

CITY OF SUNNYVALE
RETIREE HEALTHCARE PLAN

Sunnyvale, California

Basic Financial Statements
and Independent Auditor's Report

Fiscal Year Ended June 30, 2017



**CITY OF SUNNYVALE
RETIREE HEALTHCARE PLAN
Basic Financial Statements
and Independent Auditor's Report**
For the Fiscal Year Ended
June 30, 2017



Sunnyvale

City of Sunnyvale
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Prepared by the Department of Finance
Timothy J. Kirby, Director of Finance

CITY OF SUNNYVALE RETIREE HEALTHCARE PLAN

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Independent Auditor's Report

Honorable Mayor and Members
of the City Council
City of Sunnyvale, California

Report on the Financial Statements

We have audited the accompanying financial statements of the City of Sunnyvale Retiree Healthcare Plan (Plan), a trust fund of the City of Sunnyvale (City), as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the Plan's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Plan as of June 30, 2017, and the respective changes in financial net position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

As described in Note 1, the financial statements present only the Plan and do not purport to, and do not, present fairly the financial position of the City as of June 30, 2017 and changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Also discussed in Note 1 to the financial statements, effective as of July 1, 2016, the Plan adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other than Pension Plans*. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, the Schedule of Changes in the City's Net OPEB Liability and Related Ratios, the Schedule of City Contributions, and the Schedule of Investment Returns as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Macias Gini & O'Connell LLP

Walnut Creek, California
December 4, 2017

Management's Discussion and Analysis (Unaudited)

Management's Discussion and Analysis (Unaudited)
Fiscal Year Ended June 30, 2017

The City of Sunnyvale Retiree Healthcare Plan, commonly referred to as the OPEB (other post-employment benefits) Plan, is administered through a trust that meets the following criteria: 1) contributions from the employer and earnings on those contributions are irrevocable; 2) plan assets are dedicated to providing retiree healthcare in accordance with benefit terms; and, 3) plan assets are legally protected from the creditors of the City and of the OPEB Plan members.

This section of management's discussion and analysis provides an overview of the financial performance for the fiscal year ended June 30, 2017. The information presented here should be read in conjunction with the historical information presented by the accompanying basic financial statements, notes to the basic financial statements, and required supplementary information presented in this report. Certain forward-looking information, which by nature is subject to risks and uncertainties, is presented toward the end of this section.

A. FINANCIAL HIGHLIGHTS.

- On July 1, 2016, the Plan adopted Governmental Accounting Standard Board (GASB) Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. The fiduciary net position on that date was restated at \$71.3 million, reflecting the cumulative effect of applying GASB Statement No. 74.
- At June 30, 2017, the Plan's fiduciary net position was \$83 million, which was an increase of \$11.7 million from the prior year.
- Total benefit payments (including estimated implied subsidy of \$1.3 million for the non-Medicare eligible retirees) amounted to \$6.9 million, which were paid by the City's own resources outside of the trust assets in this Plan.

B. OVERVIEW OF FINANCIAL STATEMENTS AND ACCOMPANYING INFORMATION

The basic financial statements consist of a statement of fiduciary net position and a statement of changes in fiduciary net position. The information about the assets, liabilities, fiduciary net position, and changes in the fiduciary net position presented in these statements helps to determine how the trustees and administrators have discharged their fiduciary responsibilities.

Fiduciary net position restricted for retiree healthcare benefits increased \$11.7 million from the prior year. The City prefunded \$4.2 million to the OPEB Trust in addition to making benefit payments (with implied subsidy) of \$6.9 million from its own resources. The Plan earned net investment income of \$7.5 million in this year.

