements.

Key Plan Sponsor Account Information as of September 2017

Plan Sponsor:	Town of Los Gatos
Governance:	City Council for the Town of Los Gatos
Plan Name ("Plan"):	Town of Los Gatos Employee Benefit Fund Pension Plan
Trustee:	US Bank Contact: Susan Hughes, 949-224-7209 susan.hughes@usbank.com
Type of Account:	Pension Plan
ERISA Status:	Not subject to ERISA
Investment Manager:	US Bank, as discretionary trustee, has delegated investment management responsibilities to HighMark Capital Management, Inc. ("Investment Manager"), an SEC-registered investment adviser Contact: Andrew Brown, CFA, 415-705-7605 Andrew.Brown@highmarkcapital.com

Investment Authority: Except as otherwise noted, the Trustee, US Bank, has delegated investment authority to HighMark Capital Management, an SEC-registered investment adviser. Investment Manager has full investment discretion over the managed assets in the account. Investment Manager is authorized to purchase, sell, exchange, invest, reinvest and manage the designated assets held in the account, all in accordance with account's investment objectives, without prior approval or subsequent approval of any other party(ies).

Investment Objectives and Constraints

The goal of the Plan's investment program is to provide a reasonable level of growth which, will result in sufficient assets to pay the present and future obligations of the Plan. The following objectives are intended to assist in achieving this goal:

- The Plan should seek to earn a return in excess of its policy benchmark over the life of the Plan.
- The Plan's assets will be managed on a total return basis which takes into consideration both investment income and capital appreciation. While the Plan Sponsor recognizes the importance of preservation of capital, it also adheres to the principle that varying degrees of investment risk are generally rewarded with compensating returns. To achieve these objectives, the Plan Sponsor allocates its assets (asset allocation) with a strategic perspective of the capital markets.

Investment Time Horizon: Intermediate-Term 5 - 7 years

Anticipated Cash Flows: Assets in the Plan will seek to mitigate the impact of future rate increases from Calpers. It is not anticipated that the Plan will see a high level of disbursements in the first five years of the Plan. However, situations may arise, leading to a disbursement in assets to the Calpers Trust.

Investment Objective: The primary objective is to generate a reasonable level of growth. The assets in this Plan will eventually be used to fund Pension Plan obligations for assets managed in the Calpers Trust.

Risk Tolerance: *Moderately Conservative*
The account's risk tolerance has been rated moderately conservative, which demonstrates that the account can accept modest price fluctuations to pursue its investment objectives.

Strategic Asset Allocation: The asset allocation ranges for this objective are listed below:

<i>Strategic Asset Allocation Ranges</i>		
Cash	Fixed Income	Equity
0-20%	50%-80%	20%-40%
Policy: 5%	Policy: 65%	Policy: 30%

Market conditions may cause the account's asset allocation to vary from the stated range from time to time. The Investment Manager will rebalance the portfolio no less than quarterly and/or when the actual weighting differs substantially from the strategic range, if appropriate and consistent with your objectives.

Security Guidelines:

Equities

With the exception of limitations and constraints described above, Investment Manager may allocate assets of the equity portion of the account among various market capitalizations (large, mid, small) and investment styles (value, growth). Further, Investment Manager may allocate assets among domestic, international developed and emerging market equity securities.

Total Equities	20%-40%
<i>Equity Style</i>	<i>Range</i>
Domestic Large Cap Equity	10%-30%
Domestic Mid Cap Equity	0%-10%
Domestic Small Cap Equity	0%-12%
International Equity (incl. Emerging Markets)	0%-12%
Real Estate Investment Trust (REIT)	0%-8%

Fixed Income

In the fixed income portion of the account, Investment Manager may allocate assets among various sectors and industries, as well as varying maturities and credit quality that are consistent with the overall goals and objectives of the portfolio.

Total Fixed Income	50%-80%
<i>Fixed Income Style</i>	<i>Range</i>
Long-term bonds (maturities >7 years)	0%-30%
Intermediate-term bonds (maturities 3-7 years)	30%-80%
Short-Term bonds (maturities <3 years)	0%-25%
High Yield bonds	0%-6%

Performance Benchmarks:

The performance of the total Plan shall be measured over a three and five-year periods. These periods are considered sufficient to accommodate the market cycles experienced with investments. The performance shall be compared to the return of the total portfolio blended benchmark shown below.

Total Portfolio Blended Benchmark

- 15.50% S&P 500 Index
- 3.00% Russell Mid Cap Index
- 4.50% Russell 2000 Index
- 2.00% MSCI Emerging Markets Index
- 4.00% MSCI EAFE Index
- 1.00% Wilshire REIT Index
- 49.25% Bloomberg Barclays US Aggregate Index
- 14.00% ML 1-3 Year US Corp/Gov't Index
- 1.75% US High Yield Master II Index
- 5.00% Citi 1Mth T-Bill Index

Asset Class/Style Benchmarks

Over a market cycle, the long-term objective for each investment strategy is to add value to a market benchmark. The following are the benchmarks used to monitor each investment strategy:

Large Cap Equity	S&P 500 Index
Growth	S&P 500 Growth Index
Value	S&P 500 Value Index
Mid Cap Equity	Russell Mid Cap Index
Growth	Russell Mid Cap Growth Index
Value	Russell Mid Cap Value Index
Small Cap Equity	Russell 2000 Index
Growth	Russell 2000 Growth Index
Value	Russell 2000 Value Index
REITs	Wilshire REIT Index
International Equity	MSCI EAFE Index
Investment Grade Bonds	Bloomberg Barclays US Aggregate Index
High Yield	US High Yield Master II Index

Security Selection

Investment Manager may utilize a full range of investment vehicles when constructing the investment portfolio, including but not limited to individual securities, mutual funds, and exchange-traded funds. In addition, to the extent permissible, Investment Manager is authorized to invest in shares of mutual funds in which the Investment Manager serves as advisor or sub-adviser.

