



**TOWN OF LOS GATOS
FINANCE COMMITTEE REPORT**

MEETING DATE: 11/07/2017

ITEM NO: 18

DATE: OCTOBER 31, 2017

TO: MAYOR AND TOWN COUNCIL

FROM: LAUREL PREVETTI, TOWN MANAGER

SUBJECT: REVIEW, DISCUSS, AND CONSIDER THE RECOMMENDATIONS OF THE COUNCIL FINANCE COMMITTEE TO:

- A. ADOPT A RESOLUTION ESTABLISHING THE TOWN COUNCIL AS AN OVERSIGHT COMMITTEE FOR THE TOWN OF LOS GATOS IRS SECTION 115 PENSION TRUST AND CALIFORNIA EMPLOYERS' RETIREE BENEFIT TRUST (CERBT)
- B. ADOPT AN INVESTMENT POLICY FOR THE TOWN OF LOS GATOS IRS SECTION 115 PENSION TRUST AND CERBT

RECOMMENDATION:

Review, discuss, and consider the recommendations of the Council Finance Committee to:

1. Adopt a resolution (Attachment 1) establishing the Town Council as an Oversight Committee for the Town of Los Gatos IRS Section 115 Pension Trust and California Employers' Retiree Benefit Trust (CERBT)
2. Adopt an Investment Policy for the Town of Los Gatos IRS Section 115 Pension Trust and CERBT

BACKGROUND:

At its October 9, 2017 meeting, the Council Finance Committee reviewed and discussed the IRS Section 115 Trust governance. Staff recommended establishing the Town Council as an Oversight Committee for the Town of Los Gatos IRS Section 115 Pension Trust and CERBT, adopting an Investment Policy for the Trust's, adopting asset allocations and establishing Investment Policy Guidelines between the Town and Highmark Capital the Trust fiduciary. Committee discussion focused on the oversight board formation, investment policy adoption, and possible asset allocations. The Committee acted to move two recommendations forward

PREPARED BY: STEPHEN CONWAY
FINANCE DIRECTOR

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

BACKGROUND (cont'd):

to the Town Council for consideration at the November 7, 2017 Town Council meeting. The Finance Committee requested additional information and additional time for further discussion related to possible asset allocation and establishing corresponding guidelines with Highmark Capital. The next Council Finance Committee meeting is scheduled for December 4, 2017.

DISCUSSION:

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 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:

DISCUSSION (cont'd):

“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.”

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 2). 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 2). This DISCUSSION (cont'd):

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.

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

The draft Policy contained in Attachment 2 reflects the input from the Council Finance Committee as depicted as redline additions.

CONCLUSION AND STAFF RECOMMENDATION:

Staff recommends that the Town Council accept the following recommendations from the Finance Committee:

1. Establishing the Town Council as the Oversight Committee for the Town of Los Gatos IRS Section 115 Pension Trust and CERBT; and
2. Adopting an Investment Policy for the Town of Los Gatos IRS Section 115 Pension Trust and California Employers' Retiree Benefit Trust (CERBT);

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SUBJECT: REVIEW AND DISCUSS OVERSIGHT BOARD, INVESTMENT POLICY

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Attachments:

1. Draft Resolution Establishing the Oversight Committee for the Town of Los Gatos IRS Section 114 Pension Trust and California Employers' Retiree Benefit Trust (CERBT)
2. Draft IRS 115 Pension and OPEB Trust Assets Investment Policy