The comparative schedules of fiduciary net position and changes in fiduciary net position as of and for the fiscal years ended 2017 and 2016 are presented as follows:

Management's Discussion and Analysis (Unaudited), Continued
Fiscal Year Ended June 30, 2017

B. OVERVIEW OF FINANCIAL STATEMENTS AND ACCOMPANYING INFORMATION
(Continued)

Fiduciary Net Position

(Amounts in Thousands)

	2017	2016 ¹	Increase/ (Decrease)
Assets:			
Cash and Cash Equivalents	\$ 233	\$ 165	\$ 68
Investments	82,811	71,144	11,667
Total Assets	<u>83,044</u>	<u>71,309</u>	<u>11,735</u>
Liabilities:			
Investment Fees Payable	36	32	4
Total Liabilities	<u>36</u>	<u>32</u>	<u>4</u>
Net Position:			
Restricted for Retiree Healthcare	<u>\$ 83,008</u>	<u>\$ 71,277</u>	<u>\$ 11,731</u>

Changes in Fiduciary Net Position

(Amounts in Thousands)

	2017	2016 ¹	Increase/ (Decrease)
Additions:			
Employer Contributions ²	\$ 11,170	\$ 10,980	\$ 190
Net Investment Income	7,488	1,346	6,142
Total Additions	<u>18,658</u>	<u>12,326</u>	<u>6,332</u>
Deductions			
Benefit Payments ²	<u>6,927</u>	<u>5,404</u>	<u>1,523</u>
Increase (Decrease) in Net Position	11,731	6,922	4,809
Net Position - Beginning	<u>71,277</u>	<u>64,355</u>	<u>6,922</u>
Net Position - Ending	<u>\$ 83,008</u>	<u>\$ 71,277</u>	<u>\$ 11,731</u>

¹ The Plan did not issue a standalone report for fiscal year 2016. Neither was the implied subsidy amount available for that year.

² Implied subsidy (outside Trust) of \$1.3 million was first included in Employer Contributions and Benefit Payments starting in fiscal year 2017. This amount was determined by the 6/30/2016 actuarial valuation, which are included in the total OPEB liability rolled forward from the 6/30/2016 valuation to 6/30/2017.

***Management's Discussion and Analysis (Unaudited), Continued
Fiscal Year Ended June 30, 2017***

***B. OVERVIEW OF FINANCIAL STATEMENTS AND ACCOMPANYING INFORMATION
(Continued)***

The notes to the basic financial statements provide information related to assets held in trust and managed by this Plan. Also disclosed is the total OPEB liability for which the OPEB Plan assets are restricted as of the fiscal year-end. The following is a list of items disclosed in the notes to the basic financial statements:

- Summary of significant accounting policies
- Plan descriptions and contribution information
- Investments
- Receivables
- Net OPEB liability of the City, with actuarial methods and assumptions used to measure the total OPEB liability

The required supplementary information presents certain schedules that are essential to understanding the trends by comparing the OPEB information reported for the current year with available data from prior years. The following schedules are presented as required:

- a schedule of changes in the City's net OPEB liability and related ratios
- a schedule of City contributions
- a schedule of investment returns

***Management's Discussion and Analysis (Unaudited), Continued
Fiscal Year Ended June 30, 2017***

C. FORWARD-LOOKING INFORMATION

- For funding purposes, as of June 30 2016, the most recent actuarial valuation date (dated February 1, 2017), the Plan had a 45.9 percent actuarial funded ratio. The actuarial accrued liability for other post-employment benefits (OPEB) was \$158.5 million and the actuarial value of assets was \$72.8 million resulting in an unfunded accrued liability of \$85.7 million.
- As reported in the GASB 74 Report as of June 30, 2017, prepared by actuaries for the Plan, the net position of the fiduciary Plan was 49.7% of the total OPEB liability. The total OPEB liability was \$166.9 million, and the Plan fiduciary net position was \$83.0 million, resulting in a net OPEB liability of \$83.9 million.
- As of June 30, 2016, the most recent actuarial valuation date, the actuarial determined contributions for fiscal year 2018 are \$11.5 million or 12.4%, based on the projected payroll of \$92.5 million. The benefit payments are projected to \$7.5 million, including the implied subsidy of \$1.5 million.
- In fiscal year 2018, the trustees of the Plan intend to amend its investment policy to find the best balance between risk and return for optimal diversification and to modify the targets for each asset class to achieve an average total annual rate of return that is equal to or greater than the Plan's actuarial discount rate. In addition, upon amendment, the Plan investment policy would like to encourage investments that support sound environmental, social and governance investing. Investments are discouraged in entities that manufacture tobacco products, firearms, or nuclear weapons and are direct or indirect investments to support the production or drilling of fossil fuels.
- The current annual contributions of \$4.1 million to prefund the Plan, \$5.9 million for benefit payments (pay-as-you-go basis) and implied subsidy of \$1.5 million totaling to \$11.5 million are budgeted for fiscal year 2018. Projected contributions to the Plan are calculated by the actuaries; these annual contributions are projected to increase to \$35.3 million over the City's 20-year financial plan, covering fiscal periods from 2017 to 2037. These contributions, combined with the projected contributions for retiree medical benefits, are expected to be 95% funded by the end of the 20-year financial plan.