Investment Limitations:

The following investment transactions are prohibited:

- Direct investments in precious metals (precious metals mutual funds and exchange-traded funds are permissible).
- Venture Capital
- Short sales*
- Purchases of Letter Stock, Private Placements, or direct payments
- Leveraged Transactions*
- Commodities Transactions Puts, calls, straddles, or other option strategies*
- Purchases of real estate, with the exception of REITs
- Derivatives, with exception of ETFs*

**Permissible in diversified mutual funds and exchange-traded funds*

Duties and Responsibilities

Responsibilities of Plan Sponsor

The Plan Administrator and Finance Committee for the Town of Los Gatos is responsible for:

- Confirming the accuracy of this Investment Guidelines Document, in writing.
- Advising Trustee and Investment Manager of any change in the plan/account's financial situation, funding status, or cash flows, which could possibly necessitate a change to the account's overall risk tolerance, time horizon or liquidity requirements; and thus would dictate a change to the overall investment objective and goals for the account.
- Monitoring and supervising all service vendors and investment options, including investment managers.
- Avoiding prohibited transactions and conflicts of interest.

Responsibilities of Trustee

The plan Trustee is responsible for:

- Valuing the holdings.
- Collecting all income and dividends owed to the Plan.
- Settling all transactions (buy-sell orders).

Responsibilities of Investment Manager

The Investment Manager is responsible for:

- Assisting the Plan Administrator and Finance Committee for the Town of Los Gatos with the development and maintenance of this Investment Policy Guideline document.
- Meeting with Plan Administrator and Finance Committee for the Town of Los Gatos to review portfolio structure, holdings, and performance.
- Designing, recommending and implementing an appropriate asset allocation consistent with the investment objectives, time horizon, risk profile, guidelines and constraints outlined in this statement.
- Researching and monitoring investment advisers and investment vehicles.
- Purchasing, selling, and reinvesting in securities held in the account.
- Monitoring the performance of all selected assets.
- Voting proxies, if applicable.
- Recommending changes to any of the above.

- Periodically reviewing the suitability of the investments, being available to meet with the committee at least once each year, and being available at such other times within reason at your request.
- Preparing and presenting appropriate reports.
- Informing the committee if changes occur in personnel that are responsible for portfolio management or research.

Acknowledgement and Acceptance

I/We being the Plan Sponsor with responsibility for the account(s) held on behalf of the Plan Sponsor specified below, designate Investment Manager as having the investment discretion and management responsibility indicated in relation to all assets of the Plan or specified Account. If such designation is set forth in the Plan/trust, I/We hereby confirm such designation as Investment Manager.

I have read the Investment Guidelines Document, and confirm the accuracy of it, including the terms and conditions under which the assets in this account are to be held, managed, and disposed of by Investment Manager. This Investment Guidelines Document supersedes all previous versions of an Investment Guidelines Document or investment objective instructions that may have been executed for this account.

Plan Sponsor: **Town of Los Gatos**

Date: _____

Investment Manager: **Andrew Brown, CFA, Portfolio Manager, (415) 705-7605**

Date: _____





**TOWN OF LOS GATOS
FINANCE COMMITTEE REPORT**

MEETING DATE: 12/04/2017

ITEM NO: 3

DATE: NOVEMBER 28, 2017
TO: COUNCIL FINANCE COMMITTEE
FROM: LAUREL PREVETTI, TOWN MANAGER
SUBJECT: REVIEW, DISCUSS, AND RECOMMEND TO THE PENSION AND OTHER POST EMPLOYMENT BENEFIT (OPEB) OVERSIGHT COMMITTEE TO:
A. ADOPT AN ASSET ALLOCATION FOR THE TOWN OF LOS GATOS IRS SECTION 115 PENSION TRUST
B. EXPENDITURE BUDGET ADJUSTMENT FROM AVAILABLE CALIFORNIA PUBLIC EMPLOYEES RETIREMENT SYSTEM (CALPERS)/OPEB FUND BALANCE TO DEPOSIT TO THE IRS SECTION 115 PENSION TRUST

RECOMMENDATION:

Staff recommends that the Council Finance Committee review, discuss, and recommend to the Pension and OPEB Oversight Committee to:

1. Adopt an asset allocation for the Town of Los Gatos IRS Section 115 Pension Trust
2. Recommend a \$3,388,913 expenditure budget adjustment from available CalPERS/OPEB fund balance to deposit to the IRS Section 115 Pension Trust.

