



Item No. 4 Town of Atherton

FINANCE COMMITTEE STAFF REPORT

TO: FINANCE COMMITTEE

FROM: ROBERT BARRON III, FINANCE DIRECTOR

DATE: SEPTEMBER 12, 2017

SUBJECT: REVIEW AND DISCUSS PARS OPEB PRE-FUNDING TRUST PROGRAM REVIEW AND PENSION RATE STABILIZATION PRESENTATION BY PARS AND HIGH MARKET CAPITAL INVESTMENTS OF FUNDS; IF APPROPRIATE MAKE RECOMMENDATION ON INVESTMENT STRATEGY

RECOMMENDATION

Review and discuss the OPEB pre-funding trust program yearly review and pension rate stabilization presentation by PARS and High Market Capital investment of funds. If appropriate make recommendation on investment strategy.

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. The Town adopted and entered into an agreement to participate in the PARS (Public Agency Retirement Services) Post-Retirement Health Care Plan Trust Program. The Town of Atherton OPEB Trust Program team consists of PARS, US Bank, and High Mark Capital Management. PARS is the trust administrator and consultant. They provide recordkeeping/sub-trust accounting, trustee and actuarial coordination. PARS also monitors contributions and plan compliance while also serving as ongoing client liaison. U.S. Bank serves as the OPEB plan trustee for the Town. They safeguard the plan assets; provide oversight protection, serves as the plans fiduciary and custodian of assets. High Mark Capital Management is the investment manager of the Trust. They are an investment sub-advisor to U.S. Bank. This OPEB trust team has a multitude of years of corporate experience and currently oversees over 1,125 plans for 600 public agencies.

The town uses the trust to prefund future liability payments of retiree health care costs. There is an accrued actuarial liability that the Town owes based on benefits earned by active and retired

REVIEW AND DISCUSS PARS OPEB PRE-FUNDING TRUST YEARLY REVIEW

September 12, 2017

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employees. 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 recent OPEB Actuarial refresh as of July 1, 2016, the OPEB Liability was estimated as follows:

As of 7/1/2016	
Active Employees	\$1,782,870
Retirees Spouses	\$7,125,542
Accrued Actuarial Liability (AAL)	\$8,908,412
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)
ERAF Contribution FY 17/18 September 2017	(\$92,118)
Estimated Unfunded Actuarial Liability Amount	\$3,816,294

The Accrued Actuarial Liability (AAL) of \$8.9 Million represents only the *explicit subsidy* of the accrued liabilities for the Town OPEB. This is the representation of the amount of cash we need today to fund expected health costs for all earned benefits for past and current staff. The Town had set a funding target of up to \$5 Million into the OPEB trust. With the recent OPEB actuarial report as of July 1, 2016 the Finance Committee made a recommendation to City Council to contribute \$92,118 to the trust in the FY 2017/18 budget. The Town trust in 2017 will have a balance of \$5,092,118 in the trust. Based on the OPEB Actuarial report for the Town's postemployment health care program, the Town has approximately funded 72% of the accrued actuarial liability for retirees and spouses.

The updated OPEB actuarial report showed an increase to the total AAL by \$1,449,168. Increases are due to expected cost of benefits, mortality changes, actual demographics and experience. The illustration below is based on the *explicit subsidy* of the report.

Actuarial Report	As of July 1, 2014	As of July 1, 2016
Active Employees	\$1,851,691	\$1,782,870
Retirees Spouses	\$5,607,553	\$7,125,542
Accrued Actuarial Liability (AAL)	\$7,459,244	\$8,908,412

As was previously discussed in prior Finance committee meetings, there were changes in actuarial reporting due to the upcoming implementation of GASB 75 at the end of fiscal year 2017/18. The major difference in the report was the inclusion of the *implicit subsidy, a conditional liability based on actual medical costs incurred by Town census of retirees*. Our current costs are based on community rated health plans by CalPERS and as such is what our AAL Liability is based. The Town is currently working with GovInvest to perform an OPEB actuarial for implementation of GASB 75 as of July 1, 2017. This implementation includes

REVIEW AND DISCUSS PARS OPEB PRE-FUNDING TRUST YEARLY REVIEW

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listing the OPEB unfunded liability on the Town balance sheet. Staff will bring back the updated actuarial to the committee sometime next year. Once the new actuary is completed, there could be a potential recommendation for additional contribution to the Trust. The Town is in a positive funding status as the OPEB liability is approximately 57 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 both 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 recommended to maintain this investment strategy.* High Market Capital handles the investment management of the funds in the PARS trust. There are five diversified investment strategies to choose from:

Conservative
Moderate Conservative
Moderate
Balanced
Capital Appreciation

The long term outlook for the Town is to prefund our OPEB liabilities in order to pay the present and future obligations of OPEB benefits to retirees. In a matter of five years we have contributed \$5.09 Million towards the Trust. One of the Council’s core strategies is financial stability, and this includes the paying down of long term liabilities. Our current investment risks on the assets is that of 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 committee if appropriate, can make a recommendation to the City Council to change the Town investment strategy.* The current strategy has been in place since the Town opened the PARS OPEB Trust.

