



Council Meeting: December 7, 2010

SUBJECT: Approval of Trust Agreement between the City of Sunnyvale, PFM Asset Management, LLC, and U.S. National Bank Association for the Sunnyvale Retiree Medical Trust

BACKGROUND

On July 20, 2010, Council approved the City entering into an Investment Advisory Agreement with PFM Asset Management, LLC (PFM) to serve as the investment manager for the City's retiree medical trust (RTC 10-187). Once that agreement was approved, the next step in the process was to prepare the Trust Agreement (Attachment A) for Council approval, which staff has been working with PFM to develop.

EXISTING POLICY

Fiscal Sub-Element E.2.6: An Actuarial Retiree Medical Reserve will be maintained at a level that is deemed adequate to meet projected liabilities as determined by an actuarial evaluation. This Reserve should meet the GASB reporting requirements for these future costs.

DISCUSSION

Approval of the Trust Agreement is the final step required before the City is able to begin the process of formally funding its Other Post Employment Benefits (OPEB) Trust. The Trust Agreement establishes the relationship, duties, and responsibilities amongst the three parties involved with the Trust: the City (Employer), U.S. Bank National Association (Trustee), and PFM (Trust Administrator). Below is a brief summary of the roles and responsibilities of each of the three parties:

The City (Employer):

- Fund the Trust.
- Determine the amount of benefits to be paid out of the assets of the Trust.
- Select and appoint an accounting firm to audit the Trust annually.

U.S. National Bank Association (Trustee):

- Maintain sole custody of the cash, securities, and other assets of the Trust.
- Execute investment transactions at the written direction of the Trust Administrator.
- Keep accurate and detailed records of all investments, receipts, disbursements, and all other transactions and provide this information to the Trust Administrator and Employer on a quarterly basis.

PFM (Trust Administrator):

- Maintain exclusive authority and responsibility for the investment of Trust assets in permitted investments.
- Reassess and alter, if necessary, the asset allocation of the Trust annually to maintain the established asset allocation ratios.

In addition to the Trust Agreement itself, there are three exhibits to Attachment A: the Investment Advisory Agreement approved on July 20th naming PFM as the City's investment advisor for the Trust (Exhibit A), the memorandum from PFM that contains the asset-liability analysis for the Trust and PFM's asset allocation recommendation (Exhibit B), and the Investment Policy Statement (Exhibit C),

The memorandum from PFM (Exhibit B) contains an analysis of the City's overall OPEB liability based on its most recent actuarial valuation. Based on this analysis, as well as an analysis of the City's risk tolerance that was developed and reviewed with City staff, PFM has recommended an initial asset allocation (50% equities and 50% fixed income) and a long-term asset allocation (60% equities and 40% fixed income by year five). PFM has also recommended a "dollar cost averaging" approach to the initial funding of the Trust to mitigate funding risk from market fluctuations. This strategy recommends funding 25% of the initial planned contribution at the outset, with the remaining 75% invested throughout the remainder of the fiscal year.

The Investment Policy Statement (Exhibit C), which was drafted by PFM with significant input from City staff, is the document that outlines the parameters for meeting the objectives of the Trust. As such, the purpose of the Investment Policy Statement is to achieve the following:

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

FISCAL IMPACT

The City's OPEB liability as of June 30, 2009 was \$92.8 million. The City currently has \$32.8M million set aside in the Employee Benefits Fund for its initial investment into the Trust. The 20-year Long Term Financial Plan includes additional contributions to the Trust through FY 2023/2024. Following this point, the OPEB liability will be funded and the City's costs for retiree medical benefits are expected to slow to a rate that is less than the current "pay as you go" obligations. This is the result of the interest earnings from the initial contributions offsetting the total cost of retiree medical benefits and reducing the annual amount the City needs to contribute. As a result, pre-funding the City's future retiree health benefits costs via the Trust will produce a significant savings over the "pay as you go" method over the long term. These savings have been included in the adopted FY 2010/2011 Budget.