BACKGROUND:

On August 15, 2017, Town Council approved Public Agency Retirement Services (PARS) as the administrator of the Town's Section 115 Pension Trust. The 115 Pension Trust acts as an additional investment vehicle for the overall funding of pension liabilities associated with the Town's Miscellaneous and Safety Pension Plans (the "Pension Plans"). The 115 Pension Trust provides the Town with flexibility in a variety of ways, including making lump sum payments directly to CalPERS and augmenting budget stability by using trust assets to defray pension costs in future years. In addition, the 115 Pension Trust can be utilized to either mimic or alter the risk/reward profile of assets currently invested with CalPERS.

PREPARED BY: STEPHEN CONWAY
FINANCE DIRECTOR

Reviewed by: Town Manager, Assistant Town Manager, and Town Attorney

SUBJECT: REVIEW AND DISCUSS OVERSIGHT BOARD ASSET ALLOCATION AND FUNDING LEVEL

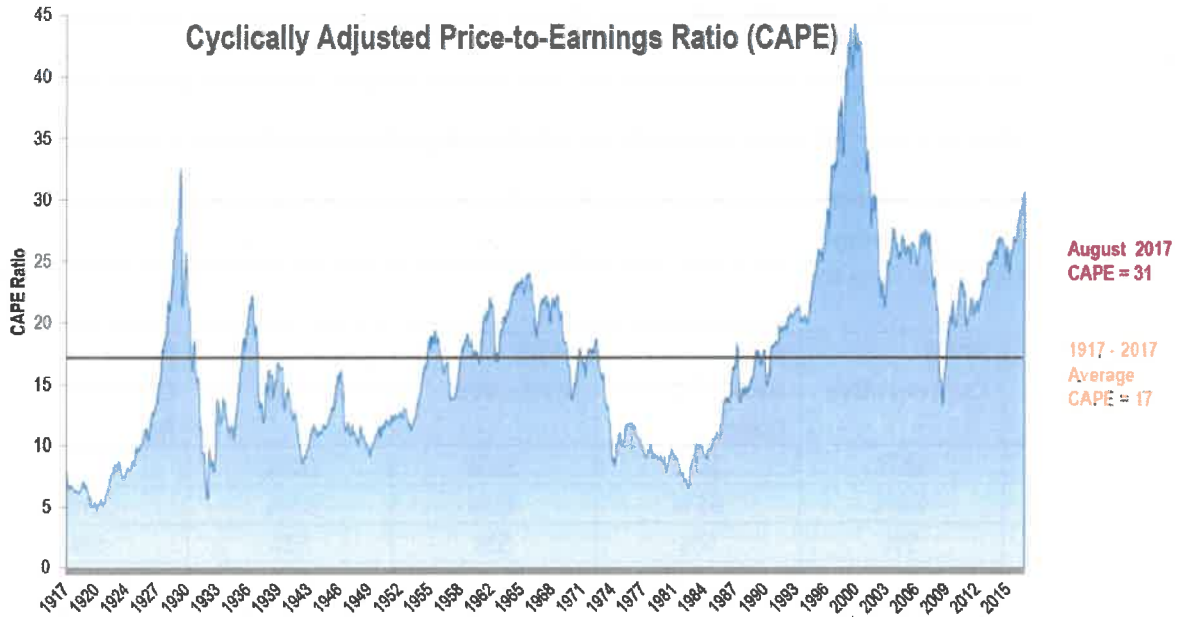
DATE: NOVEMBER 28, 2017

On October 9, 2017, the Finance Committee deliberated staff's recommendation to invest in the PARS Moderately Conservative allocation. Staff's recommendation was based on maintaining more diversification from existing equity exposures and the uncertainty of timing of future withdrawals from the Trust. The Committee opted not to accept staff's recommendation at the time and requested additional information regarding the current asset allocation with CalPERS, the costs associated with each PARS asset allocation, and the total amount of monies to be invested.

