



## Item No. 7 Town of Atherton

### FINANCE COMMITTEE STAFF REPORT

**TO:** FINANCE COMMITTEE

**FROM:** ROBERT BARRON III, FINANCE DIRECTOR

**DATE:** SEPTEMBER 13, 2016

**SUBJECT:** REVIEW AND DISCUSS PARS OPEB PRE-FUNDING TRUST  
PROGRAM REVIEW PRESENTATION BY PARS AND HIGH MARKET  
CAPITAL

#### RECOMMENDATION

1. Review and discuss the OPEB pre-funding trust program yearly review presentation by PARS and High Market Capital.

#### BACKGROUND

The Town of Atherton established an irrevocable trust to prefund the Town's OPEB (Other Post-Employment Benefits) retiree health care costs for its employees identified in the Town's policies or applicable collective bargaining agreements. The Town participates in the PARS (Public Agency Retirement Services) Post-Retirement Health Care Plan Trust Program. Over the past couple of years the Council has taken significant steps to reduce the Town's OPEB Liability. The Town made an initial OPEB contribution of \$1,299,316 to the PARS Trust in Fiscal Year 2012-2013 and over the years has continued to make contributions. Based on the OPEB Actuarial refresh as of July 1, 2014, the OPEB Liability was estimated as follows:

<b>As of 7/1/2014</b>	
Active Employees	\$1,851,691
Retirees Spouses	\$5,607,553
<b>Accrued Actuarial Liability (AAL)</b>	<b>\$7,459,244</b>
Prior Town Contribution to PARS Trust FY 12/13	(\$1,299,316)
Contribution Towards PARS Trust FY 13/14	(\$2,000,000)
ERAF Contribution FY 14/15	(\$1,020,000)
ERAF Contribution FY 15/16 August 2015	(\$680,684)
<b>Estimated Unfunded Actuarial Liability Amount</b>	<b>\$2,459,244</b>

**REVIEW AND DISCUSS PARS OPEB PRE-FUNDING TRUST YEARLY REVIEW**

**September 13, 2016**

**Page 2 of 3**

Town discussions revolved around making a contribution of up to \$5 Million into the OPEB Trust. Based on the current OPEB Actuarial report for the postemployment health care program, the Town has almost funded the accrued actuarial liability for retirees and spouses. During Town FY 2016-17 budget discussions, there was no recommendation for a contribution towards the Trust. This fiscal year the Town will do a refresh of its OPEB postemployment health care program actuary. Staff believes that once the new actuary is completed, then there will be a potential recommendation for additional contribution to the Trust. The Town is in excellent funding status and the OPEB liability is approximately 67 percent funded.

The Trust enables the Town to pre-fund the cost of benefits today and leverage interest earnings to lower the long-term future costs. The Town of Atherton continues to structure its investment options to meet our OPEB goals. The PARS trust provides investment flexibility in strategy approach and risk tolerance. The Town's current long-term average target rate of return is set at 6 percent (%). *The current investment strategy for the Town is the Moderate Index Plus (passive) as the committee last year recommended to maintain this investment strategy.* High Market Capital has five diversified investment strategies to choose from:

<b>Conservative</b>
<b>Moderate Conservative</b>
<b>Moderate</b>
<b>Balanced</b>
<b>Capital Appreciation</b>

We monitor investment risks on assets with a long term outlook to provide promising returns on investments. Staff recommends that the investment strategy should be maintained as the Moderate Index Plus (Passive). The overall goal of Town's investment plan is to produce sufficient long-term returns to pay the present and future obligations of OPEB benefits to retirees.

**Moderate Index PLUS Investment Strategy**

<b>Beginning Balance as of July 1, 2015</b>	<b>Additional Contributions</b>	<b>Trust Earnings Minus expenses</b>	<b>Ending Balance as of July 1, 2016</b>
<b>\$4,625,891</b>	<b>\$680,684</b>	<b>\$220,112</b>	<b>\$5,526,686</b>

*Attached is also the PARS annual account report for the Trust from the period 7/1/2015 to 7/1/2016*

*The Town continues to use the PARS trust to administer its health plan program for payment of retiree health plan pay as you go. Contributions of \$410,473 were made in the year for retiree health and equates to \$410,473 in distributions. The pay as you go for retiree health is a budget expense in the Town operating budget. The OPEB Trust has earned \$526,686 since inception or 10.5 percent.*

