

**INVESTMENT POLICY STATEMENT**

**FOR**

**CITY OF SUNNYVALE**

**OTHER POST-EMPLOYMENT BENEFITS TRUST**

# TABLE OF CONTENTS

<u>SECTION</u>	<u>PAGE</u>
Purpose .....	<u>13</u>
Investment Authority .....	<u>13</u>
Statement of Investment Objectives .....	<u>24</u>
Investment Guidelines .....	<u>24</u>
Time Horizon	
Liquidity and Diversification	
Asset Allocation	
Rebalancing Philosophy	
Risk Tolerance	
Performance Expectations	
Selection of Investment Managers.....	<u>56</u>
Guidelines for Portfolio Holdings .....	<u>57</u>
Direct Investments by Advisor	
Limitations on Managers' Portfolios	
• <del>Equities</del>	
• <del>Fixed Income</del>	
• <del>Alternatives</del>	
• <del>Cash Equivalents</del>	
Portfolio Risk Hedging	
Prohibited Portfolio Investments	
Safekeeping	
Control Procedures .....	<u>89</u>
Review of Investment Objectives	
Review of Investment Performance	
Voting of Proxies	
Adoption of Investment Policy Statement.....	<u>940</u>



The City of Sunnyvale, California (the “City”) has established the City of Sunnyvale Other Post-Employment Benefits Trust (the “Trust”). The Trust is intended to provide for funding of non-pension post-employment benefits (“OPEB”) for employees who meet the age and service requirements outlined in the City’s plan documents. The Trustees of the Trust hereby adopt this Investment Policy Statement (“Policy Statement”) for the following purposes.

### **Purpose**

The main investment objective of the Trust is to achieve long-term growth of Trust assets by maximizing long-term rate of return on investments and minimizing risk of loss to fulfill the City’s current and long-term OPEB obligations.

The purpose of this Policy Statement is to achieve the following:

1. Document investment objectives, performance expectations and investment guidelines for Trust assets.
2. Establish an appropriate investment strategy for managing all Trust assets, 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 Trust.
3. Establish investment guidelines to control overall risk and liquidity.
4. Establish periodic performance reporting requirements that will effectively monitor investment results and ensure that the investment policy is being followed.
5. Comply with all fiduciary, prudence, due diligence and legal requirements for Trust assets.

### **Investment Authority**

The City oversees certain policies and procedures related to the operation and administration of the Trust. The City will have authority to implement the investment policy and guidelines in the best interest of the Trust to best satisfy the purposes of the Trust. In implementing this Policy Statement, the City believes it may delegate certain functions to:

1. An investment advisor (“Advisor”) to assist the City in the investment process and to maintain compliance with this Policy Statement. The Advisor may assist the City in establishing investment policy, objectives, and guidelines; selecting investment managers (“Managers”) or mutual funds and other common investment vehicles as specifically approved by the City from time to time (“Investments”); reviewing Managers and Investments over time; measuring and evaluating performance; and other tasks as deemed appropriate. The Advisor may also select Investments with discretion to purchase, sell, or hold specific securities that will be used to meet the Trust’s investment objectives. Neither the Advisor nor any Manager shall ever take possession of any securities, cash or other assets of the Trust, all of which shall be held by the

custodian. The Advisor will: a) adjust asset allocation for the Fund subject to the guidelines and limitations set forth in this Policy Statement; b) select investment managers (“Managers”) and strategies consistent with its role as a fiduciary; c) monitor and review Managers and measure and evaluate their performance against their peers based upon the performance of the total funds under their direct management; and d) execute other tasks as deemed appropriate in its role as Advisor for Fund assets. Neither the Advisor nor any Manager shall ever take possession of any securities, cash or other assets of the Trust, all of which shall be held by the custodian. The Advisor must be registered with the Securities and Exchange Commission.

2. A custodian to maintain possession of physical securities and records of street name securities owned by the Trust, collect dividend and interest payments, redeem maturing securities, and effect receipt and delivery following purchases and sales, among other duties. The custodian may also perform regular accounting of all assets owned, purchased, or sold, as well as movement of assets into and out of the Trust.
3. A trustee, such as a bank trust department, if the Trust does not have its own Trustees, to assume fiduciary responsibility for the administration of Trust assets; provided, however, that if the City shall have appointed an investment advisor, then any trustee appointed under this paragraph shall have no authority with respect to selection of investments.
4. ~~Additional~~ Specialists such as attorneys, auditors, actuaries, and retirement plan consultants, and others to assist the City in meeting its responsibilities and obligations to administer Trust assets prudently.