DISCUSSION:*CalPERS Asset Allocation*

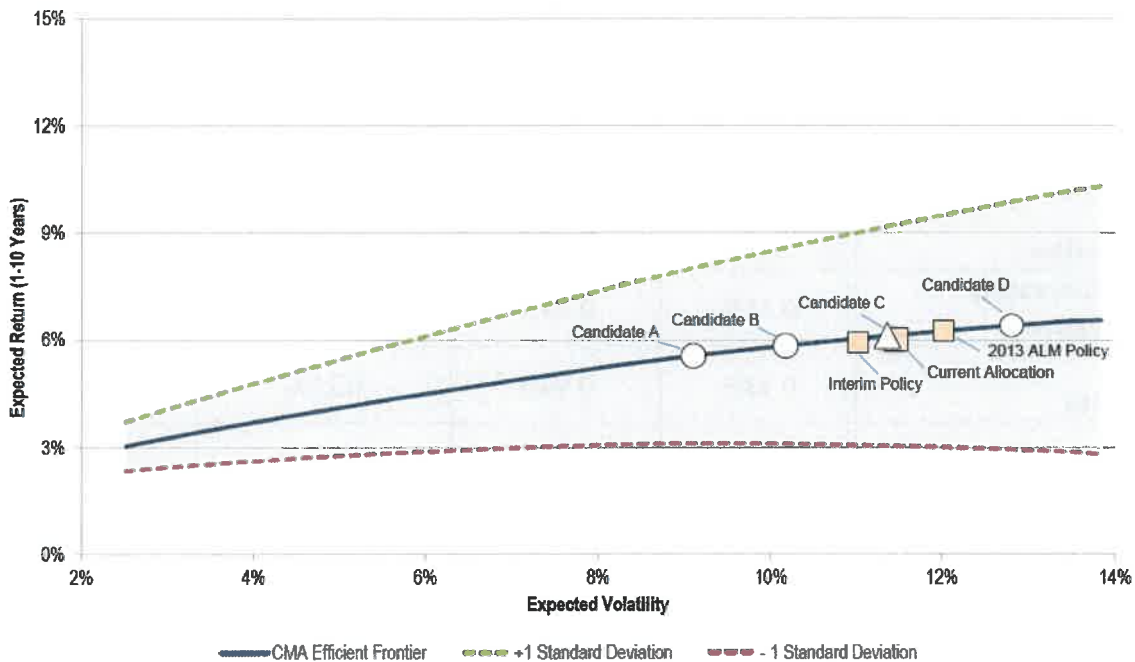
On October 13, 2017, staff attended the CalPERS 2017 Asset Liability Management (ALM) Workshop. During the workshop CalPERS Investment staff presented information regarding the current construct of the Public Employees' Retirement Fund (PERF) and updated expected returns. In addition the workshop presented four alternative asset allocation portfolios and the expected return/risks associated with those portfolios. The expected portfolio returns were illustrated in 1-10 year returns, 11-60 year returns, and a blended 1-60 year return. As the table below illustrates, CalPERS staff believes the expected returns for the next decade will be below the currently assumed rate of return of 7.0%. CalPERS staff partially attributes the lower short term (1-10 year) expected return on market valuations being currently high relative to historical standards. Historically, approximately two-thirds of pension assets are derived from investment earnings. In addition, research consistently shows that about 90% of the variation in portfolio returns is attributable to strategic asset allocation.

Asset Allocation of Preliminary Candidate Portfolios					Allocation 9/30/2017	Interim Policy 9/30/2016	ALM Policy 2013
Asset Class Component	Candidate A ○	Candidate B ○	Candidate C △	Candidate D ○	□	□	□
Global Equity	34%	42%	50%	59%	50%	48%	47%
Private Equity	8%	8%	8%	8%	8%	8%	12%
Fixed Income	44%	36%	28%	19%	19%	20%	19%
Real Assets	13%	13%	13%	13%	-	-	-
Real Estate	-	-	-	-	9%	11%	11%
Infrastructure/Forestland	-	-	-	-	2%	2%	3%
Inflation Assets	0%	0%	0%	0%	8%	9%	6%
Liquidity	1%	1%	1%	1%	4%	4%	2%
Expected Compound Return (1-10 yrs.)	5.6%	5.8%	6.1%	6.4%	6.0%	5.9%	6.2%
Long Term Expected Return (11-60 yrs.)	7.8%	8.0%	8.3%	8.5%	8.1%	8.0%	8.3%
Blended Return (1-60 yrs.)	6.50%	6.75%	7.00%	7.25%	6.85%	6.77%	7.09%
Expected Volatility	9.1%	10.2%	11.4%	12.8%	11.5%	11.0%	12.0%
Cash Yield:	3.1%	3.0%	2.9%	2.7%	-	-	-



CalPERS 2017 Asset Liability Management Workshop

The ALM Workshop also provided the following analysis to illustrate the variability associated with expected returns relative to the current CalPERS and candidate portfolios.



CalPERS 2017 Asset Liability Management Workshop

PARS 115 Trust Asset Allocation Expenses

Highmark Capital Management currently provides the 115 Pension Trust with five different asset allocation options. Each asset allocation has varying degrees of exposure to equity, fixed income, and cash. The five asset allocations are intended to provide the Pension Plans with five distinct risk/reward profiles. Relative to the current CalPERS asset allocation, the PARS Balanced and Capital Appreciation portfolios have similar (or higher) equity exposure to CalPERS and the PARS Moderate, Moderately Conservative, and Conservative portfolios have lower equity exposure. The following are the asset allocations provided by PARS:

	PARS Conservative	PARS Moderately Conservative	PARS Moderate	PARS Balanced	PARS Capital Appreciation
Equity	15%	30%	50%	60%	75%
Fixed Income	80%	65%	45%	35%	20%
Cash	5%	5%	5%	5%	5%
Expected Return	4.95%	5.68%	6.48%	6.85%	7.39%
Expected Standard Deviation	4.13%	5.26%	7.54%	8.84%	10.9%

The following table provides the fees associated the five asset allocations listed above:

	Weighted embedded Expense Ratio*	Weighted investment management fee**	PARS trust administration fee	Total fees
PARS Conservative	0.09%	0.33%	0.25%	0.67%
PARS Moderately Conservative	0.11%	0.34%	0.25%	0.70%
PARS Moderate	0.13%	0.34%	0.25%	0.72%
PARS Balanced	0.14%	0.34%	0.25%	0.73%
PARS Capital Appreciation	0.15%	0.34%	0.25%	0.74%

*Represents the weighted embedded expense ratio for that fund (Source: Morningstar Direct)

**Represents the weighted investment management fee net of any waivers in place for assets invested in funds for which HighMark serves as sub-adviser/adviser; assuming a \$5 million account

PAGE 5 OF 5

SUBJECT: REVIEW AND DISCUSS OVERSIGHT BOARD ASSET ALLOCATION AND FUNDING
LEVEL

DATE: NOVEMBER 28, 2017

115 Trust Investable Monies

The current available balance subject to final audit and approval of the Town Council of the CalPERS/OPEB Reserve is approximately \$3.3 million. This includes the previously unallocated pension funds total of \$1.8 million held in a reserve account for future pension costs. With the creation of the 115 Pension Trust, staff recommends allocating these funds to the Trust for a total initial investment of \$3.3 million.