*Senior Portfolio Manager Andrew Brown from High Market Capital is here today to discuss the investment highlights of the Town of Atherton OPEB trust, and answer questions regarding the*

**REVIEW AND DISCUSS PARS OPEB PRE-FUNDING TRUST YEARLY REVIEW**

**September 13, 2016**

**Page 3 of 3**

*Town's strategy. Mitch Barker and Jennifer Meza of PARS are here as well to discuss the pre-funding program. Today's presentation is a review of the OPEB pre-funding program of the Town.*

**FISCAL IMPACT**

None

**ATTACHMENT**

PARS OPEB Prefunding Trust Program Review

PARS-Town of Atherton OPEB Statement

Pages 3 & 5 of the Atherton Actuarial Valuation of Postemployment Health Care Program

OPEB Pre-Funding Trust Program  
Client Review



# Town of Atherton

September 13, 2016

PUBLIC  
AGENCY  
RETIREMENT  
SERVICES

# PARS

TRUSTED SOLUTIONS. LASTING RESULTS.



# Contacts

## **PARS**

Mitch Barker, Executive Vice President

[mbarker@pars.org](mailto:mbarker@pars.org); 800.540.6369 ext. 116

Jennifer Meza, Senior Client Services Coordinator

[jmeza@pars.org](mailto:jmeza@pars.org); 800.540.6369 ext. 141

## **HighMark Capital Management**

Andrew Brown, CFA, Senior Portfolio Manager

[Andrew.Brown@highmarkcapital.com](mailto:Andrew.Brown@highmarkcapital.com); 415.705.7605

# OPEB Trust Team

	 		
Role	<b>Trust Administrator and Consultant</b> <ul style="list-style-type: none"> <li>• Recordkeeping/Sub-trust Accounting</li> <li>• Actuarial Coordination</li> <li>• Monitor Contributions/ Process Disbursements</li> <li>• Monitor Plan Compliance                             <ul style="list-style-type: none"> <li>• Ongoing Client Liaison</li> </ul> </li> <li>• <b>Pre-fund Pension Option</b></li> </ul>	<b>Trustee</b> <ul style="list-style-type: none"> <li>• Safeguard Plan Assets</li> <li>• Oversight Protection                             <ul style="list-style-type: none"> <li>• Plan Fiduciary</li> </ul> </li> <li>• Custodian of Assets</li> </ul>	<b>Investment Manager</b> <ul style="list-style-type: none"> <li>• Investment Sub-advisor to U.S. Bank                             <ul style="list-style-type: none"> <li>• Open Architecture</li> </ul> </li> <li>• Investment Policy Assistance</li> </ul>
Corporate Experience	32 years <i>(1984 – 2016)</i>	153 years <i>(1863 – 2016)</i>	97 years <i>(1919 – 2016)</i>
OPEB Experience	20 years	11 years	20 years
Number of Plans under Administration	1,400+ plans for 700+ public agencies		
Dollars under Administration	More than \$2 billion	More than \$4 trillion	More than \$14.9 billion under management