Moderate Index PLUS Investment Strategy

Beginning Balance as of July 1, 2016	Additional Contributions	Trust Earnings Minus expenses	Ending Balance as of July 1, 2017
\$5,405,489		\$450,144.79	\$5,855,634

Attached is also the PARS annual account report for the Trust from the period 7/1/2016 to 7/1/2017

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 \$390,058 were made in the year for retiree health and equates to \$390,068 in distributions. The pay as you go for retiree health is a budget expense in the Town operating budget. The OPEB Trust has earned \$855,634 since inception or 17.1 percent.

REVIEW AND DISCUSS PARS OPEB PRE-FUNDING TRUST YEARLY REVIEW

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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 Town's strategy. Jennifer Meza of PARS is here as well to discuss the pre-funding program and a new pension rate stabilization trust program available for municipalities. 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

Page 1 of the Atherton Actuarial Valuation of Postemployment Health Care Program

TOWN OF ATHERTON
PARS OPEB Trust Program

Account Report for the Period
7/1/2016 to 6/30/2017

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 6/30/2017
OPEB	\$5,405,489.84	\$390,058.22	\$484,091.43	\$33,936.66	\$390,068.20	\$0.00	\$5,855,634.63
Totals	\$5,405,489.84	\$390,058.22	\$484,091.43	\$33,936.66	\$390,068.20	\$0.00	\$5,855,634.63

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	
0.53%	2.44%	8.98%	4.52%	-	-	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, Trustee and Investment Management fees

SECTION I

Summary of Valuation Results

Table 1-1 Summary of Valuation Results		
	<u>7/1/2016</u>	<u>7/1/2014</u>
Present Value of Future Benefits		
Active	\$5,189,359	\$3,135,237
Retiree	<u>\$9,380,054</u>	<u>\$5,607,553</u>
Total	\$14,569,413	\$8,742,790
Actuarial Accrued Liability		
Active	\$2,775,369	\$1,851,691
Retiree	<u>\$9,380,054</u>	<u>\$5,607,553</u>
Total	\$12,155,423	\$7,459,244
Actuarial Value of Assets	\$5,405,490	\$3,513,466
Unfunded Actuarial Accrued Liability	\$6,749,933	\$3,945,778
Expected Employer Share of Current Year Plan Cost (Pay-As-You-Go)	\$464,433 *	\$409,229
Annual Required Contribution	\$668,846	\$367,793
Number of Plan Participants		
Actives	37	35
Retirees and Surviving Spouses	<u>38</u>	<u>36</u>
Total	75	71
Key Assumptions		
Discount Rate	6.00%	6.00%
Initial Trend Rate: Pre-65	8.00%	6.40%
Initial Trend Rate: Post-65	5.50%	6.40%
Ultimate Trend Rate	5.00%	5.00%
Year Ultimate Trend Rate Reached	2030	2021

*Excludes implicit subsidy related to retiree premiums (since unadjusted premiums represent the current cash cost) and the implied subsidy related to active employee premiums (but the Town can elect to recognize this as a retiree cash cost under GASB 45).



TOWN OF ATHERTON

OPEB Prefunding Trust Program Client Review &
Pension Rate Stabilization Program (PRSP)

September 12, 2017

PUBLIC
AGENCY
RETIREMENT
SERVICES

PARS

TRUSTED SOLUTIONS. LASTING RESULTS.

CONTACTS

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OPEB/PENSION PROGRAM TEAM



Trust Administrator & Consultant	Trustee	Investment Manager
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- Recordkeeping/sub-trust accounting
- Actuarial coordination
- Monitor contributions/process disbursements
- Monitor plan compliance
- Ongoing client liaison

- Safeguard plan assets
- Oversight protection
- Plan fiduciary
- Custodian of assets

- Investment sub-advisor to U.S. Bank
- Open architecture
- Investment strategy and asset allocation development
- Investment policy assistance

Corporate Experience

33 years (1984 – 2017)

154 years (1863 – 2017)

98 years (1919 – 2017)