CONCLUSION AND STAFF RECOMMENDATION:

Given the aforementioned equity exposure currently obtained through the CalPERS PERF and the uncertainty of timing of withdrawals, staff still recommends choosing an asset allocation that maintains a relatively more conservative level of risk at this time. However, staff appreciates that the Finance Committee may prefer to recommend an asset allocation to the Pension and OPEB Oversight Committee which exhibits equity levels similar to PERF or higher.



**TOWN OF LOS GATOS
FINANCE COMMITTEE REPORT**

MEETING DATE: 06/17/2019

ITEM NO: 3

DATE: JUNE 10, 2019
TO: COUNCIL FINANCE COMMITTEE
FROM: LAUREL PREVETTI, TOWN MANAGER
SUBJECT: REVIEW AND PROVIDE DIRECTION ON ADDITIONAL DISCRETIONARY
PAYMENT STRATEGIES

RECOMMENDATION:

Review and provide direction on additional discretionary payment strategies.

BACKGROUND:

Based on direction from the Town Council and Town Pension and Other Post-Employment Benefits (OPEB) Trusts Oversight Committee (Pension/OPEB Committee), staff presented a report to the Town Pension and OPEB Trusts Oversight Committee on March 5, 2019 entitled "Review and Provide Direction on Additional Discretionary Payment (ADP) Strategies" (Attachment 1). The ADP strategies are intended to reduce unfunded Pension and OPEB obligations. The staff report provided high level informational material about the three primary types of ADP strategies available: (1) long-term capital accumulation and appreciation, (2) pension contribution management, and (3) direct payments to CalPERS. The report concluded that to date, the primary strategies utilized by the Town have been the prefunding of OPEB obligations and ADPs provided to PARS for long-term capital accumulation and appreciation of the Town's pension assets.

On June 4, 2019 the Town Council adopted the FY 2019/20 Operating Budget which among other items identified an additional \$3.2 million allocation to reducing either outstanding OPEB or pension unfunded obligations. Also on June 4, 2019, the Town Pension and OPEB Trusts Oversight Committee held its quarterly meeting. As with past meetings, both bodies expressed

PREPARED BY: ARN ANDREWS
ASSISTANT TOWN MANAGER

Reviewed by: Town Manager, Finance Director, and Town Attorney

PAGE 2 OF 11

SUBJECT: REVIEW AND PROVIDE DIRECTION ON ADDITIONAL DISCRETIONARY PAYMENT STRATEGIES

DATE: JUNE 10, 2019

BACKGROUND (Continued):

an interest in the Town Finance Committee reviewing previous guidance for the exclusive allocation of ADPs to the PARS 115 Pension Trust and analyzing alternative allocation approaches. In addition, there have been recent discussions regarding the appropriateness of the current asset allocations for both the OPEB and Pension Trusts. The Town Council and the Pension/OPEB Committee would also like the Finance Committee to review previous asset allocation decisions and report back to both bodies:

DISCUSSION:

The following report is intended to be informational and summarize previous data, analysis, and Committee decisions regarding the allocation of ADPs and pension/OPEB plan asset allocations. Based on the Finance Committee's deliberations, staff will return at the August Committee meeting with more detailed analysis based on the Committee's direction. If in August the Committee is ready to make a recommendation to the Town Council, the topic would be scheduled in coordination with the Mayor as is the Town's practice. Assuming a September Town Council discussion, this would align well with the anticipated availability of the actuarial valuations update and year end performance reports for both the pension and OPEB plans.

The Town has four primary vessels for receiving additional discretionary payments which include: Town OPEB 115 Trust, CalPERS Town Miscellaneous Plan and Safety Plan, and Town Pension 115 Trust. The following summaries will outline the advantages and disadvantages associated with each one of those vehicles.

Town OPEB 115 Trust

The Town's retiree healthcare plan is an Internal Revenue Code Section 115 Trust which is administered by the Town Pension and OPEB Trusts Oversight Committee. The Oversight Committee is responsible for the management and control of the healthcare assets. In 2009, the Town Council approved a Finance Department recommendation to initiate a ten-year phase in of pre-funding future OPEB obligations. Prior to 2009, the Town like most other cities, followed the generally accepted government accounting principle of paying OPEB benefits on a "pay as you go" basis. The Finance Department recommendation also included participating in the CalPERS managed California Employers' Retiree Benefit Trust (CERBT) Fund. As the table below illustrates, as of July 31, 2018 the Town pre-funded \$12,360,000 since the Trust Fund was established. In addition, the Town's investment in CERBT Strategy 1 has earned approximately \$4.2 million in investment earnings with an average annualized rate of return of 8.33%.