***Management's Discussion and Analysis (Unaudited), Concluded
Fiscal Year Ended June 30, 2017***

D. REQUEST FOR INFORMATION

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the Plan's finances and to demonstrate the Plan's accountability for the funds it receives. If you have questions about this report or need additional financial information, contact the Finance Department of the City of Sunnyvale, 650 W. Olive Avenue, Sunnyvale, California 94086.

Basic Financial Statements

CITY OF SUNNYVALE RETIREE HEALTHCARE PLAN

Statement of Fiduciary Net Position
June 30, 2017

	Other Post-Employment Benefit Trust Fund
Assets	
Cash and Cash Equivalents	\$ 233,375
Interest Receivable	141
Investments at Fair Value:	
Mutual Fund-Fixed Income	30,313,083
Mutual Fund-Equity	52,497,460
Total Investments	<u>82,810,543</u>
Total Assets	<u>83,044,059</u>
Liabilities:	
Investment-Related Fees Payable	<u>36,124</u>
Total Liabilities	<u>36,124</u>
Net Position Restricted for Postemployment Benefits Other Than Pensions	<u><u>\$ 83,007,935</u></u>

See Accompanying Notes to the Basic Financial Statements

CITY OF SUNNYVALE RETIREE HEALTHCARE PLAN**Statement of Changes in Fiduciary Net Position
for the Year Ended June 30, 2017**

	Other Post-Employment Benefit Trust Fund
Additions:	
Employer Contributions - Direct	\$ 4,243,000
Employer Contributions - Outside of OPEB Trust	5,599,297
Employer Contributions - Implied Subsidy	1,328,000
Subtotal - Employer Contributions	11,170,297
Net Investment Income:	
Net Increase in Fair Value of Investments	5,973,954
Interest	1,203
Dividends	1,727,153
Less Investment-Related Expense	(214,535)
Subtotal - Net Investment Income	7,487,775
Total Additions	18,658,072
Deductions:	
Benefit Payments with Implied Subsidy	6,927,297
Total Deductions	6,927,297
Net Increase in Net Position	11,730,775
Net Position Restricted for Retiree Healthcare:	
Net Position, Beginning of Year	-
Cumulative Effect of Applying GASB 74	71,277,160
Beginning of Year, Restated	71,277,160
Net Position, End of Year	\$ 83,007,935

See Accompanying Notes to the Basic Financial Statements

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2017

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Financial Reporting Entity

The City of Sunnyvale provides healthcare benefits to eligible retirees and their dependents through the California Public Employee's Retirement System (CalPERS) healthcare program (PEMHCA). Benefit levels are established through agreements and memorandums of understanding between the City and employees or bargaining units.

To implement a funding plan to address the unfunded liabilities associated with retiree medical benefits, the City of Sunnyvale created an Other Postemployment Benefits (OPEB) Trust. Note 2 provides more detail about the plan administration.

The City of Sunnyvale Retiree Healthcare Plan (the "Plan") is a single-employer defined benefit retiree healthcare plan administered by the City of Sunnyvale through a Trust that meets the criteria in Paragraph 3 of Governmental Accounting Standards Board (GASB) Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*.

The Trust is included as an OPEB Trust Fund in the financial reporting entity of the City of Sunnyvale.

Basic Financial Statements

The Plan's resources are required to be held in trust for the members and beneficiaries of the Plan and, therefore, are accounted for as a Fiduciary Fund - Other Postemployment Benefits Trust Fund.

Measurement Focus

The Plan's financial statements are prepared using the economic resources measurement focus.