Plans Under Administration

1,600+ plans, 850+ public agencies, 400,000+ participants

Dollars under Administration

Over \$2.4 billion

Over \$4 trillion

Over \$15.9 billion under management



SUMMARY OF AGENCY'S OPEB PLAN

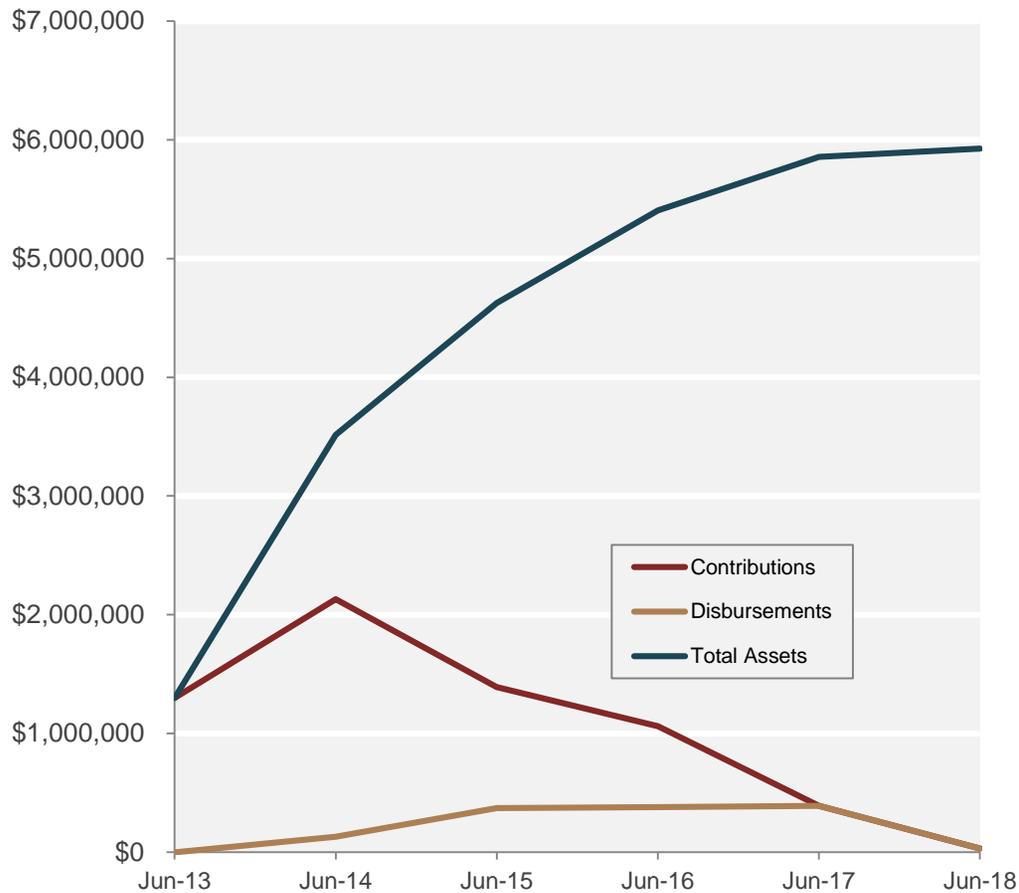
Plan Effective Date:	IRC Section 115 Irrevocable Exclusive Benefit Trust
Trustee Approach:	Discretionary
Plan Effective Date:	May 16, 2012
Plan Administrator:	George Rodericks – Town Manager
Plan Contact:	Robert Barron III – Finance Director
Current Investment Strategy:	Moderate (Passive) Strategy; Pooled Account

AS OF JULY 31, 2017:

Initial Contribution:	June 2013: \$1,299,316
Additional Contributions:	\$5,004,036
Total Contributions:	\$6,303,352
Disbursements:	\$1,302,234
Total Investment Earnings:	\$1,025,795
Account Balance:	\$5,925,282

SUMMARY OF AGENCY'S OPEB PLAN

CONTRIBUTIONS, DISBURSEMENTS, AND TOTAL ASSETS AS OF JULY 31, 2017:



Plan Year Ending

Year	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	\$390,058	\$390,068	\$5,855,635
Jun-18*	\$32,014	\$32,014	\$5,925,282