### **Statement of Investment Objectives**

The investment objectives of the Trust are as follows:

1. To invest assets of the Trust in a manner consistent with the following fiduciary standards: (a) all transactions undertaken must be for the sole interest of Trust beneficiaries, and (b) assets are to be diversified in order to minimize the impact of large losses from individual investments.
2. To provide for funding and anticipated withdrawals ~~when required or deemed necessary on~~ a continuing basis for payment of benefits and reasonable expenses of operation of the Trust.
3. To ~~conserve and~~ enhance the value of Trust assets in real terms over the long-term through asset appreciation and income generation, while maintaining a reasonable investment risk profile.
4. To minimize principal fluctuations subject to performance expectations over the Time Horizon (as defined below).
5. To achieve a long-term level of return commensurate with contemporary economic conditions and equal to or exceeding the investment objective set forth in this Policy Statement under the section labeled “Performance Expectations”.

## Investment Guidelines

Within this section of the Policy Statement, several terms will be used to articulate various investment concepts. The descriptions are meant to be general and may share investments otherwise considered to be in the same asset class. They are:

“Growth Assets” - a collection of investments and/or asset classes whose primary risk and return characteristics are focused on capital appreciation. Investments within the Growth Assets category can include income and risk mitigating characteristics, so long as the predominant investment risk and return characteristic is capital appreciation. Examples of such investments or asset classes are: domestic and international equities or equity funds and certain real estate investments.

“Income Assets” - a collection of investments and/or asset classes whose primary risk and return characteristics are focused on income generation. Investments within the Income Assets category can include capital appreciation and risk mitigating characteristics, so long as the primary investment risk and return characteristic is income generation. Examples of such investments or asset classes are: fixed-income securities, guaranteed investment contracts and certain real estate investments.

“Real Return Assets” - a collection of investments and/or asset classes whose primary risk and return characteristics are focused on real returns after inflation. Investments within the Real Return category can include inflation protected securities, commodities and certain real estate investments.

### Time Horizon

The Trust’s investment objectives are based on a 20-year-long-term investment horizon (“Time Horizon”) of rolling five years or longer. Interim fluctuations should be viewed with appropriate perspective. The City has adopted a long-term investment horizon such that the risks and duration of investment losses are carefully weighed against the long-term potential for appreciation of assets.

### Liquidity and Diversification

In general, the Trust ~~will generally will may~~ hold ~~some no more than six months of~~ cash, cash equivalent, and/or money market funds for near-term Trust benefits and expenses (the “Trust Distributions”). The City initially expects that it will continue to pay benefits from its ~~general-current~~ funds, but reserves the right to change that procedure at any time with reasonable notice to the Advisor. All remaining assets will be invested in longer-term ~~investmentssecurities~~ and shall be diversified with the intent to minimize the risk of long-term investment losses. Consequently, the total portfolio will be constructed and maintained to provide diversification with regard to the concentration of holdings in individual issues, issuers, countries, governments or industries.

### Asset Allocation

The City believes that to achieve the greatest likelihood of meeting the Trust’s investment objectives and the best balance between risk and return for optimal diversification, assets will be invested in

accordance with the targets for each asset class as follows to achieve an average total annual rate of return that is equal to or greater than the Trust’s actuarial discount rate as described in the section titled “Performance Expectations”.