Basis of Accounting

The Plan's financial statements are prepared using the accrual basis of accounting. Contributions are recognized in the period in which the contributions are due and the Plan has a legally enforceable right to the resources. Benefits and refunds are recognized when due and payable in accordance with the terms of the Plan.

Cash, Cash Equivalents, and Investments

Cash equivalents include cash on hand, demand deposits, and highly liquid investments with original maturities of three months or less at the time of acquisition.

In accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, highly liquid investments with maturities of one year or less at time of purchase and guaranteed investment contracts are stated at amortized cost. All other investments are stated at fair value. GASB Statement No. 72, *Fair Value Measurement and Application*, defines fair value as the exit price that would be received to sell an investment in an orderly transaction at the measurement date.

Notes to Basic Financial Statements, Continued
Fiscal Year Ended June 30, 2017

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued

In accordance with GASB Statement No. 40, *Deposit and Investment Disclosures (Amendment of GASB No. 3)*, disclosures about deposits and investment risks are reported in the following areas:

- Interest Rate Risk
- Credit Risk
- Concentration of Credit Risk
- Custodial Credit Risk

Administrative Costs

Investment-related fees are disbursed from the Trust. The calculation of fees to compensate the services from the Trust Administrator and the Trustee are specified in the Trust Agreement; these fee expenses - such as investment advisory and management fees and trustee fees - are reported in the additions section of the Plan's statement of changes in fiduciary net position.

The City of Sunnyvale pays for audit costs of the Trust.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from these estimates.

Effects of New Accounting Pronouncements

On July 1, 2016, the Plan adopted GASB Statement No. 74, which addresses reporting by OPEB plans that administer benefits on behalf of governments. The requirements of this Statement will improve financial reporting primarily through enhanced note disclosures and schedules of required supplementary information that will be presented by OPEB plans that are administered through trusts that meet the specified criteria in Paragraph 3 of this Statement. The new disclosure requirements are intended to enhance the decision-usefulness of the OPEB plan financial reports in the following ways:

- Information about measures of net OPEB liabilities will explain how the liabilities changed from year to year;
- Information about net OPEB liabilities, including ratios, will indicate the extent to which the total OPEB liability is covered by the fiduciary net position of the OPEB plan;
- Information about actuarial methods and assumptions used to determine total OPEB liability will enhance the comparability of reported information for similar types of OPEB plans;
- The contribution schedule will provide measures to evaluate decision related to the assessment of contribution rates in comparison with actuarially determined rates;
- New information about rates of return on OPEB plan investments will inform financial report users about the effects of market conditions on the OPEB plan's assets over time and provide information for users to assess the relative success of the OPEB plan's investment strategy and the relative contribution that investment earnings provide to the OPEB plan's ability to pay benefits to plan members when they come due.

Notes to Basic Financial Statements, Continued
Fiscal Year Ended June 30, 2017

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued

In December 2015, the GASB issued Statement No. 79, *Certain External Investment Pools and Pool Participants*. This Statement addresses how certain state and local government external investment pools and participants in external investment pools may measure and report their investments in response to changes contained in an SEC rule that took effect in April 2016. Statement No. 79 replaces the reference in existing GASB literature to Rule 2a7 with criteria that are similar in many respects to those in Rule 2a7. This Statement provides guidance that will allow many pools to continue to qualify for amortized cost accounting. This Statement also establishes additional note disclosure requirements for qualifying pools and pool participants. The requirements of this Statement are effective for reporting periods beginning after June 15, 2015, except for certain provisions on portfolio quality, custodial credit risk, and shadow pricing. Those provisions are effective for the Plan's fiscal year ending June 30, 2017. This Statement did not have a significant impact on the Plan's financial statements.

The Plan is currently analyzing its accounting practices to determine the potential impact on its financial statements for the following GASB statements:

In January 2017, the GASB issued Statement No. 84, *Fiduciary Activities*. The objective of this Statement is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. This Statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities. An activity meeting the criteria should be reported in a fiduciary fund in the basic financial statements. Governments with activities meeting the criteria should present a statement of fiduciary net position and a statement of changes in fiduciary net position. The requirements of this statement are effective for reporting periods beginning after December 15, 2018.