PUBLIC CONTACT

Public contact was made by posting the Council agenda on the City's official-notice bulletin board outside City Hall, at the Sunnyvale Senior Center, Community Center and Department of Public Safety; and by making the agenda and report available at the Sunnyvale Public Library, the Office of the City Clerk and on the City's Web site.

ALTERNATIVES

1. Approve the attached Trust Agreement and authorize the City Manager to sign it as currently presented.
2. Approve the attached Trust Agreement and authorize the City Manager to sign it with modifications.
3. Do not approve the attached Trust Agreement and do not authorize the City Manager to sign it.

RECOMMENDATION

Staff recommends Alternative 1, approve the attached Trust Agreement and authorize the City Manager to sign it as currently presented.

Reviewed by:

Grace Leung, Director of Finance
Prepared by: Drew Corbett, Budget Manager

Approved by:

Gary M. Luebbers
City Manager

Attachments

- A. Trust Agreement between the City of Sunnyvale, PFM Asset Management, LLC, and U.S. National Bank Association
- Exhibit A: Investment Advisory Agreement between the City of Sunnyvale and PFM Asset Management, LLC
 - Exhibit B: City of Sunnyvale OPEB Trust Asset-Liability Analysis and Asset Allocation Recommendation
 - Exhibit C: Investment Policy Statement

POST-EMPLOYMENT WELFARE BENEFITS PROGRAM TRUST

By and among

City of Sunnyvale

PFM ASSET MANAGEMENT LLC,
as Trust Administrator

and

U.S. Bank,
as Trustee

Dated _____, 2010

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POST-EMPLOYMENT WELFARE BENEFITS PROGRAM TRUST

This Trust Agreement is made this _____ day of _____, 2010 (this “Agreement”), among City of Sunnyvale (“Employer”), U.S. BANK NATIONAL ASSOCIATION (together with any successor trustee hereunder, “Trustee”) and PFM ASSET MANAGEMENT LLC (together with any successor trust administrator hereunder, “Trust Administrator”);

W I T N E S S E T H:

WHEREAS, Employer wishes to provide for retiree health benefits and other post-employment benefits other than pension benefits (“OPEB”) (“Benefits”) for employees and other participants (all collectively referred to herein as “Beneficiaries”) as and to the extent provided in its benefit plans attached to this Agreement as Exhibit A, as amended or supplemented from time to time (“Plans”) and as described in Section I, below; and

WHEREAS, Employer and Trustee desire to establish a trust (“Trust”), which will be an entity separate from Employer for the exclusive purpose of providing funds to pay Benefits, with the intent that (i) the income of the Trust will be exempt from federal and state income tax (under Internal Revenue Code Section 115 with respect to federal income tax), (ii) transfers to the Trust will not be taxable to Beneficiaries, (iii) the Trust will qualify for purposes of Governmental Accounting Standards Board Statement 45 (“GASB 45”) pursuant to GASB 45, and (iv) all assets of the Trust are and will be irrevocably dedicated to, and shall be used for the exclusive purpose of, providing for payments of Benefits and for paying expenses of administering the Trust, and will not be available to any creditors of Employer; and;

WHEREAS, Trustee is willing to accept the Trust; and

WHEREAS, the Trust is authorized under California Government Code Sections 53201, 53206, and 53622, and Section 5 of Article XIII B of the California Constitution; and

WHEREAS, the Trust is an entity separate from Employer for the exclusive benefit of the Beneficiaries and not of Employer; and

WHEREAS, the indicia of ownership of Trust assets shall be held by Trustee at all times and the Trust assets shall not be considered funds or assets of Employer for any purpose; and

WHEREAS, PFM Asset Management LLC is willing to serve as Trust Administrator of the Trust with the rights and duties of the Trust Administrator provided in this Agreement (“Trust Administrator”).

