MEETING DATE: 08/04/2020

ITEM NO: 5

ADDENDUM

TOWN OF LOS GATOS

TOWN PENSION AND OPEB TRUSTS OVERSIGHT COMMITTEE REPORT

DATE:	August 3, 2020
TO:	Town Pension and OPEB Trusts Oversight Committee
FROM:	Laurel Prevetti, Town Manager
SUBJECT:	Consider Finance Committee Recommendation Regarding a Methodology for Additional Discretionary Payments to CalPERS

REMARKS:

Attachment 2 contains public comment received since the issuance of the staff report on Thursday, July 30, 2020, and before 11:00 a.m. Monday, August 3, 2020.

Attachments previously received with the Staff Report:

1. June 8, 2020, Finance Committee Staff Report

Attachment distributed with this Addendum:

2. Public Comments received 11:01 a.m. Thursday, July 30, 2020 and 11:00 a.m. Monday, August 3, 2020.

PREPARED BY: ARN ANDREWS
Assistant Town Manager

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

From: Phil Koen
Sent: Monday, August 3, 2020 9:07 AM
To: Marcia Jensen <MJensen@losgatosca.gov>; Marico Sayoc <MSayoc@losgatosca.gov>; BSpector <BSpector@losgatosca.gov>; Rob Rennie <RRennie@losgatosca.gov>
Cc: Laurel Prevetti <LPrevetti@losgatosca.gov>; Arn Andrews <aandrews@losgatosca.gov>
Subject: Pension and OPEB Trust meeting - August 4, 2020

Agenda Item #5

The Staff report discusses the concept of "unique market exposure" and gives an example of this concept in page 2 of the report. However, I have a slightly different understanding, which I think the Committee should validate with CALPERS. The issue of when a payment is made to CALPERS is a non-issue since CALPERS **time weights the amount of the ADP investment not the rate of return.** Using the Staff's example, if PERF Fund had a **10% gain for the entire year** and the Town made an ADP of $5m on January 1 (at the mid-point of the fiscal year), CALPERS would compute the gain on the $5m by time weighting the investment and then multiplying it **by the full year performance return, regardless of market fluctuations from the date of the ADP until the end of the fiscal period**. That means the $5m would be effectively invested for only 6 months, resulting in only **$2.5m being time weighted exposed** to the full year return of 10%. Since the full year return of 10% is greater than the 7% expected rate of return, the ADP would generate a "**gain"** of $75k (3% x $2.5m) and not a "loss" as suggested by the Staff. (As a side note, It would be helpful if Staff showed the calculations which support their position that the ADP "would be allocated a proportionate investment loss as opposed to an investment gain).

The important point here is that CALPERS uses the **return for the entire year** in determining whether or not a gain or loss basis is created and time weights the ADP to avoid the exact situation the Staff has identified. This approach neutralizes all "market timing issues" since the investment return is applied based on the full year results. Based on my understanding CALPERS does not track the gain or loss from an ADP separately from the full year investment return. This should be very easy to verify and I would encourage the Committee to request Staff to verify what I have outlined above. Assuming I am correct, the timing of making an ADP during a fiscal year therefore is a non-issue with regard to computing return performance for the ADP. Having said that, the default condition should be to make an ADP as soon as possible because of the benefit of saving the 7% interest charged by CALPERS. Once a loss basis is extinguished, the interest charge associated with that loss basis stops.

Thank you for your time.

Phil Koen

ATTACHMENT 2