In March 2017, the GASB issued Statement No. 85, *Omnibus 2017*. The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits [OPEB]). For OPEB plan reporting, this Statement addresses issues in presenting payroll-related measures in required supplementary information for purposes of reporting by OPEB plans. The requirements of this statement are effective for reporting periods beginning after June 15, 2017.

Notes to Basic Financial Statements, Continued
Fiscal Year Ended June 30, 2017**NOTE 2 – PLAN DESCRIPTION AND CONTRIBUTION INFORMATION***Plan Administration*

Since 2007, the City of Sunnyvale has set aside funds in the its Employee Benefits Internal Service Fund for meeting future OPEB obligations. On July 20, 2010, Sunnyvale City Council approved an Investment Advisory Agreement with PFM Asset Management, LLC (PFM) to establish and administer the retiree medical trust, a tax-qualified irrevocable trust organized under Internal Revenue Code Section 115 to pre-fund retiree healthcare benefits. On December 7, 2010, Sunnyvale City Council approved a Trust Agreement among the City of Sunnyvale (Employer), PFM (Trust Administrator), and U.S. Bank National Association (Trustee of Trust assets).

Plan Membership at June 30, 2017:

Inactive employees or beneficiaries currently receiving benefits	787
Inactive employees entitled to but not yet receiving benefits	85
Active employees	857
	<u>1,729</u>

Benefits Provided

The Plan provides healthcare benefits to eligible retirees and their dependents through the California Public Employees' Retirement System healthcare program (PEMHCA). PEMHCA requires that medical insurance contributions for retired annuitants paid for by a contracting agency be equal to the medical contributions paid for its active employees. Benefit provisions are established and may be amended through agreements and memorandums of understanding between the City, its non-represented employees, and the unions representing City employees.

The City provides a retiree healthcare stipend equal to the lesser of the medical premium or a dollar limit that varies by employee group (\$438 for SEIU, \$467 for PSOA, \$473 for COA, and \$796 for SEA/Confidential/Management per month at June 30, 2017). The City pays 100% of the medical premium for management employees who retired on or before December 31, 2007 and 100% of the medical premium up to a dollar cap for management employees who retire after December 31, 2007. Management employees appointed on or after July 1, 2007 are subject to a vesting schedule ranging from 50% after 5 years of management service to 100% after 15 years of management service.

The Plan also provides potential retiree medical benefits to all Councilmembers. Councilmembers only receive the benefit if they retire from CalPERS within 120 days of when they leave office with the City. Benefits are subject to change and do not constitute a contract. At June 30, 2017, the monthly City contribution of \$128 represents the PEMHCA required minimum employer contribution amount.

Notes to Basic Financial Statements, Continued
Fiscal Year Ended June 30, 2017**NOTE 2 – PLAN DESCRIPTION AND CONTRIBUTION INFORMATION, Continued****Contributions**

The June 30, 2014 actuarial valuation (finalized on February 4, 2015 - before the Actuarial Standards of Practice requiring the inclusion of implied subsidy in actuarial valuations) set the fiscal year 2017 annually required contribution at \$8,135,000. The June 30, 2016 actuarial valuation estimated the implied subsidy for the fiscal year ended June 30, 2017 to be \$1,328,000, which was presented as both an addition to and a deduction from the net position.

For the fiscal year ended June 30, 2017, the City pre-funded \$4,243,000 to the Trust. The City also contributed \$5,599,297 outside of Trust on a pay-as-you-go basis for current benefit payments and PEMHCA administration expenses. These City contributions are separately identified line items in the City Employee Benefits Internal Service Fund's long-term financial plan, an integral part of the City's annually adopted budget.

NOTE 3 – INVESTMENTS**Investment Policy**

The OPEB Trust Investment Policy was established pursuant to Sunnyvale City Council Policy 7.1E.2.6, "An Actuarial Retiree Medical Reserve will be maintained at a level that is deemed adequate to meet the projected liabilities as determined by an actuarial evaluation."

The Investment Policy Statement for the OPEB Trust was approved by Sunnyvale City Council and adopted on January 12, 2011 and amended on February 25, 2014 to 1) clarify language applicable to each asset class with the objective to take advantage of market opportunity while maintaining a broadly diversified portfolio and 2) make the Investment Policy Statement consistent with current investment language.