WHEREAS, Trust Administrator shall have exclusive authority and responsibility for the management, disposition and investment of Trust assets in its sole judgment in accordance with this Agreement, without any requirement of consent by Employer or, except as expressly

provided herein, of notice to Employer; and

WHEREAS, the Trust does not contravene Article XVI, Section 6 of the California Constitution by reason of the fact that the Trust is and will remain an entity different and separate from Employer; and

WHEREAS, Employer is a state or political subdivision or other entity the income of which is exempt from federal income tax under Internal Revenue Code Section 115; and

WHEREAS, Trustee is a national banking association and a corporate trustee, with all requisite powers and capabilities to act as Trustee and administer the Trust as set forth in this Agreement; and

NOW, THEREFORE, Employer hereby irrevocably establishes the Trust with Trustee to be held, administered, and distributed by Trustee as provided in this Agreement, and Trust Administrator, Employer, and Trustee agree as follows:

Section I. Exhibits.

The following Exhibits are attached hereto and by this reference incorporated herein and made a part hereof

- (a) Exhibit A to this Agreement contains a copy or other description of the Plans and defines the terms “Beneficiaries,” “Plans” and “Benefits,” as used in the preamble to this Agreement.
- (b) Exhibit B to this Agreement describes Employer’s initial contribution to the Trust.
- (c) Exhibit C to this Agreement is a copy of the Investment Policy Statement delivered by Trust Administrator to Employer, which is satisfactory to Employer.

Section II. General Trust Provisions.

- (a) The Trust is irrevocable.
- (b) The principal of the Trust, together with any earnings thereon, shall be held by Trustee separate and apart from any assets of Employer. All Trust assets and all income thereon are irrevocably dedicated to, and shall be used for the exclusive purpose of, making payments of Benefits to or for the benefit of Beneficiaries and for paying expenses of administering the Trust. At no time will any Trust assets be used for, or diverted to, any other purposes.
- (c) The Trustee shall have exclusive right, title and interest in and to the assets of the

Trust.

(d) Assets held in the Trust may not be used to satisfy claims of creditors of Employer, except to the extent that such are claims to receive Benefits.

(e) Beneficiaries shall have no preferred claim, lien on, or security interest in, or any beneficial interest in any particular assets of the Trust. Beneficiaries shall be entitled to receive payments of assets of the Trust only when, as and if determined by Employer in accordance with this Agreement.

(f) Except to the extent allowed by law, the expectation of any Beneficiary to receive any Benefits is not subject to attachment or garnishment or other legal process by any creditor of any such Beneficiary, nor shall any Beneficiary have the right to alienate, anticipate, commute, pledge, encumber or assign any Benefit until the same shall have been paid.

(g) In its sole discretion, Employer from time to time at any time may make (or cause to be made) additional contributions of cash or other assets acceptable to Trustee to the Trust, from employer contributions, employee contributions or any other source. Neither Trustee, or any Beneficiary or any party to or any other entity referred to in this Agreement shall have any right to compel such additional contributions. All such contributions and all income thereon are irrevocably dedicated to, and shall be used for the exclusive purpose of, making payments of Benefits and for paying expenses of administering the Trust.

(h) Trustee shall not be responsible for enforcing the payment of any contributions to the Trust.

(i) Trust Administrator shall have exclusive authority and responsibility for the management and investment of Trust assets, and Trustee is authorized and directed to comply with the written directions of Trust Administrator concerning Trust assets. Trust Administrator shall not issue any such direction in violation of the terms of the Trust.

(j) No Beneficiary shall be deemed a third-party beneficiary of this Agreement, nor shall any Beneficiary have the right to compel any payment of any amount from the assets of the Trust or to enforce any duties of any party to or other entity referred to in this Agreement.

(k) Employer shall appoint a responsible accounting firm to conduct an annual audit of the Trust at the sole expense of Employer. The results of such audit shall be provided to Trust Administrator, to Trustee and, to Employer.