<u>Asset Classes</u>	<u>Asset Weightings</u>	
	<u>Range</u>	<u>Target</u>
<b>Growth <u>Assets</u></b>		
Domestic Equity	<del>29</del> 5% - <del>49</del> 5%	<del>39</del> 5%
International Equity	<del>19</del> % - <del>41</del> 29%	<del>21</del> 19%
<del>Other</del> <u>Alternatives</u>	<del>0</del> % - <del>20</del> 15%	<del>0</del> %
<b>Income <u>Assets</u></b>		
Fixed Income	<del>20</del> 6% - <del>60</del> 6%	<del>40</del> 6%
<del>Other</del> <u>Cash Equivalent</u>	<del>0</del> % - 20%	<del>0</del> %
 <u>Real Return Assets</u>	 <u>0% - 20%</u>	 <u>0%</u>
 <u>Cash Equivalents</u>	 <u>0% - 20%</u>	 <u>0%</u>

~~It is the City’s intention to systematically migrate the asset allocation of the Trust’s portfolio toward a targeted global asset allocation of 60 percent equities and 40 percent fixed income over a five year period ending June 30, 2016, with appropriate targets and ranges for the various sub-classes shown above to be adjusted periodically upon the advice of the Advisor and approved by the City.~~

The Advisor and each Manager will be evaluated against their peers on the performance of the total funds under their direct management.

#### Rebalancing Philosophy

The asset allocation range established by this Policy Statement represents a long-term perspective. As such, rapid unanticipated market shifts or changes in economic conditions may cause the asset mix to fall outside Policy Statement ranges. ~~When these divergences occur allocations breach the specified ranges,~~ the Advisor will rebalance, and cause the Managers to rebalance; ~~the assets within the specified ranges.~~ The Advisor may also rebalance assets based on market conditions.

#### Risk Tolerance

Subject to investment objectives and performance expectations, ~~the~~The Trust will be managed in a style that seeks to minimize principal fluctuations over the established Time Horizon ~~and that is consistent with the Trust's investment objectives.~~

#### Performance Expectations

Over the long-term, ~~a rolling five years or longer period~~, the performance objective for ~~the~~ Trust will be to achieve ~~a an average total annual rate of return net of fees that is~~ equal to or greater than the Trust's actuarial discount rate, which is expected to ~~be~~ approximately ~~-6.57%~~ hereafter. Additionally, it is expected that the annual rate of return on Trust assets ~~and the future associated actuarial assumptions~~ will be commensurate with the then-prevailing investment environment ~~and asset allocation~~. Measurement of this return expectation will be judged by reviewing returns in the context of industry standard benchmarks, peer universe comparisons for individual Trust ~~i~~Investments and blended benchmark comparisons for the Trust in its entirety.

### Social and Environmental Responsibility

~~The City has a desire to encourage investments that support sound environmental, social and governance (ESG) investing. While the portfolio may not be classified as an ESG portfolio, iInvestments are encouraged in entities that support community well-being through safe and environmentally sound practices and fair labor practices and. Investments are encouraged in entities that support equality of rights regardless of sex, race, age, disability, or sexual orientation is encouraged. Investments are discouraged in entities that manufacture tobacco products, firearms, or nuclear weapons and. Investments are discouraged in entities that are direct or indirect investments to support the production or drilling of fossil fuels.~~

### Selection of Investment Managers

The Advisor shall prudently select appropriate Managers to invest the assets of the Trust. Managers must meet the following criteria:

- ~~— The Manager must be a bank, insurance company, or investment adviser as defined by the Investment Advisers Act of 1940.~~
- The Manager must provide historical quarterly performance data compliant with Global Investment Performance Standards (GIPS®), Securities & Exchange Commission (“SEC”), ~~and~~ Financial Industry Regulatory Agency (“FINRA”) rules, or industry recognized standards, as appropriate.
- The Manager must provide detailed information on the history of the firm, key personnel, support personnel, key clients, and fee schedule (including most favored nation clauses). This information can be a copy of a recent Request for Proposal (“RFP”) completed by the Manager or regulatory disclosure.
- The Manager must clearly articulate the investment strategy that will be followed and document that the strategy has been successfully adhered to over time.
- The investment professionals making the investment decisions must have a minimum of three (3) years of experience managing similar strategies with at their current firm or at a previous firm.
- Where other than common funds such as mutual funds or commingled trusts are utilized, the Manager must confirm receipt, understanding and adherence to this Policy Statement and any investment specific policies by signing a consent form provided to the Manager prior to investment of Trust assets.