SUBJECT: REVIEW AND PROVIDE DIRECTION ON ADDITIONAL DISCRETIONARY PAYMENT STRATEGIES

DATE: JUNE 10, 2019

DISCUSSION (Continued):

Account summary as of July 31, 2018 (Source: CalPERS Annual Review)	
Initial contribution (6/29/2009)	\$400,000
Additional contributions	\$11,960,000
Disbursements	(\$0)
CERBT expenses	(\$53,431)
Investment earnings	\$4,212,256
Total market value of assets	\$16,518,825
Average annualized internal rate of return (6/29/2009-7/31/2018)	8.33%

CalPERS CERBT Asset Allocation Strategies

The California Employers’ Retiree Benefit Trust (CERBT) provides multiple options for investment of the Town’s retiree healthcare assets. The CalPERS managed CERBT provides three distinct asset allocations. Each asset allocation has varying degrees of exposure to equity, fixed income, Treasury Inflation Protected Securities (TIPS), Real Estate Investment Trusts (REITs), and commodities. Following are the three asset allocations:

2018 Asset Allocation Targets	Strategy 1	Strategy 2	Strategy 3
	2018	2018	2018
Global Equity	59%	40%	22%
Fixed Income	25%	43%	50%
Global Real Estate (REITs)	8%	8%	8%
Treasury Inflation Protected Securities (TIPS)	5%	5%	16%
Commodities	3%	4%	5%

SUBJECT: REVIEW AND PROVIDE DIRECTION ON ADDITIONAL DISCRETIONARY PAYMENT STRATEGIES

DATE: JUNE 10, 2019

DISCUSSION (Continued):

The three investment options represent varying degrees of investment risk/return profiles. As the table below illustrates, a reduction in equity exposure correlates to a reduction in long-term expected returns and a reduction in the variability of those returns as expressed by standard deviation.

2018 Asset Allocation Strategies	Strategy 1	Strategy 2	Strategy 3
	2018	2018	2018
Expected Long Term Annualized Rate of Investment Return	7.59%	7.01%	6.22%
Discount Rate	Determined by Actuary (Currently 6.75%)	Determined by Actuary (Currently 6.75%)	Determined by Actuary (Currently 6.75%)
Standard Deviation of Expected Investment Returns	11.83%	9.24%	7.28%

OPEB Funding Status

Since the initial \$400,000 prefunding in 2009, the OPEB funded status has grown steadily due to the additional contributions and investment earnings. Based on the June 30, 2017 Retiree Healthcare Plan Actuarial Valuation performed by Bartel Associates, the funded status of the plan has grown to 55%.

Valuation Date	Total OPEB Liability	Actuarial Value of Assets	Funded Status
6/30/2013	\$19,211,000	\$4,866,000	25%
6/30/2015	\$20,977,000	\$8,238,000	39%
6/30/2017	\$24,773,000	\$13,605,000	55%
Projected 6/30/2018	\$26,390,000	\$16,148,000	61.2%

Source: Bartel Associates Actuarial Valuations

SUBJECT: REVIEW AND PROVIDE DIRECTION ON ADDITIONAL DISCRETIONARY PAYMENT STRATEGIES

DATE: JUNE 10, 2019

DISCUSSION (Continued):

It is important to note that during the development of the 2017 actuarial valuation, the Oversight Committee elected to lower the discount rate from 7.25% to 6.75%. In addition, since the development of the 2017 actuarial valuation, the Town’s bargaining groups and Management and Confidential employees agreed to eliminate the current retiree healthcare benefit prospectively for new employees. During labor negotiations, staff asked Bartel Associates to perform a preliminary review of what the implications may be for the funding status and potential funded status if ADPs were allocated to the OPEB plan. Provided below is a summary of the preliminary data:

2018 Asset Allocation Strategies & Discount Rates (Amounts in 000’s)	CERBT Strategy 1	CERBT Strategy 2	CERBT Strategy 3
	6.75%	6.25%	5.50%
Actuarial Accrued Liability (AAL)	\$26,390	\$28,020	\$30,785
Market Value of Assets (MVA)	16,277	16,277	16,277
Unfunded AAL (UAAL)	10,113	11,743	14,508
Funded Percentage	61.7%	58.1%	52.9%
\$ Amount Needed for 80% Funded %	\$4,835	\$6,139	\$8,351

OPEB Trust ADP Advantages

- Multiple asset allocation options
- Control over asset allocation
- Control over discount rate/assumed rate of return
- Control over amortization period
- Immediate unfunded actuarial accrued liability (UAAL) and contribution impact
- Less UAAL interest cost
- Reduces accounting net pension liability

OPEB Trust ADP Disadvantages

- Market timing risk
- Assets restricted to OPEB benefits

DISCUSSION (Continued):

CalPERS Town Miscellaneous and Safety Plans

The Town’s pension plans are administered by the Board of Administration of the California Public Employees’ Retirement System (CalPERS). In addition, the Board has exclusive control of the administration and investment of funds. The Miscellaneous Plan is administered by CalPERS and invested in the Public Employees’ Retirement Fund (PERF A). Sworn employees are covered under the Safety Plan which is a pooled cost-sharing plan and invested in PERF C. According to the 2017 Annual Valuations provided by CalPERS, the Miscellaneous Plan and Safety Plan had \$69.5 million and \$62.5 million calculated Market Value of Assets, respectively. According to CalPERS, 59 cents of every dollar paid out of the PERF fund has historically been from investment returns.