*Plan Year Ending June 2018 is based on 1 month of activity

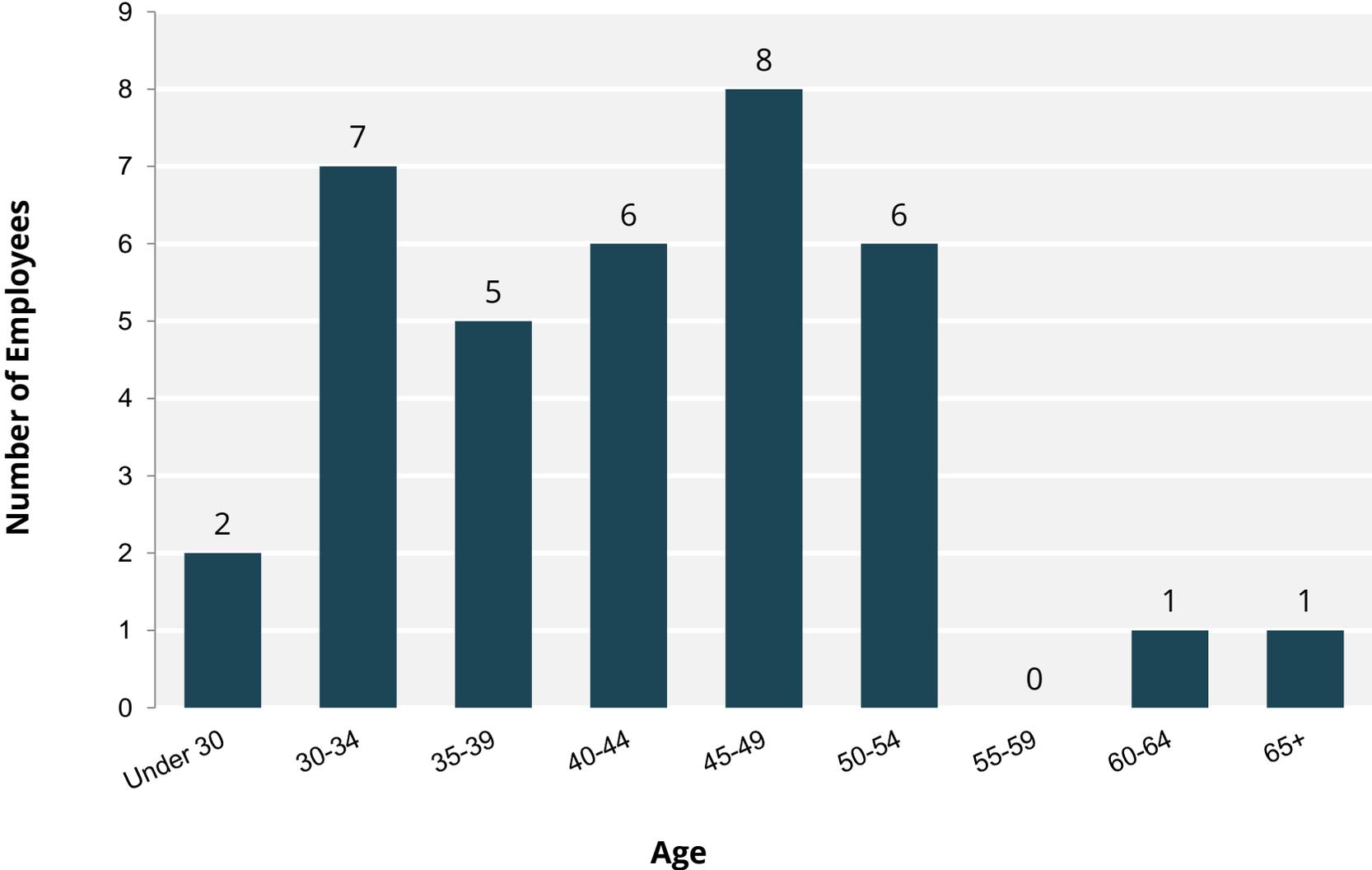
OPEB ACTUARIAL RESULTS

- We have received the actuarial report by Nicolay Consulting Group dated November 12, 2014 with a valuation date as of July 1, 2014. In the table below, we have summarized the results.

Demographic Study	Valuation Date: January 1, 2009	Valuation Date: July 1, 2014
Actives	51	36
Retirees	18	36
Total	69	72

OPEB ACTUARIAL RESULTS

ACTIVE AGE DISTRIBUTION



OPEB ACTUARIAL RESULTS

	Pay-as-you-Go Discount Rate: 4.00% January 1, 2009	Prefunding Discount Rate: 6.00% July 1, 2014
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*
Annual Benefit Payments (Pay-as-you-Go)	\$243,694	\$432,333**

Rule of thumb: For every one percent increase in the discount rate, the unfunded liability is lowered by 10-12%.

* 2015-2016

** 2016-2017 FY

HIGHMARK CAPITAL INVESTMENT REVIEW

Town of Atherton

September 12, 2017

**Presented by
Andrew Brown, CFA**

DISCUSSION HIGHLIGHTS – Town of Atherton OPEB

Asset Allocation: PARS/PRHCP Moderate Index Plus

Allocation Target – 50% stocks (40-60% range), 46.5% bonds (40-60% range), 3.5% cash (0-20% range)

- Large cap 25%, mid-cap 3.5%, small cap 7.5%, international 12.5%, Real estate 1.5%

Performance: : PARS/PRHCP Moderate Index Plus

(as of 7-31-2017) Gross of Investment management fees, Net of Fund level fees

- 3-months: 2.67%
- Year to date: 6.92%
- 1-Year 7.81%
- 3-Year 5.29%
- ITD (July 2013) 6.68%

- Bonds – rate volatility has increased post Fed rate hike(s)
 - 2 rate hikes this year. -0.61% return for previous 12 months, 2.65% annualized since inception
- Stocks
 - Story of the last 12 months
 - International markets vs. US divergence closing??
 - Domestically valuations are rich
 - REITs lag