## Guidelines for Portfolio Holdings

### Direct Investments by Advisor

Every effort shall be made, to the extent practical, prudent and appropriate, to select iInvestments that have investment objectives and policies that are consistent with this Policy Statement (as outlined in the following sub-sections of the “Guidelines for Portfolio Holdings”). However, given the nature of the iInvestments, it is recognized that there may be deviations between this Policy Statement and the objectives of these iInvestments.

### Limitations on Managers’ Portfolios

#### EQUITIES

No more than the greater of 5%– or the weighting in the relevant index (Russell 3000 Index for U.S. issues and MSCI ACWI ex-U.S. for non-U.S. issues) of the Manager’s total equity portfolio valued at market may be invested in the common equity of any one corporation, ownership of the shares of one company shall not exceed 52% of those outstanding, and not more than 4025% of equity valued at market may be held in any one sector, as defined by the Global Industry Classification Standard (GICS).

Domestic Equities:- Other than the above constraints, there are no quantitative guidelines as to issues, industry or individual security diversification. However, prudent diversification standards should be developed and maintained by the Manager.

International Equities:- The overall non-U.S. equity allocation should include a diverse global mix that is comprised of the equity of companies from multiple regions and sectors.

#### FIXED INCOME

Fixed income securities of any one issuer shall not exceed 5% of thea total bond portfolio at time of purchase. The 5% limitation does not apply to issues of the U.S. Treasury or other Federal Agencies. The overall rating of the fixed income assets as calculated by the Advisor shall be investment grade, based on the rating of one of the SEC’s Nationally Recognized Statistical Rating Organizations (“NRSROs”).

#### OTHER ASSETS/ALTERNATIVES

Alternatives may consist of non-traditional asset classes such as real estate, private equity, and commodities, when deemed appropriate. The total allocation to this category may not exceed 20% of the overall portfolio. Prior to adding an allocation to any of the following asset classes, with the exception of publicly-traded mutual fund vehicles, the Advisor shall receive approval from the City.

~~and assets thought to hedge inflation, as described below, when deemed appropriate.~~

*Hedge Funds:* Primary objective shall be to enhance the risk-return profile of the overall portfolio. This can be accomplished by using a combination of hedge fund strategies that may enhance returns at a reasonable level of risk or reduce volatility while providing a reasonable level of return. These asset classes may differ from traditional public market asset classes due to the use of certain strategies including short-selling, leverage, and derivatives. Hedge funds may also invest across asset classes. The use of direct hedge funds and fund-of-hedge funds are allowed. For purposes of asset allocation targets and limitations, single strategy hedge funds will be categorized under the specific asset class of the fund. For example, a long/short U.S. equity fund will be categorized as “Other” in the Growth Assets category while a long/short credit fund will be categorized as “Other” in the Income Assets category. Multi-strategy hedge funds that cannot be easily categorized under one asset class will be included in “Other” under either the Growth Assets or Income Assets category depending on the risk-return profile of the strategy.

*Private Equity:* Private equity is less liquid than publicly traded equity securities and can provide returns that are greater than what is available in publicly traded markets. The private equity portfolio may include investments in a variety of commingled/partnership and direct investment vehicles including, but not limited to, venture capital, buyout, turnaround, mezzanine, distressed security, and special situation funds. The private equity portfolio is recognized to be long-term in nature and highly illiquid. Due to their higher risk, private equity investments are expected to provide higher returns than publicly traded equity securities. For purposes of asset allocation targets and limitations, these funds will be categorized as “Other” under the Growth Assets category.

Real Estate: Real estate assets will be held only in diversified investments, primarily holding Real Estate Investment Trusts (REITs) ~~and servicing companies, securities and/or non-publicly traded private real estate~~ and shall be diversified across a broad array of property types and geographic locations. Investments of this type are designed to provide a stable level of income combined with potential for price appreciation, particularly in periods of unexpected inflation. For private real estate, the illiquid, long-term nature should be considered. For purposes of asset allocation targets and limitations, publicly traded REITs will be categorized as “Other” under the Growth Assets category. Depending on the investment characteristics of a private real estate fund, the fund will be categorized as “Other” under either the Income Assets category, for example, a core real estate fund, or under the Growth Assets category, for example, an opportunistic real estate fund where capital gains are expected to make up a significant portion of the total return.