CalPERS Public Employees Retirement Fund (PERF) Asset Allocation

The PERF was established by statute in 1931 and provides retirement, death and disability benefits to members of its participating employers, which include the State of California, non-teaching, non-certified employees in schools, and various other public agencies. The benefits options for the public agencies are established by statute and voluntarily selected by contract with the system in accordance with the provisions of the Public Employees' Retirement Law.

In December 2017, the CalPERS Board voted on the asset allocation of the PERF's investment portfolio for the next four years. The Board examined four potential portfolios and their impact on the PERF. Each portfolio represented different distributions of assets based on varying rates of expected return and risk of volatility. The Board selected the portfolio with expected volatility of 11.4 percent and a return of 7.0 percent, which aligns with the December 2016 decision to lower the discount rate to 7.0 percent over three years. The following tables provide the PERF investment returns for the 12-month period that ended June 30, 2018, as well as five-year, ten-year, and twenty-year periods since inception.

CalPERS Investment Return	2018	5 Years	10 Years	20 Years	PERF Since Inception (1988)
	8.6%	8.1%	5.6%	6.1%	8.4%

The current asset allocation is provided in the next table.

SUBJECT: REVIEW AND PROVIDE DIRECTION ON ADDITIONAL DISCRETIONARY PAYMENT STRATEGIES

DATE: JUNE 10, 2019

DISCUSSION (Continued):

2018 PERF Asset Allocation Targets	PERF A	PERF C
	2018	2018
Global Equity	49%	49%
Private Equity	8%	8%
Global Debt Securities	22%	22%
Real Assets	12%	12%
Liquidity	3%	4%
Inflation	6%	6%

Miscellaneous and Safety Pension Plan Funding Status

As of June 30, 2017, the funded status of the PERF was 70.1 percent. The funded status as of June 30, 2018, is estimated to be approximately 71.0 percent. PERF funded status values were calculated using a 7.00 percent discount rate. In December 2016, the CalPERS board voted to lower the discount rate from 7.5 percent to 7.0 percent. Also in February 2018, the CalPERS Board voted to shorten the period over which actuarial gains and losses are amortized from 30 to 20 years. The table below illustrates the funding history for both the Town’s Miscellaneous and Safety Plans.

Pension Plan	Valuation Date 6/30/11	Valuation Date 6/30/14	Valuation Date 6/30/17
Miscellaneous	72.6%	76.2%	69.6%
Safety	71.7%	82.2%	73.9%

SUBJECT: REVIEW AND PROVIDE DIRECTION ON ADDITIONAL DISCRETIONARY PAYMENT STRATEGIES

DATE: JUNE 10, 2019

DISCUSSION (Continued):

Provided below is the schedule of amortization bases for the Miscellaneous Plan as of June 30, 2017. Similar to the early analysis performed on the OPEB Plan by Bartel Associates, if the Finance Committee were interested, staff could ask Bartel Associates to run scenarios which illustrate the effects on contribution rates and funding status for paying down/off varying amortization bases.

Reason for Base	Date Established	Ramp Up/Down 2019-20	Amortization Period	Balance 6/30/17	Expected Payment 2017-18	Balance 6/30/18	Expected Payment 2018-19	Balance 6/30/19	Scheduled Payment for 2019-20
ASSUMPTION CHANGE	06/30/03	No Ramp	6	\$1,780,035	\$266,995	\$1,632,584	\$273,196	\$1,468,020	\$280,479
METHOD CHANGE	06/30/04	No Ramp	7	\$(166,052)	\$(22,588)	\$(154,698)	\$(23,102)	\$(141,989)	\$(23,720)
BENEFIT CHANGE	06/30/07	No Ramp	9	\$1,646,511	\$190,679	\$1,568,412	\$194,828	\$1,480,355	\$200,062
ASSUMPTION CHANGE	06/30/09	No Ramp	12	\$2,566,712	\$247,607	\$2,496,373	\$252,637	\$2,415,725	\$259,458
SPECIAL (GAIN)/LOSS	06/30/09	No Ramp	22	\$2,100,631	\$142,257	\$2,105,604	\$144,524	\$2,108,588	\$148,467
SPECIAL (GAIN)/LOSS	06/30/10	No Ramp	23	\$1,755,770	\$116,186	\$1,762,739	\$117,992	\$1,768,343	\$121,214
ASSUMPTION CHANGE	06/30/11	No Ramp	14	\$1,710,594	\$150,016	\$1,679,253	\$152,924	\$1,642,629	\$157,063
SPECIAL (GAIN)/LOSS	06/30/11	No Ramp	24	\$809,430	\$52,416	\$813,831	\$53,210	\$817,729	\$54,664
PAYMENT (GAIN)/LOSS	06/30/12	No Ramp	25	\$199,878	\$12,683	\$201,234	\$12,870	\$202,495	\$13,222
(GAIN)/LOSS	06/30/12	No Ramp	25	\$1,791,787	\$113,697	\$1,803,946	\$115,376	\$1,815,246	\$118,531
(GAIN)/LOSS	06/30/13	100% →	26	\$10,388,059	\$419,466	\$10,706,787	\$567,711	\$10,895,099	\$729,061
ASSUMPTION CHANGE	06/30/14	80% ↗	17	\$4,484,869	\$166,960	\$4,637,116	\$255,108	\$4,709,113	\$349,398
(GAIN)/LOSS	06/30/14	80% ↗	27	\$(7,403,556)	\$(202,526)	\$(7,730,575)	\$(308,168)	\$(7,971,898)	\$(422,159)
(GAIN)/LOSS	06/30/15	60% ↗	28	\$3,320,211	\$46,754	\$3,512,507	\$94,780	\$3,669,008	\$146,078
ASSUMPTION CHANGE	06/30/16	40% ↗	19	\$1,502,722	\$(42,200)	\$1,655,372	\$31,238	\$1,743,036	\$64,186
(GAIN)/LOSS	06/30/16	40% ↗	29	\$4,225,172	\$0	\$4,531,497	\$62,882	\$4,794,909	\$129,230
ASSUMPTION CHANGE	06/30/17	20% ↗	20	\$1,176,961	\$(50,144)	\$1,314,221	\$(51,586)	\$1,462,925	\$27,570
(GAIN)/LOSS	06/30/17	20% ↗	30	\$(1,513,779)	\$0	\$(1,623,528)	\$0	\$(1,741,234)	\$(24,135)
TOTAL				\$30,375,955	\$1,608,258	\$30,912,675	\$1,946,420	\$31,138,099	\$2,328,669