Section III. Payments from Trust.

(a) The Employer shall determine the amount of Benefits payable under the Plans and

shall have exclusive authority and responsibility to determine the amount of such Benefits to be paid out of the assets of the Trust and the amount which shall be paid to each Beneficiary. Employer shall direct Trustee in writing to disburse amounts in respect of Benefits from the Trust to disburse amounts in respect of Benefits directly to or for the benefit of Beneficiaries. No assets of the Trust may be paid to Employer at the instructions of the Employer.

(b) Except as otherwise provided by law, Trustee shall be fully protected in making payments out of the Trust at the direction of Employer.

(c) Trustee's sole obligation as to disbursements from the Trust in respect of Benefits shall be to observe the instructions of Employer to the extent that the Trust has assets to make disbursements as instructed by Employer. Nothing contained in the Trust or any Plan shall constitute a guarantee that Trust assets will be sufficient to pay any Benefit to any Beneficiary.

(d) Trustee is authorized to disburse amounts from the Trust to pay the expenses of administering the Trust as expressly authorized by this Agreement, or as instructed in writing by Trust Administrator.

Section IV. Investments.

(a) Trustee shall hold and administer Trust assets without distinction between principal and income.

(b) Trustee, in the exercise of its fiduciary judgment or as instructed by Trust Administrator, may commingle, hold and invest as one fund, for investment or administration purposes, the assets (or a portion of the assets) of the Trust and similar trusts; provided that Trustee shall account separately for all assets, income, gains, losses, distributions and expenses of Trust.

(c) Trust assets shall be invested only in Permitted Investments. Trust Administrator shall have full power and authority to invest and reinvest Trust assets in any Permitted Investments permitted under this Agreement.

(d) Transactions in Permitted Investments which require execution through a broker shall be executed through such broker or brokers as Trust Administrator shall select. The indicia of ownership of Trust assets shall be held by Trustee at all times, and the Trustee shall serve as sole custodian with respect to Trust assets.

(e) Any entity affiliated with Trustee may act as broker or dealer to execute transactions, including the purchase of securities directly distributed, underwritten or issued by an entity affiliated with Trustee, at standard commission rates, mark-ups or concessions, and to provide investment services with respect to the Trust.

(f) To the extent directed by Trust Administrator, Trustee is authorized and empowered:

(1) To invest and reinvest Trust assets, together with the income therefrom, in Permitted Investments.

(2) To maintain accounts at, execute transactions through, and lend on an adequately secured basis stocks, bonds or other securities to, any brokerage firm including any firm that is an affiliate of Trustee.

(3) To vote upon or tender any stocks, bonds or other securities and to give general or special proxies or powers of attorney with or without power of substitution; to exercise any conversion privileges, subscription rights or other options of which Trustee receives actual notice, and to make any payments incidental thereto; to consent to or otherwise participate in corporate reorganizations or other changes affecting corporate securities and to delegate discretionary powers and to pay any assessments or charges in connection therewith; and generally to exercise any of the powers of an owner with respect to stocks, bonds, securities or other property held in Trust.

(4) To deposit or invest all or any part of the assets of the Trust in savings accounts or certificates of deposit or other deposits in a bank or savings and loan association or other depository institution, including Trustee or any of its affiliates; provided that, with respect to such deposits with Trustee or an affiliate, the deposits bear a reasonable rate of interest.

(5) To invest and reinvest any Trust assets in one or more collective investment funds.

(6) To hold, manage, improve, repair and control all investment property, real or personal, forming part of the Trust; to sell, convey, transfer, exchange, partition, pledge, encumber, lease for any term, even extending beyond the duration of this Trust, and otherwise dispose of the same from time to time.