Outlook

- GDP 2 – 2.5%, Inflation 1.9%, unemployment 4.5%, 10 year Tsy 2.75%, FED 1 more hike 2017
- Geopolitical - North Korea, Russia, German elections, Brexit
- No Tax deal, negative repercussions.
- FED/Inflation/Valuations

Selected Period Performance
PARS/PRHCP MODERATE, INDEX PLUS
Account 6746019206
Period Ending: 07/31/2017

Sector	3 Months	Year to Date (7 Months)	1 Year	3 Years	Since Inception (49 Months)
Cash Equivalents	.19	.35	.43	.22	.16
<i>Citigroup 3 Month T-Bill Index</i>	<i>.21</i>	<i>.39</i>	<i>.52</i>	<i>.23</i>	<i>.18</i>
Total Fixed Income	.95	2.57	-.61	2.23	2.65
<i>BC US Aggregate Bd Index</i>	<i>1.10</i>	<i>2.71</i>	<i>-.51</i>	<i>2.71</i>	<i>3.00</i>
Total Equities	4.43	11.68	17.06	8.24	11.11
Large Cap Funds	4.14	11.17	16.61	10.70	13.25
<i>S&P 500 Composite Index</i>	<i>4.14</i>	<i>11.59</i>	<i>16.04</i>	<i>10.87</i>	<i>13.46</i>
Mid Cap Funds	3.36	9.06	13.29	9.41	12.41
<i>Russell Midcap Index</i>	<i>3.42</i>	<i>9.58</i>	<i>13.04</i>	<i>9.31</i>	<i>12.33</i>
Small Cap Funds	2.23	5.53	19.56	10.37	12.25
<i>Russell 2000 Index</i>	<i>2.11</i>	<i>5.77</i>	<i>18.45</i>	<i>9.89</i>	<i>11.18</i>
International Equities	6.81	18.60	18.57	2.15	5.49
<i>MSCI EAFE Index</i>	<i>6.47</i>	<i>17.09</i>	<i>17.77</i>	<i>2.79</i>	<i>6.95</i>
<i>MSCI EM Free Index</i>	<i>10.19</i>	<i>25.49</i>	<i>24.84</i>	<i>2.39</i>	<i>5.63</i>
REIT Funds	2.77	3.82	-4.43		
<i>Wilshire REIT Index</i>	<i>2.97</i>	<i>2.94</i>	<i>-4.77</i>	<i>8.66</i>	<i>9.67</i>
Total Managed Portfolio	2.67	6.92	7.81	5.29	6.68

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 August 31, 2017

Current Asset Allocation		Investment Vehicle	
Equity		Range: 40%-60%	49.96%
Large Cap Core	IVV	iShares S&P 500 Index Fund	14.72%
Large Cap Value	IVE	iShares S&P 500 Value Fund	5.95%
Large Cap Growth	IVW	iShares S&P 500 Growth Fund	4.27%
Mid Cap Core	IWR	iShares Russell MidCap Index Fund	3.54%
Small Cap Value	IWN	iShares Russell 2000 Value Fund	3.77%
Small Cap Growth	IWO	iShares Russell 2000 Growth Fund	3.80%
International Core	EFA	iShares MSCI EAFE Index Fund	9.18%
Emerging Markets	VWO	Vanguard FTSE Emerging Markets ETF	3.23%
Real Estate	VNQ	Vanguard REIT ETF	1.48%
Fixed Income		Range: 40%-60%	46.36%
Short-Term	VFSUX	Vanguard Short-Term Corp Adm Fund	6.27%
Intermediate-Term	AGG	iShares Barclays Aggregate Bond Fund	37.64%
Bank Loan	BKLN	PowerShares Senior Loan ETF	2.45%
Cash		Range: 0%-20%	3.67%
	FGZXX	First American Government Oblig Z	3.67%
TOTAL			100.00%