# Plan Overview

**Type of Plan:** IRC Section 115 Irrevocable Exclusive Benefit Trust

**Trustee Approach:** Discretionary

**Plan Effective Date:** May 16, 2012

**Plan Administrator:** George Rodericks- City Manager

**Current Investment Strategy:** Moderate (Index) Strategy

- Selected on 6/26/2012

**As of 7/31/2016:**

**Initial Contribution:** June 2013 – \$1,299,316

**Additional Contributions:** \$4,613,304

**Total Contributions:** \$5,912,620

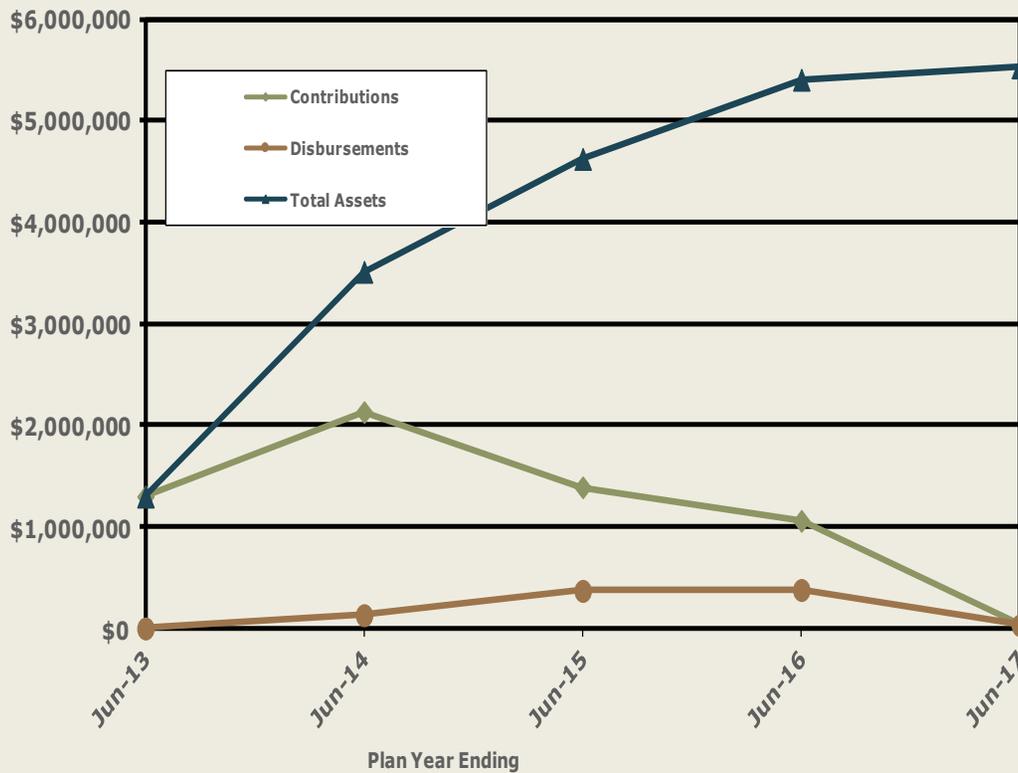
**Disbursements:** (\$911,492)

**Total Investment Earnings:** \$594,546

**Account Balance:** \$5,526,687

# Summary of the Plan's Activity

**Town of Atherton  
Total Assets, Contributions & Disbursements**



Plan Y/E	Contributions	Disbursements	Total Assets
Jun -13	\$1,299,316	\$0	\$1,298,993
Jun -14	\$2,131,844	\$130,716	\$3,513,466
Jun -15	\$1,390,303	\$370,303	\$4,625,891
Jun -16	\$1,059,817	\$379,133	\$5,405,490
Jun -17*	\$31,341	\$31,341	\$5,526,687

\* Plan Year Ending June 2017 is based on 1 month of activity through 07/31/2016

# Actuarial Results

We have received the actuarial reports prepared by Nicolay Consulting Group on with a valuation date of July 1, 2014. In the tables below, we have summarized the results.

## Demographic Study

	January 1, 2009 Valuation	July 1, 2014 Valuation
Active Participants	51	36
Retirees	18	36
Total Plan Members	69	72

# Actuarial Results (continued)

	January 1, 2009 Valuation 4.00% Discount Rate (Pay-as-you-go)	July 1, 2014 Valuation 6.00% Discount Rate (Pre-funding)
Present Value of Benefits (PVB)	\$12,263,327	\$9,013,372
Actuarial Accrued Liability (AAL)	\$9,051,041	\$7,788,996
Actuarial Value of Assets	\$0	\$4,810,526
Unfunded Actuarial Accrued Liability (UAAL)	\$9,051,041	\$2,978,470*
Normal Cost	\$578,987	\$165,397
UAAL Amortization	\$370,050	\$175,067
Annual Required Contribution (ARC)	\$949,037	\$340,464*
Pay-As-You-Go	\$243,694	\$413,104*

**Note:** Rule of thumb is - for every one percent increase in the discount rate, the unfunded liability is reduced by 10-12%.

\*2015-2016 FY

**Town of Atherton**

**July 31, 2016**

**Presented by  
Andrew Brown, CFA**

## DISCUSSION HIGHLIGHTS – Town of Atherton

### Asset Allocation: PARS/PRHCP Moderate Index (As of 9-1-2016)

- Allocation Target – 49.25% stocks (40-60% range), 47.5% bonds (40-60% range), 3.25% cash (0-20% range)
- Large cap 23.5%, mid-cap 3.5%, small cap 9.25%, international 11.25%, REIT 1.75%.