(7) To take such actions as may be necessary or desirable to protect the Trust from loss due to the default on mortgages held in the Trust including the appointment of agents or trustees in such other jurisdictions as may seem desirable, to transfer property to such agents or trustees, to grant to such agents such powers as are necessary or desirable to protect the Trust, to direct such agent or trustee, or to delegate such power to direct, and to remove such agent or trustee.

(8) To settle, compromise or abandon all claims and demands in favor of or against the Trust.

(9) To borrow money from any source and to execute promissory

notes, mortgages, or other obligations and to pledge or mortgage any Trust assets as security.

(10) To designate and engage the services of such agents, representatives, advisers, counsel and accountants, any of whom may be an affiliate of Trustee or a person who renders services to such an affiliate and, as part of its expenses under this Agreement, to pay their reasonable expenses and compensation.

(11) To hold in cash, without liability for interest, such portion of the Trust assets as is pending investment, or payment of expenses, or the distribution of Benefits.

(12) To make, execute and deliver, as Trustee, any and all deeds, leases, mortgages, conveyances, waivers, releases or other instruments in writing necessary or appropriate for the accomplishment of any powers listed in this Agreement.

(13) To register securities, or any other property, in its name or in the name of any nominee, including the name of any affiliate or the nominee name designated by any affiliate, with or without indication of the capacity in which property shall be held, or to hold securities in bearer form and to deposit any securities or other property in a depository or clearing corporation.

(14) To pay or cause to be paid from the Trust any and all real or personal property taxes, income taxes or other taxes with respect to the Trust.

(15) To enter into interest rate, currency, cash-flow, indexed (including indexed to equities) and other types of swaps and hedges designed to hedge payment, interest rate, currency, duration, spread or similar exposure related to any investment or program of investments of Trust assets or to manage asset/liability matching between investments and Benefits to be paid therefrom.

(16) To exercise all of the further rights, powers, options and privileges granted, provided for, or vested in trustees generally under the laws of the State of California so that the powers conferred upon Trustee herein shall not be in limitation of any authority conferred by law or under this Agreement, but shall be in addition thereto; provided that such powers satisfy applicable requirements (if any) of the laws of the State of California.

(17) Generally to do all other acts which Trustee deems necessary or appropriate for the protection of the Trust.

Section V. Trust Administrator Services and Trust Administrator and Trustee Compensation.

(a) Trust Administrator shall determine the asset allocation of investments for Trust assets in its judgment from time to time in light of the anticipated amounts of cash required by

the Trust for distributions and other expenses, and the principles set forth in the Investment Policy Statement. Trust Administrator shall execute the Investment Policy Statement by buying and selling investments for the Trust as described in Section IV hereof. Initially, the Trust assets shall be invested in specified investment funds in specified proportions as set forth in the Investment Policy Statement. Thereafter, Trust Administrator shall exercise its professional judgment with respect to investments and shall have no obligation to consult with or obtain approval of Employer.

(b) Trust Administrator shall reassess and may alter the asset allocation of the Trust at least annually. Trust Administrator shall “rebalance” the investments of the Trust at least annually to maintain the ratios of the asset allocation of the Trust then in effect, and shall consult with the Actuary and Employer at least annually to determine whether there are reasons to revise the Investment Policy Statement. Trust Administrator shall continuously review the performance of the investment of Trust assets and, in its judgment, shall purchase or sell Permitted Investments for the Trust. In addition, Trust Administrator shall provide to Employer and Trustee a quarterly analysis of the performance of the investments of the Trust and statement of any changes in investments made in such quarter. The asset information for such analysis shall be supplied to Trust Administrator by Trustee.

(c) Trustee shall have sole custody of cash, securities and other assets of the Trust. Trust Administrator is authorized to give instructions to Trustee as to deliveries of securities and payments of cash for the account of the Trust. Trust Administrator shall not take possession of or act as custodian for the cash, securities or other assets of the Trust and shall have no responsibility in connection therewith.