TOWN OF ATHERTON

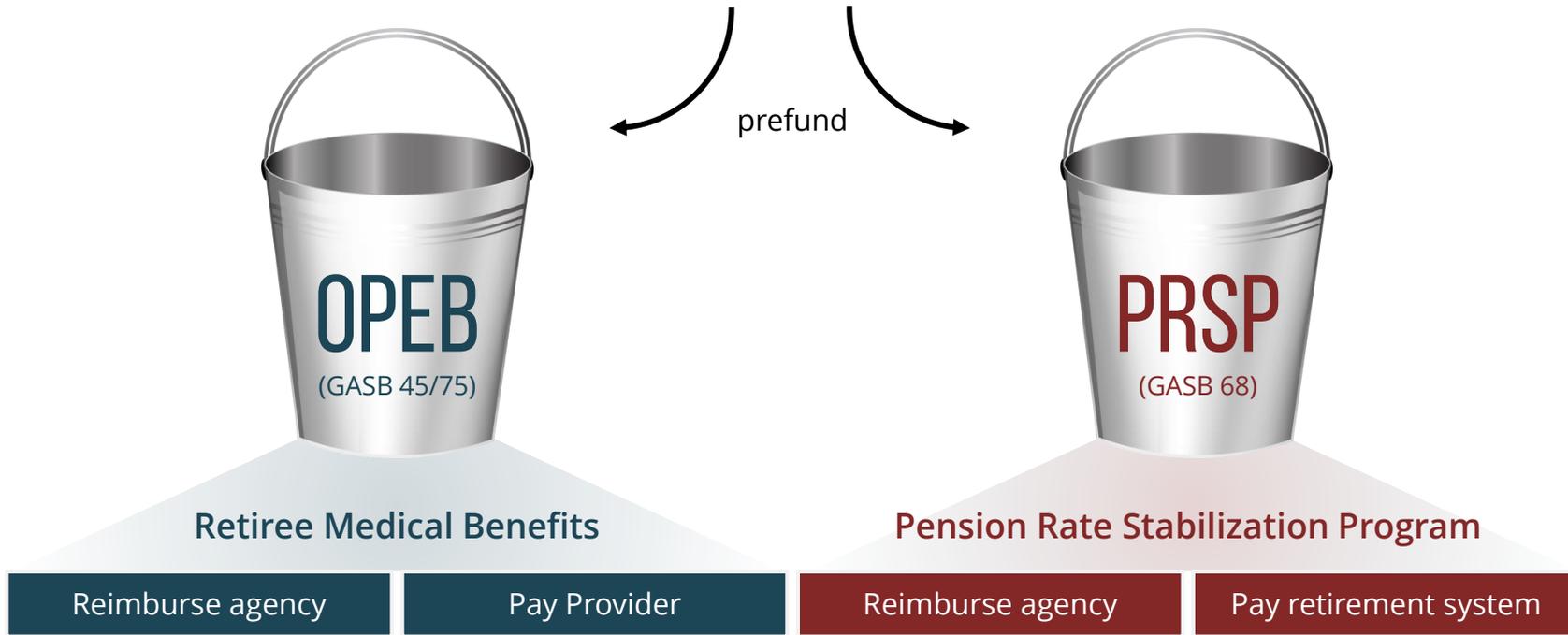
For Period Ending July 31, 2017

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	2.59	5.05	16.16	16.77	12.27	15.20	9.31
iShares S&P 500 Index Fnd	2.05	4.13	11.57	16.00	10.82	14.72	7.69
iShares S&P 500 Value Index	1.36	2.93	6.20	14.15	8.67	13.73	5.66
MID CAP EQUITY FUNDS							
iShares Russell Midcap Index	1.45	3.37	9.46	12.83	9.12	14.81	8.09
SMALL CAP EQUITY FUNDS							
iShares Russell 2000 Value	0.62	0.88	1.14	19.08	9.42	13.65	6.85
iShares Russell 2000 Growth	0.86	3.40	10.97	17.87	10.39	14.73	8.58
INTERNATIONAL EQUITY FUNDS							
iShares MSCI EAFE Index	2.87	6.48	17.12	17.68	2.71	8.97	1.39
Vanguard FTSE Emerging Markets ETF	5.35	7.49	20.85	19.69	1.92	4.32	1.68
REAL ESTATE FUNDS							
Vanguard REIT ETF	1.26	2.73	3.88	-4.66	8.48	9.13	7.18
BOND FUNDS							
iShares Barclays Aggregate Bond	0.43	1.13	2.74	-0.54	2.67	1.96	4.33
Vanguard Short-Term Investment-Grade Adm	0.37	0.73	1.95	1.22	2.06	2.07	3.25
PowerShares Senior Loan Portfolio	0.75	0.87	1.73	4.43	2.12	3.20	--

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 and reliable. Securities are not FDIC insured, have no bank guarantee and may lose value.

THE PARS IRS-APPROVED COMBINATION 115 TRUST



- Assets are sub-accounted for separately
- Pre-fund one now and the other later
- Addresses unfunded liabilities
- Can choose different investment risk tolerance levels for each

- Can access funds at anytime; OPEB for OPEB and pension for pension
- Assets (OPEB and Pension) aggregate and reach lower fees on tiered schedule sooner – saving money!
- No cost to set up; no fees until assets are added

PARS PRSP CLIENT LIST – BAY AREA

CITIES & TOWNS

City of Alameda
City of Brisbane
City of Capitola
City of Daly City
City of Dublin
City of Half Moon Bay
City of Healdsburg
City of Morgan Hill
City of Napa
City of Norwalk
City of Oakley
City of Palo Alto
City of Redwood City
City of Rohnert Park
City of Santa Clara
City of Sausalito
City of Union City
Town of Colma
Town of Los Gatos
Town of Tiburon