Miscellaneous and Safety Pension Plan ADP Advantages

- Immediate UAL and contribution impact
- Can elect shorter amortization (Fresh Start)
- Can elect to pay specific amortization bases
- Less UAL interest cost

Miscellaneous and Safety Pension Plan ADP Disadvantages

- Single asset allocation option
- No control over discount rate/assumed rate of return
- Market timing risk
- Assets restricted to pension benefits
- No current benefit to accounting net pension liability
- Pooled liability risk with Safety Plan

Town Pension 115 Trust

On August 15, 2017, Town Council approved Public Agency Retirement Services (PARS) as the administrator of the Town's Section 115 Pension Trust. The 115 Pension Trust acts as an additional investment vehicle for the overall funding of pension liabilities associated with the

SUBJECT: REVIEW AND PROVIDE DIRECTION ON ADDITIONAL DISCRETIONARY PAYMENT STRATEGIES

DATE: JUNE 10, 2019

DISCUSSION (Continued):

Town’s Miscellaneous and Safety Pension Plans (the “Pension Plans”). The 115 Pension Trust provides the Town with flexibility in a variety of ways, including making lump sum payments directly to CalPERS and augmenting budget stability by using trust assets to defray pension costs in future years. In addition, the 115 Pension Trust can be utilized to either mimic or alter the risk/reward profile of assets currently invested with CalPERS.

On December 4, 2017, the Council Finance Committee recommended to invest in the PARS Capital Appreciation Index Plus. PARS utilizes the services of Highmark Capital for the management of the 115 assets. In addition, the Committee recommended that assets placed in the 115 Pension Trust be dollar cost averaged over the next year to mitigate risks associated with a single market entry point. On December 19, 2017, the Town Pension and OPEB Trusts Oversight Committee affirmed the Committee recommendations.

Asset Allocation Strategies

Highmark Capital Management currently provides the 115 Pension Trust with five different asset allocation options. Each asset allocation has varying degrees of exposure to equity, fixed income, and cash. The five asset allocations are intended to provide the Pension Plans with five distinct risk/reward profiles. The following are the equity exposures and investment objectives for the asset allocations provided by PARS:

PARS Strategy	Investment Objective	Equity Allocation	Fixed Income	Cash
Capital Appreciation	Provide growth of principal and income	65-85%	10-30%	0-20%
Balanced	Provide growth of principal and income	50-70%	30-50%	0-20%
Moderate	Provide growth of principal and income	40-60%	40-60%	0-20%
Moderately Conservative	Provide current income and moderate capital appreciation	20-40%	50-80%	0-20%
Conservative	Provide a consistent level of inflation-protected income over the long-term	5-20%	60-95%	0-20%

DISCUSSION (Continued):

The asset allocation for the PARS Capital Appreciation Index Plus portfolio as of April 30, 2019 is provided below.

PARS Strategy	Equity Allocation	Fixed Income	Cash
Capital Appreciation	76%	22%	2%

For the period ending April 30, 2019 the investment returns for the PARS Capital Appreciation Index Plus portfolio are provided below with an expected standard deviation of 11.85%.

PARS Strategy	1 Month	3 Month	1 Year*
Capital Appreciation	2.37%%	5.99%	6.79%

*Plans Inception Date 3/20/2018

PARS Funding Status

In March 2018 the initial \$300,000 was deposited into the PARS account with additional \$300,000 deposits programmed monthly for a current total of \$4.4 million in assets as of April 30, 2019.

PARS Pension Trust ADP Advantages

- Actuarial equivalence with CalPERS for interest savings if assumed rate of return achieved
- Multiple asset allocation options
- Control over asset allocation
- Assets can be used to pay CalPERS directly or reimburse the Town for CalPERS contributions

PARS Pension ADP Disadvantages

- Market Timing Risk
- Assets Restricted to Pension Benefits
- No Current Benefit to Accounting Net Pension Liability

PAGE 11 OF 11

**SUBJECT: REVIEW AND PROVIDE DIRECTION ON ADDITIONAL DISCRETIONARY PAYMENT
STRATEGIES**

DATE: JUNE 10, 2019

CONCLUSION:

Staff looks forward to the discussion with the Committee and its direction on next steps

ATTACHMENT:

1. Public Comment