(d) (1) Except as otherwise stated herein, the Trust shall incur total costs not exceeding 1.0% (one percent) per year of the Net Assets of the Trust for the payment of Trust Administration Fees. “Net Assets” means the net market value of all cash and investments assets as of the end of the most recent quarter as determined and reported by Trustee. “Trust Administration Fees” means the fees of the applicable investment funds, the fees for all services of Trust Administrator, and fees of Trustee in its role as custodian of the Trust assets (which fees of Trustee shall be paid by Trust Administrator to Trustee).

(2) At the end of each calendar quarter, Trust Administrator shall submit to Trustee, with a copy to Employer, an invoice for payment of the Trust Administration Fees for the preceding calendar quarter, which amount shall not exceed 0.25% (one-quarter of one percent) of the Net Assets of the Trust. Trust Administrator is authorized to instruct Trustee to disburse funds from the Trust for the payment of the Trust Administration Fees to Trust Administrator. If either Trust Administrator or Trustee shall serve for less than the entire quarter, the compensation shall be pro-rated.

(3) For services provided by Trustee to the Trust pursuant to this Agreement (exclusive of the services provided by Trustee as custodian, the fees for which are paid as set forth in paragraph (d)(1) above), Trustee shall be paid an annual fee not to exceed \$1,000 (the “Trustee Fee”). Trustee is authorized to disburse funds from the Trust to itself for the payment

of the Trustee Fee.

(4) If and to the extent that Trustee shall request Trust Administrator to render services to the Trust other than those to be rendered by Trust Administrator hereunder, such additional services shall be compensated separately on terms to be agreed upon between Trust Administrator and Trustee.

(e) (1) Trust Administrator shall furnish at its own expense all necessary administrative services, office space, equipment, clerical personnel, telephone and other communication facilities, and executive and supervisory personnel required to perform its duties under this Agreement.

(2) Except as expressly provided otherwise herein, Trustee is authorized to disburse funds from the Trust to pay the expenses of administering the Trust, including, without limitation, taxes, payable by the Trust, fees and expenses of legal counsel to the Trust, if any, and, insurance premiums.

(f) Trust Administrator hereby represents that it is a registered investment advisor under the Investment Advisers Act of 1940. Trust Administrator shall immediately notify Employer and Trustee if at any time during the term of this Agreement it is not so registered or if its registration is suspended. Trust Administrator agrees to perform its duties and responsibilities under this Agreement with reasonable care as provided by law. The federal securities laws impose liabilities under certain circumstances on persons who are required to act in good faith. Nothing in this Agreement shall in any way constitute a waiver or limitation of any rights which Employer, Trust Administrator or Trustee may have under any federal securities laws.

(g) Employer and Trustee understand that Trust Administrator performs investment advisory services for various other clients which may include investment companies, commingled trust funds and individual portfolios. Employer and Trustee agree that Trust Administrator may give advice or take action with respect to any of its other clients which may differ from advice given or the timing or nature of action taken with respect to the Trust, so long as it is the policy of Trust Administrator, to the extent practical, to allocate investment opportunities to the Trust over a period of time on a fair and equitable basis relative to other clients. Trust Administrator shall not have any obligation to purchase, sell or exchange any security for the Trust solely by reason of the fact that Trust Administrator, its principals, affiliates, or employees may purchase, sell or exchange such security for the account of any other client or for themselves.

(h) Trust Administrator shall promptly give notice to Employer and Trustee if Trust Administrator shall have received written notice of the filing against it or any professional of Trust Administrator who has performed any service with respect to the Trust in the 24 preceding months, of any complaints or disciplinary actions by the Securities and Exchange Commission or any other agency or department of the United States, any registered securities exchange, the NASD, any Attorney General or any regulatory agency or authority of any State.

(i) Trust Administrator, its employees, officers and representatives, shall not be deemed to be employees, agents, partners, servants, and/or joint ventures of Employer or Trustee by virtue of this Agreement or any actions or services rendered under this Agreement.