COUNTIES

County of Solano

SPECIAL DISTRICTS

Central Contra Costa Sanitary District
Delta Diablo (Sanitation District)
Moraga-Orinda Fire Protection District
Napa County Mosquito Abatement District
Novato Sanitary District
Southern Marin Fire Protection District
West Bay Sanitary District

EDUCATIONAL DISTRICTS

Campbell Union HSD



PENSION FUNDING STATUS

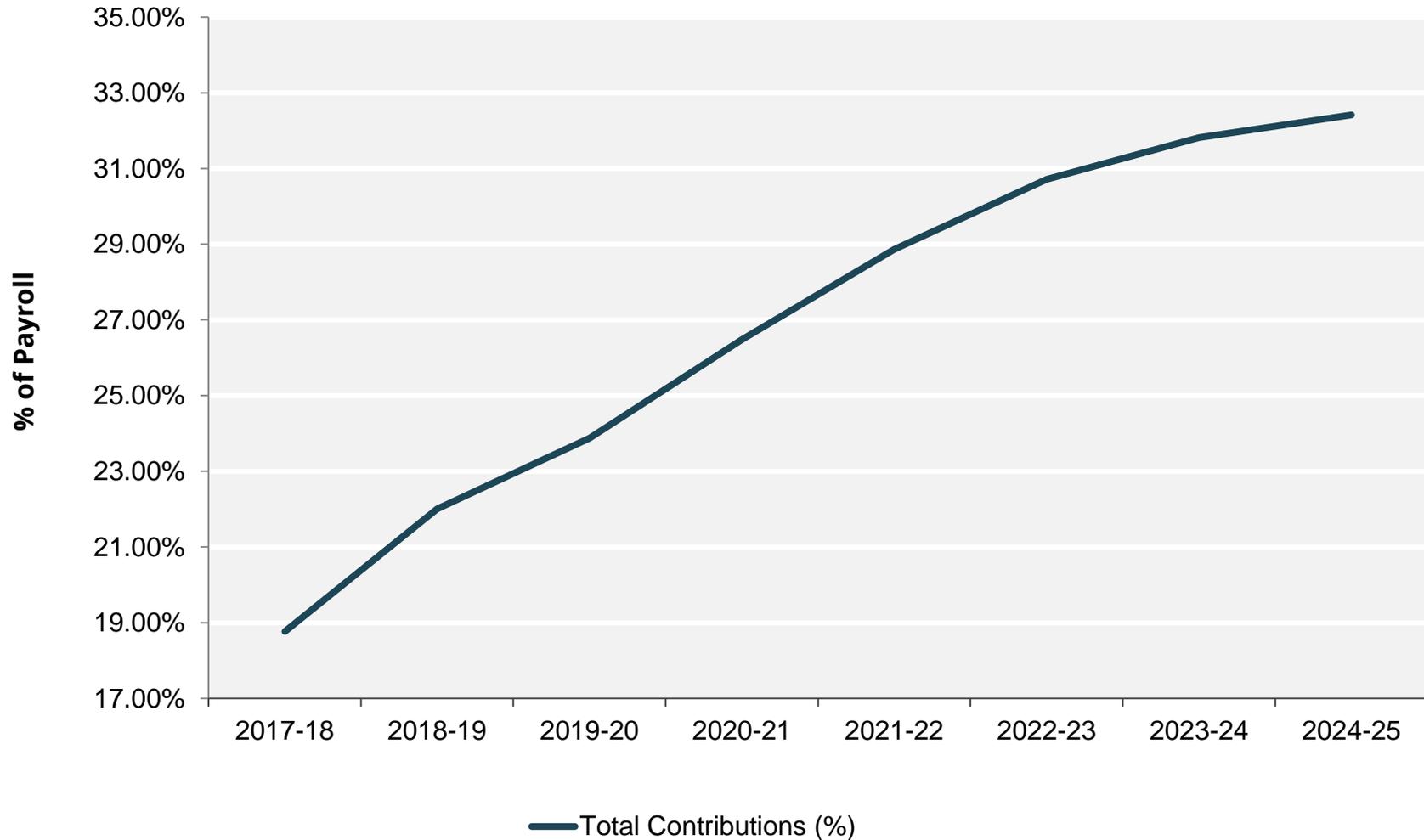
As of June 30, 2016, Town of Atherton's CalPERS pension plan is funded as*:

Actuarial Liability	\$55.2 M
Assets	\$39.6 M
Unfunded Liability	\$15.6 M
Funded Ratio	71.81%
Employer Contribution Amount (FY 17-18)	\$1.4 M
Projected Employer Contribution Amount (FY 24-25)	\$2.8 M (99.40% ↑)

* Data from Agency's 2015-16 CalPERS actuarial valuation

PROJECTED EMPLOYER CONTRIBUTIONS (MISC.)