To achieve the greatest likelihood of meeting the Trust's investment objectives and the best balance between risk and return for optimal diversification, assets would 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.

Asset Class	Asset Weightings	
	Range	Target
Growth		
Domestic Equity	25% - 45%	35%
International Equity	9% - 29%	19%
Alternatives	0% - 15%	0%
Income		
Fixed Income	26% - 66%	46%
Cash Equivalent	0% - 20%	0%
Total Portfolio		100%

Notes to Basic Financial Statements, Continued
Fiscal Year Ended June 30, 2017**NOTE 3 – INVESTMENTS, Continued**

The asset allocation range established by this Investment Policy represents a long-term perspective. Rapid unanticipated market shifts or changes in economic conditions may cause the asset mix to fall outside Investment Policy Statement ranges. The 2014 Investment Policy intended to achieve a target asset allocation of 60 percent equities and 40 percent fixed income. These allocation targets, not maximum or minimum, are used as a guide so that the City may respond to market conditions as appropriate with these targets in mind.

Fair Value Measurement

GASB Statement No. 72, *Fair Value Measurement and Application*, establishes a hierarchy of inputs to valuation techniques used to measure fair value. The hierarchy has three levels. Level 1 inputs are quoted prices in active markets; Level 2 inputs are significant observable inputs; Level 3 inputs are significant unobservable inputs.

Open-end mutual funds are not subject to categorization by the fair value hierarchical levels. The fair value of an open-end mutual fund is determined by the fund's current share price, which is readily determinable if the fair value per share is determined and published and is the basis for current transactions.

At June 30, 2017, in addition to holding \$233,375 in open-end money market mutual funds (cash equivalents), the Plan had positions in open-end mutual funds as follows:

Investments	06/30/2017	Percentage of
	Fair Value	Fair Value
Mutual Funds-Domestic Equity	\$ 40,087,685	48.4%
Mutual Funds-International Equity	12,409,775	15.0%
Mutual Funds-Fixed Income	30,313,083	36.6%
Total	<u>\$ 82,810,543</u>	<u>100.0%</u>

Notes to Basic Financial Statements, Continued
Fiscal Year Ended June 30, 2017**NOTE 3 – INVESTMENTS, Continued****Risk Disclosure**

Interest rate risk is the risk the changes in interest rates demanded by the market will adversely affect the fair value of an investment. The Plan's interest rate risk disclosure is presented in the following schedule for the fixed-income mutual fund investments:

Fixed-Income Investments	Average Maturity		Total Fair Value
	2 to 5 Years	5 to 10 Years	
Vanguard High Yield Corporate Fund Admiral Shares	\$ 2,716,180	\$ -	\$ 2,716,180
Vanguard Intermediate Investment-Grade Corporate Fund Admiral		10,000,370	10,000,370
Baird Core Plus Bond Fund Class Institutional		10,008,646	10,008,646
Metropolitan West Total Return Bond Fund Class I		7,587,887	7,587,887
Fixed-Income Investments, June 30, 2017	<u>\$ 2,716,180</u>	<u>\$ 27,596,903</u>	<u>30,313,083</u>

Disclosures about credit risk, custodial credit risk, concentration of credit risk do not apply to the Plan's mutual fund investments for the following reasons:

- The various mutual fund investments held by the Plan are not rated by Nationally Recognized Statistical Rating Organizations
- Open-end mutual funds are not evidenced by securities that exist in physical or book entry form
- Open-end mutual funds diversify investments among organizations

Rate of Return

For the year ended June 30, 2017, the annual money-weighted rate of return on investments, net of investment expense, was 10.30 percent. The money-weighted rate of return expresses investment performance (net of investment expense) adjusted for the changing amounts invested monthly.

NOTE 4 – RECEIVABLES

At year end, the Plan reported interest receivable of \$141 from its investments in money market mutual funds.