### Performance: PARS/PRHCP Moderate Index

*(as of 7-31-2016) net of embedded fund expenses, gross of investment management fees*

- Quarter: 3.81%
- Year to date: 6.28%
- 1-Year: 3.57%
- 3-Year: 5.63%
- Inception to date (7/2013) 6.32%
- Bonds – Short duration a negative, High yield a detractor
- Stocks –
  - International equity in negative territory for last 12-month period. Emerging market modest positive
  - Small cap modest return, Mid-cap and large cap mid single digit return
  - REITs – Benefit of low interest rate environment
  - Value overweight vs. growth

### Changes since last meeting

- Sold High Yield ETF
- Sold Dow Jones Euro Stoxx 50 ETF
- Add Vanguard REIT ETF

### Outlook remainder 2016

- Continue focus on the FED and monetary policy – 1 rate hike in 2016
- International economic fears – Brexit, Europe, China, Commodities, U.S. election
- GDP est. 2%
- Unemployment 4.8%
- 10-yr yield 2.25%, Fed Funds 0.75% - 1%
- PCE Inflation 2%

**Selected Period Performance**  
**PARS/PRHCP MODERATE, INDEX PLUS**  
**Account 6746019206**  
**Period Ending: 07/31/2016**

Sector	3 Months	Year to Date (7 Months)	1 Year	2 Years	3 Years	Since Inception (37 Months)
Cash Equivalents	.07	.16	.19	.11	.08	.07
<i>iMoneyNet, Inc. Taxable</i>	.03	.06	.07	.04	.03	.03
Total Fixed Income	2.26	5.54	5.16	3.68	3.69	3.73
<i>BC US Aggregate Bd Index</i>	2.47	5.98	5.93	4.37	4.23	4.16
Total Equities	5.48	7.48	1.54	4.08	7.67	9.24
Large Cap Funds	5.39	7.85	4.99	7.87	10.63	12.18
<i>S&amp;P 500 Composite Index</i>	5.82	7.66	5.61	8.37	11.16	12.64
Mid Cap Funds	6.53	10.79	4.81	7.52	10.36	12.12
<i>Russell Midcap Index</i>	6.76	10.31	4.37	7.49	10.37	12.10
Small Cap Funds	7.88	9.07	.68	6.04	7.84	9.98
<i>Russell 2000 Index</i>	8.29	8.32	.00	5.84	6.74	8.92
REIT Funds	13.69	18.04				
<i>Wilshire REIT Index</i>	13.33	15.93	21.03	16.06	14.94	14.81
International Equities	2.56	3.05	-7.17	-5.19	.52	1.57
<i>MSCI EAFE Index</i>	.62	.42	-7.53	-3.97	2.00	3.66
<i>MSCI EM Free Index</i>	5.16	11.77	-.75	-7.28	-.29	.06
Total Managed Portfolio	3.81	6.28	3.57	4.05	5.63	6.32

Account Inception : 07/01/2013

Returns are gross of account level investment advisory fees and net of any fees, including fees to manage mutual fund or exchange traded fund holdings. Returns for periods over one year are annualized. The information presented has been obtained from sources believed to be accurate and reliable. Past performance is not indicative of future returns. Securities are not FDIC insured, have no bank guarantee, and may lose value.

# ASSET ALLOCATION – Town Of Atherton

As of July 31, 2016

Current Asset Allocation		Investment Vehicle	
<b>Equity</b>		<b>Range: 40%-60%</b>	<b>50.46%</b>
Large Cap Core	IVV	iShares S&P 500 Index Fund	5.67%
Large Cap Value	IVE	iShares S&P 500 Value Fund	11.52%
Large Cap Growth	IVW	iShares S&P 500 Growth Fund	6.88%
Mid Cap Core	IWR	iShares Russell MidCap Index Fund	2.70%
Mid Cap Value	IWS	iShares Russell MidCap Value Fund	1.04%
Small Cap Value	IWN	iShares Russell 2000 Value Fund	5.81%
Small Cap Growth	IWO	iShares Russell 2000 Growth Fund	3.63%
International Core	EFA	iShares MSCI EAFE Index Fund	8.66%
Emerging Markets	VWO	Vanguard FTSE Emerging Markets ETF	2.85%
Real Estate	VNQ	Vanguard REIT ETF	1.69%
<b>Fixed Income</b>		<b>Range: 40%-60%</b>	<b>46.87%</b>
Short-Term	VFSUX	Vanguard Short-Term Corp Adm Fund	7.61%
Intermediate-Term	AGG	iShares Barclays Aggregate Bond Fund	39.27%
<b>Cash</b>		<b>Range: 0%-20%</b>	<b>2.67%</b>
	FPZXX	First American Prime Obligations Fund	2.67%
<b>TOTAL</b>			<b>100.00%</b>