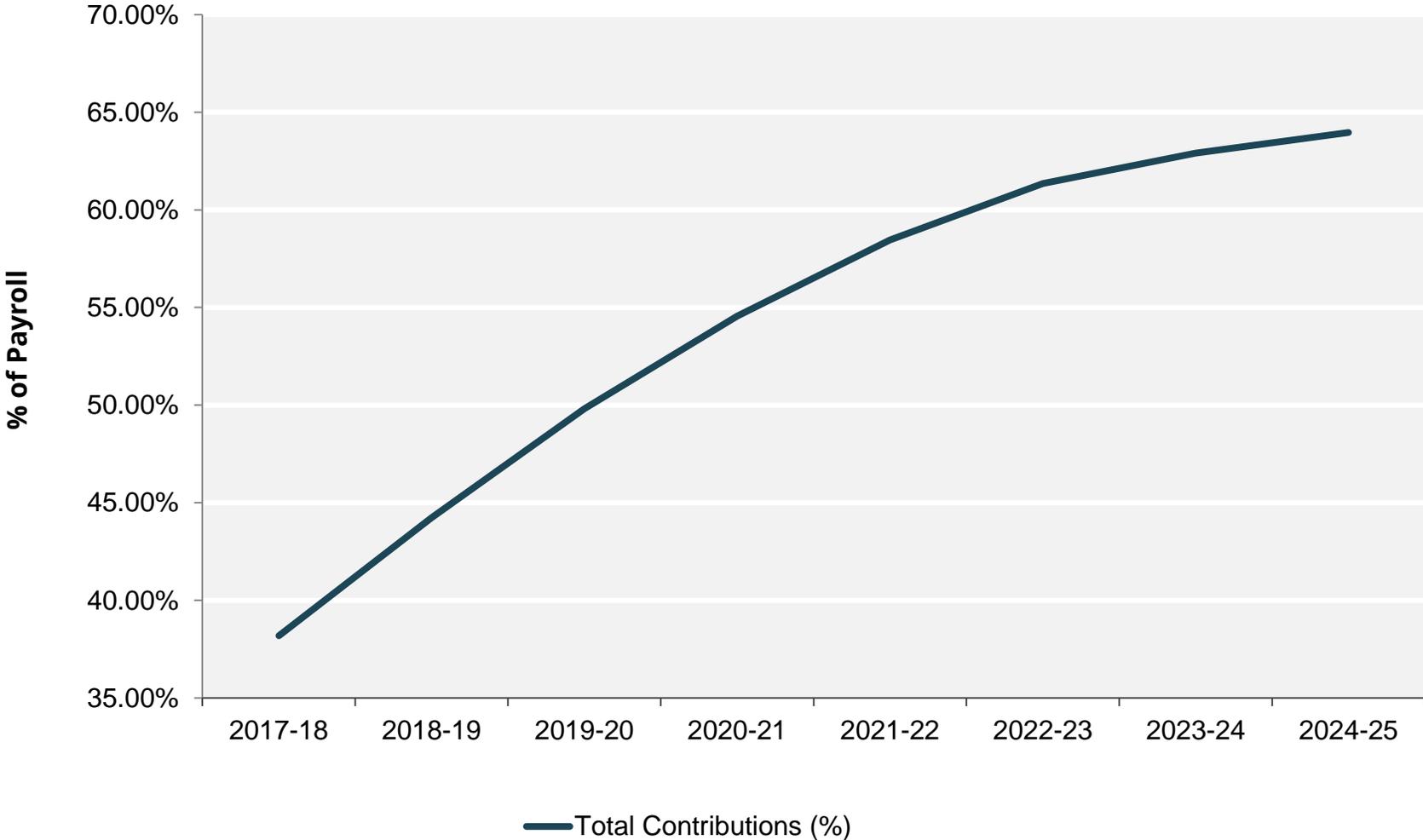
Projected misc. contributions increase from \$0.3 M to \$0.7 M* (108% ↑)



* Data from Agency's 2015-16 CalPERS actuarial valuation

PROJECTED EMPLOYER CONTRIBUTIONS (SAFETY)

Projected safety contributions increase from \$1 M to \$2 M* (96.5% ↑)



* Data from Agency's 2015-16 CalPERS actuarial valuation

WHY PREFUND PENSION IN A SEPARATE TRUST?

- 1 The Town has complete control over contributions and disbursements; timing, amount, and risk tolerance level
- 2 Helps offset pension rate increases or underperformance by retirement system
- 3 Rainy Day Fund: Emergency source of funds when Employer revenues are impaired based on when conditions dictate
- 4 Assets (OPEB and Pension) will aggregate and reach lower fees on tiered schedule sooner – saving money!
- 5 Can use these funds for pension obligations at anytime
- 6 Addresses future pension liabilities
- 7 Can choose less aggressive investment strategy than retirement system
- 8 Diversified Investing/Potential for Greater Return than General Fund