Notes to Basic Financial Statements, Continued
Fiscal Year Ended June 30, 2017**NOTE 5 – NET OPEB LIABILITY OF THE CITY**

The components of the net OPEB liability of the City at June 30, 2017 were as follows:

Total OPEB Liability	\$ 166,918,000
Plan Fiduciary Net Position	<u>83,007,935</u>
City's Net OPEB Liability	<u>\$ 83,910,065</u>
Plan Fiduciary Net Position as a Percentage of the Total OPEB Liability	49.7%

Actuarial Methods and Assumptions Used to Determine Total OPEB Liability

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Actuarially determined amounts are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. No significant changes in benefits, the covered population or other factors affecting the valuation results have occurred after the most recent, June 30, 2016, actuarial valuation.

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan participants to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations. The actuarial value of assets was determined using techniques that spread the effects of investment gains and losses over a five-year rolling period, resulting in not less than 80% nor more than 120% of market value.

Notes to Basic Financial Statements, Continued
Fiscal Year Ended June 30, 2017**NOTE 5 – NET OPEB LIABILITY OF THE CITY, Continued**

Additional information as of the latest actuarial valuation follows:

Valuation Date	The results of the June 30, 2016 actuarial valuation were rolled forward to June 30, 2017, the Plan's fiscal year-end.
Actuarial Cost Method	Entry age
Amortization Method	Level percentage of payroll
Implied Subsidy	Implied subsidy included for non-Medicare eligible retirees (projected benefit payments are based on claim cost or age-adjusted premiums approximating claim costs)
Actuarial Assumptions:	
Discount Rate	6.5% - full actuarially determined contribution funding
Expected Long-Term Rate of Return	6.5%, net of plan investment expenses, including inflation
Inflation	3% annually
Payroll Growth	3.25% annually, including inflation
Cap increase on benefit payments	0% to 5% depending on bargaining unit
Medical Trend	6.5% to 5% over a 4-year period for retirees not eligible for Medicare. 6.7% to 5% over a 4-year period for retirees eligible for Medicare.
Mortality	CalPERS 1997-2011 Experience Study, Mortality Improvement Scale MP-2014 modified to converge to ultimate mortality improvement rates in 2022

Notes to Basic Financial Statements, Continued
Fiscal Year Ended June 30, 2017**NOTE 5 – NET OPEB LIABILITY OF THE CITY, Continued**

The expected nominal long-term rate of return was derived from stochastic projections of expected long-term real rates of return net of investment expenses under various economic scenarios using expected geometric real rates of return and correlation for fund asset classes plus inflation. Best estimates of arithmetic real rates of return for each major asset class included in the target asset allocation as of June 30, 2017 are summarized in the following table:

Asset Class	Expected Geometric Real Return *
Growth Assets	
Domestic Equity	5.35%
International Equity	5.35%
Alternatives	
Real Estate	4.03%
Commodities	1.90%
TIPS	1.53%
Income Assets	
Fixed Income	1.55%
Cash Equivalent	0.00%
Assumed Long-Term Rate of Inflation	3.00%
Assumed Long-Term Investment Expenses	0.30%
Expected Long-Term Net Rate of Return	6.50%

* Based on adjusted capital market assumptions used by CalPERS' investment advisors in May 2010.

Discount Rate

The discount rate used to measure the total OPEB liability was 6.5 percent. The projection of cash flows used to determine the discount rate assumed that City contributions will be made at rates equal to the actuarially determined contribution rates. Based on those assumptions, the OPEB plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on OPEB plan investments was applied to all periods of projected benefit payments to determine the total OPEB liability.

Notes to Basic Financial Statements, Concluded
Fiscal Year Ended June 30, 2017

NOTE 5 – NET OPEB LIABILITY OF THE CITY, Continued

Sensitivity of the Net OPEB Liability to Changes in the Discount Rate

The following presents the net OPEB liability of the City, as well as what the City's net OPEB liability would be if it were calculated using a discount rate that is 1-percentage-point lower (5.5 percent) or 1-percentage-point higher (7.5 percent) than the current discount rate:

	Discount Rate -1% (5.5%)	Current Discount Rate (6.5%)	Discount Rate +1% (7.5%)
Net OPEB Liability	\$ 108,431,065	\$ 83,910,065	\$ 64,057,065