Inflation Hedge: Shall consist of pooled vehicles holding among other assets: Treasury Inflation Protected Securities (“TIPS”), commodities or commodity contracts, index-linked derivative contracts certain real estate or real property and the equity of companies in businesses thought to hedge inflation. Inflation hedge assets will be reported in the Real Return Assets category.

#### CASH EQUIVALENTS

Cash equivalents shall be held in funds complying with Rule 2(a)-7 of the Investment Company Act of 1940.

#### Portfolio Risk Hedging

Portfolio investments designed to hedge various risks including volatility risk, interest rate risk, etc. are allowed to the extent that the investments are not used for the sole purpose of leveraging Trust assets. Investments do not create direct portfolio leverage. One example of a hedge vehicle is an exchange traded fund (“ETF”) which takes short positions.

#### Prohibited Investments

Except for purchase within authorized investments, securities having the following characteristics, are not authorized and shall not be purchased: letter stock and other unregistered securities, commodities or commodity contracts ~~where the Trust is a counterparty, short sales, margin transactions, or private placements (with the exception of Rule 144A securities), or venture capital funds, private equity, or hedge funds.~~ Further, derivatives, options, or futures, or any other investment for the sole purpose of direct portfolio leveraging are prohibited. Direct ownership of real estate, natural resource properties such as oil, gas or timber and the purchase of collectibles is also prohibited.

#### Safekeeping

All assets of the Trust shall be held by a custodian approved by the City and in consultation with the Advisor for safekeeping of Trust assets. The custodian shall produce statements on a monthly basis, listing the name and value of all assets held, and the dates and nature of all transactions in accordance with the terms in the Trust Agreement. Investments of the Trust not held as liquidity or investment reserves shall, at all times, be invested in interest-bearing accounts. Investments and portfolio securities may not be loaned.

## **Control Procedures**

### **Review of Investment Objectives**

The Advisor shall review annually and report to the City the appropriateness of this Policy Statement for achieving the Trust's stated objectives. It is not expected that this Policy Statement will change frequently. In particular, short-term changes in the financial markets should not require an adjustment in this Policy Statement.

### **Review of Investment Performance**

The Advisor shall report on a quarterly basis to the City ~~to review~~ the investment performance of the Trust. In addition, the Advisor will be responsible for keeping the City advised of any material change in investment strategy, Managers, and other pertinent information potentially affecting performance of the Trust.

The Advisor shall compare the investment results on a quarterly basis to appropriate peer universe benchmarks, as well as market indices in both equity and fixed income markets. Examples of benchmarks and indexes that will be used include [the Russell 3000 Index for the broad U.S. equity strategies](#); the S&P 500 Index for large cap [U.S. equities](#), Russell 2000 Index for small cap [U.S. equities](#), MSCI [ACWI ex U.S. for broad-based non-U.S. equity strategies](#); MSCI Europe, Australasia, and Far East (EAFE) Index for [developed](#) international equities, Barclays Capital Aggregate Bond Index for fixed income securities, and the U.S. 91 Day T-bill for cash equivalents. [The Russell 3000 Index will be used to benchmark the U.S. equities portfolio; the MSCI ACWI ex-U.S. Index will be used to benchmark the non-U.S. equities portfolio; the Barclays U.S. Aggregate Bond Index will be used to benchmark the fixed-income portfolio. The categories "Other" will be benchmarked against appropriate indices depending on the specific characteristics of the strategies and funds used.](#)

### **Voting of Proxies**

~~The Advisor will vote the shares of the Investments, and Managers will vote securities in the respective portfolio managed by such Managers, consistently with its proxy policy and in the best interest of the Trust.~~ [The City recognizes that proxies are a significant and valuable tool in corporate governance. The voting rights of individual stocks held in separate accounts or collective, common, or pooled funds will be exercised by the investment managers in accordance with their own proxy voting policies. The voting rights of funds will be exercised by the Advisor.](#)



## **Adoption of Investment Policy Statement**

Any changes and exceptions to this Policy Statement will be made in writing and adopted by the City. Once adopted, changes and exceptions will be delivered to each Manager, as appropriate, by the Advisor.

**Approved by the City of Sunnyvale:**

Represented by:

\_\_\_\_\_  
Director of Finance~~Chair~~

\_\_\_\_\_  
Date