## TOWN OF ATHERTON

### For Period Ending July 31, 2016

LARGE CAP EQUITY FUNDS							
Fund Name	1-Month Return	3-Month Return	Year-to- Date	1-Year Return	3-Year Return	5-Year Return	10-Year Return
iShares S&P 500 Growth Index	4.63	7.01	6.18	5.12	13.05	13.87	9.26
iShares S&P 500 Index Fnd	3.68	5.80	7.63	5.56	11.10	13.31	7.69
iShares S&P 500 Value Index	2.70	4.53	9.01	5.60	8.64	12.39	5.80
MID CAP EQUITY FUNDS							
iShares Russell Midcap Index	4.54	6.71	10.18	4.20	10.18	12.54	8.63
iShares Russell Midcap Value	4.23	6.84	13.32	7.54	10.38	13.20	8.12
SMALL CAP EQUITY FUNDS							
iShares Russell 2000 Growth Fund	5.39	7.67	11.81	5.58	5.93	9.92	5.76
iShares Russell 2000 Growth	6.55	8.93	4.94	-5.11	7.55	10.93	8.47
INTERNATIONAL EQUITY FUNDS							
iShares MSCI EAFE Index	5.05	0.62	0.48	-7.54	1.89	2.92	1.90
Vanguard FTSE Emerging Markets ETF	4.67	6.27	12.84	-1.33	0.44	-2.48	3.89
REAL ESTATE FUNDS							
Vanguard REIT ETF	4.18	14.00	18.25	22.23	14.64	13.00	7.66
BOND FUNDS							
iShares Barclays Aggregate Bond	0.61	2.44	5.94	5.83	4.21	3.49	4.92
Vanguard Short-Term Investment-Grade Adm	0.46	1.31	3.56	3.55	2.56	2.39	3.71

Source: SEI Investments, Morningstar Investments

Returns less than one year are not annualized. Past performance is no indication of future results. The information presented has been obtained from sources believed to be accurate. Securities are not FDIC insured, have no bank guarantee and may lose value.



**TOWN OF ATHERTON**  
**PARS OPEB Trust Program**

**Monthly Account Report for the Period**  
**7/1/2016 to 7/31/2016**

Robert Barron III  
 Finance Director  
 Town of Atherton  
 91 Ashfield Road  
 Atherton, CA 94027

**Account Summary**

Source	Beginning Balance as of 7/1/2016	Contributions	Earnings	Expenses	Distributions	Transfers	Ending Balance as of 7/31/2016
Employer Contribution	\$5,405,489.84	\$31,340.73	\$125,314.30	\$4,117.31	\$31,340.73	\$0.00	\$5,526,686.83
<b>Totals</b>	<b>\$5,405,489.84</b>	<b>\$31,340.73</b>	<b>\$125,314.30</b>	<b>\$4,117.31</b>	<b>\$31,340.73</b>	<b>\$0.00</b>	<b>\$5,526,686.83</b>

**Investment Selection**

Moderate Index PLUS

**Investment Objective**

The dual goals of the Moderate Strategy are growth of principal and income. It is expected that dividend and interest income will comprise a significant portion of total return, although growth through capital appreciation is equally important. The portfolio will be allocated between equity and fixed income investments.

**Investment Return**

1-Month	3-Months	1-Year	Annualized Return			Plan's Inception Date
			3-Years	5-Years	10-Years	
2.32%	3.79%	3.86%	5.51%	-	-	6/24/2013

Information as provided by US Bank, Trustee for PARS; Not FDIC Insured; No Bank Guarantee; May Lose Value

Past performance does not guarantee future results. Performance returns may not reflect the deduction of applicable fees, which could reduce returns. Information is deemed reliable but may be subject to change.