Sensitivity of the Net OPEB Liability to Changes in the Medical Trend Rates

Medical premiums were assumed to increase with a pre-Medicare medical cost increase rate of 6.5% for 2018, grading down to 5% for 2021 and thereafter. The post-Medicare medical cost increase rates were 6.7% for 2018, grading down to 5% for 2021 and thereafter. The following presents the net OPEB liability of the City, as well as what the City's net OPEB liability would be if it were calculated using healthcare cost trend rates that are 1-percentage-point lower or 1-percentage-point higher than the current medial trend rates:

	1% Decrease in Medical Trend Rates	Current Medical Trend Rates	1% Increase in Medical Trend Rates
Net OPEB liability	\$ 68,196,065	\$ 83,910,065	\$ 101,390,065

Required Supplementary Information (Unaudited)

CITY OF SUNNYVALE RETIREE HEALTHCARE PLAN**Required Supplementary Information
Fiscal Year Ended June 30, 2017****SCHEDULE OF CHANGES IN THE
CITY'S NET OPEB LIABILITY AND RELATED RATIOS****Last 10 Years¹**

(Amounts in Thousands)

	2017
Total OPEB liability	
Service Cost	\$ 5,288
Interest	10,076
Benefit Payments	(6,927)
Net change in Total OPEB Liability	8,437
Total OPEB Liability - Beginning	158,481
Total OPEB Liability - Ending (a)	<u>\$ 166,918</u>
 Plan Fiduciary Net Position	
Contributions - Employer	11,170
Net Investment Income	7,488
Benefit Payments	(6,927)
Net Change in Plan Fiduciary Net Position	11,731
Plan Fiduciary Net Position-Beginning	71,277
Plan Fiduciary Net Position-Ending (b)	<u>\$ 83,008</u>
 City's Net OPEB liability (a) - (b)	<u>\$ 83,910</u>
 Plan Fiduciary Net Position as a Percentage of the Total OPEB Liability	49.7%
 Covered-Employee Payroll	\$ 91,394
 City's Net OPEB Liability as a Percentage of Covered Employee Payroll	91.8%

¹ Historical information is required only for measurement periods for which GASB Statement No. 74 is applicable.

CITY OF SUNNYVALE RETIREE HEALTHCARE PLAN

Required Supplementary Information, Continued Fiscal Year Ended June 30, 2017

SCHEDULE OF CITY CONTRIBUTIONS

Last 10 Years¹

(Amounts in Thousands)

	2017	2016	2015	2014	2013	2012	2011 ²
Actuarially Determined Contribution	\$ 8,135	\$ 7,937	\$ 9,758	\$ 9,471	\$ 9,298	\$ 9,024	\$ 14,108
Contributions in Relation to the Actuarially Determined Contribution ³	(9,842)	(9,824)	(10,150)	(9,000)	(9,971)	(8,620)	(36,742)
Contribution Deficiency (Excess)	<u>\$ (1,707)</u>	<u>\$ (1,887)</u>	<u>\$ (392)</u>	<u>\$ 471</u>	<u>\$ (673)</u>	<u>\$ 404</u>	<u>\$ (22,634)</u>
Covered-Employee Payroll	\$ 91,394	\$ 87,488	\$ 86,273	\$ 86,131	\$ 83,623	\$ 84,699	\$ 86,955
Contributions as a Percentage of Covered Employee Payroll	10.8%	11.2%	11.8%	10.4%	11.9%	10.2%	42.3%

¹ Historical information is required only for measurement periods for which GASB Statement No. 74 is applicable.

² The City established the OPEB Trust in fiscal year 2011.

³ The fiscal year 2017 employer contribution was determined as part of the June 30, 2014 valuation.

The June 30, 2014 actuarial valuation was finalized on February 4, 2015, before the revised ASOP 6 went into effect.

ASOP 6 requires implied subsidy valued for community rated plans.

Required Supplementary Information, Concluded
Fiscal Year Ended June 30, 2017

SCHEDULE OF INVESTMENT RETURNS**Last 10 Years**

<u>Year</u>	<u>Annual Money-Weighted Rate of Return, Net of Investment Expense</u>
2017	10.30%

¹ Historical information is required only for measurement periods for which GASB Statement No. 74 is applicable.