Investment Return: Annualized rate of return is the return on an investment over a period other than one year multiplied or divided to give a comparable one-year return.

Account balances are inclusive of Trust Administration (unless invoiced), Trustee and Investment Management fees

# FINAL

Table 2-1b

**Present Value of Future Benefit Cost  
Attributable to Past Service (i.e., Actuarial Accrued Liability)  
as of July 1, 2014**

	<u>Management</u>	<u>Police</u>	<u>APOA Misc.</u>	<u>Teamsters</u>	<u>Total</u>
Actives	\$ 608,889	\$ 783,378	\$ 278,549	\$ 342,604	\$ 2,013,420
Retirees and Spouses	<u>1,818,897</u>	<u>2,450,342</u>	<u>172,592</u>	<u>1,139,212</u>	<u>5,581,043</u>
Actuarial Accrued Liability	\$ 2,427,786	\$ 3,233,720	\$ 451,141	\$ 1,481,816	\$ 7,594,463
Actuarial Value of Assets					\$ 3,513,466
Unfunded Actuarial Accrued Liability					\$ 4,080,997

## Projected Postemployment Health Benefit Costs

Table 2-2 contains a ten-year projection of the benefits that the Town is expected to pay to current and future retirees.

Table 2-2

**Estimated Future  
pay-as-you-go Benefits**

<u>Year</u>	<u>Estimated Amount</u>
2014 / 15	\$406,634
2015 / 16	\$413,104
2016 / 17	\$432,333
2017 / 18	\$446,761
2018 / 19	\$460,580
2019 / 20	\$474,636
2020 / 21	\$496,480
2021 / 22	\$521,025
2022 / 23	\$540,559
2023 / 24	\$549,046

# FINAL

Table 2-4 presents a projection under the assumptions that the Town **contributes \$1,020,000 in 2014/15 and \$680,684 in 2015/16, in addition to benefits paid**, the discount rate remains 6.00%, and the Normal Cost component of the ARC increases by 5% per year throughout the period.

Table 2-4 Town of Atherton					
Projection of Annual OPEB Cost and Net OPEB Obligation Based on a 6.00% discount rate and the Entry Age Normal Actuarial Cost Method					
	2014 / 2015	2015 / 2016	2016 / 2017	2018 / 2019	2019 / 2020
<b>Actuarial Accrued Liability (AAL)</b>	<b>\$ 7,594,463</b>	<b>\$ 7,788,996</b>			
<b>Actuarial Value of Assets at beginning of year</b>	<b>\$ 3,513,466</b>	<b>\$ 4,810,526</b>			
<b>Unfunded Actuarial Accrued Liability (UAAL)</b>	<b>\$ 4,080,997</b>	<b>\$ 2,978,470</b>			
<b>Remaining Amortization Period</b>	<b>25</b>	<b>24</b>			
Normal Cost	\$ 157,521	\$ 165,397			
Amortization of UAAL	<u>232,996</u>	<u>\$ 175,067</u>			
Annual Required Contribution (ARC)	\$ 390,517	\$ 340,464			
Annual Required Contribution (ARC)	\$ 390,517	\$ 340,464			
Interest on net OPEB Obligation	(\$ 66,772)	(\$ 129,133)			
Adjustment to ARC	<u>\$ 63,537</u>	<u>\$ 126,502</u>			
<b>Annual OPEB Cost</b>	<b>\$ 387,281</b>	<b>\$ 337,833</b>			
Town Contribution (including benefits paid)	<u>(\$1,426,634)</u>	<u>(\$ 1,093,788)</u>			
Increase in net OPEB Obligation (Asset)	(\$1,039,353)	(\$ 755,955)			
<b>Net OPEB Obligation (Asset) - Beginning of Year</b>	<b>(\$1,112,868)</b>	<b>(\$2,152,221)</b>			
<b>Net OPEB Obligation (Asset) - End of Year</b>	<b>(\$2,152,221)</b>	<b>(\$2,908,176)</b>			
Projected Benefits Paid	\$ 406,634	\$ 413,104			

**Important Note:** The Actuarial Standards Board recently issued a major restatement of ASOP 6. Perhaps the most important change will be the prohibition of using "community rated accounting," which is described at the bottom of page 10. This may result in an as yet unknown, significant increase in accounting costs, probably starting in the 2016/17 fiscal year.