(j) Trust Administrator shall maintain appropriate records of all its activities hereunder.

(k) Trust Administrator warrants that it has delivered to Employer and Trustee, at least five business days prior to the execution of this Agreement, Trust Administrator's current Securities and Exchange Commission Form ADV, Part II, including, without limitation, Exhibit H thereto (Trust Administrator's disclosure statement). Employer and Trustee acknowledge receipt of such disclosure statement at least five business days prior to the execution of this Agreement.

(l) The provisions of this Agreement shall be binding on Trust Administrator and its successors and assigns, provided, however, that the rights and obligations of Trust Administrator may not be assigned without the prior written consent of Employer.

Section VI. Trustee Accounting.

(a) Trustee shall keep accurate and detailed records of all investments, receipts, disbursements, and all other transactions, including such specific records as shall be agreed upon in writing between Trust Administrator and Trustee.

(b) Within 60 days following the close of each calendar quarter (and within 60 days after removal or resignation of Trustee), Trustee shall deliver to Trust Administrator and Employer a written account of the Trust during such calendar quarter (or during the period from the close of the last preceding calendar quarter to the date of such removal or resignation), setting forth all deposits, investments, receipts, disbursements and other transactions effected by it, including a description of transfers made and income received by the Trust, all securities and investments purchased and sold with the cost or net proceeds of such purchases or sales (accrued interest paid or receivable being shown separately), all disbursements for the payment of Benefits, administrative expenses (any amounts paid to Trustee shown separately) or other costs paid from the Trust, and showing all cash, securities and other property held in the Trust at the end of such calendar quarter or as of the date of such removal or resignation, as the case may be.

(c) All securities shall be valued at fair market value as of the date of valuation, as determined by Trustee on the basis of such available information as Trustee may deem reasonable, subject to such smoothing method (for actuarial valuation purposes) that averages returns over a period of years that may be adopted by Trust Administrator and submitted in writing to Trustee.

Section VII. Standard of Care and Indemnification.

(a) All Trust assets and all income thereon shall be used for the exclusive purpose of providing for the payments of Benefits to or for the benefit of Beneficiaries and for paying expenses of administering the Trust. Trustee and Trust Administrator, when making, selling or otherwise managing investments of the funds, shall discharge their duties with respect to the investment of the funds (i) solely in the interest of, and for the exclusive purposes of making payments of Benefits to or for the benefit of Beneficiaries, maximizing the amount available for providing Benefits, minimizing Employer contributions thereto, and paying expenses of administering the Trust, (ii) 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, and (iii) shall diversify the investments of the assets so as to minimize the risk of loss and to maximize the rate of return, in accordance with the Investment Policy Statement.

(b) Employer, from its own funds and not from any assets of the Trust, shall indemnify Trustee and each of its affiliates (collectively, "Trustee Indemnified Parties") against, and shall hold them harmless from, any and all loss, claims, liability, and expense, including cost of defense and reasonable attorneys' fees, (collectively, "damages") imposed upon or incurred at any time by any Trustee Indemnified Party by reason of or in connection with the performance of Trustee's services under this Agreement, except to the extent such damages resulted from such Trustee Indemnified Party's performance (or non-performance) of its duties under this Agreement in a manner that constitutes willful misconduct or negligent breach of the standard of care articulated in Section VII(a) above.

(c) Employer, from its own funds and not from any assets of the Trust, and Trustee, solely from the assets of the Trust and not from its own assets, jointly and severally, shall indemnify Trust Administrator and each of its affiliates (collectively, "Administrator Indemnified Parties") against, and shall hold them harmless from, any and all damages imposed upon or incurred by any Administrator Indemnified Party by reason of, or in connection with its services under this Agreement, except to the extent that such damages resulted from the Administrator Indemnified Party's performance (or non-performance) of its duties under this Agreement in a manner that constitutes willful misconduct or negligent breach of the standard of care articulated in Section VII(a) above.

(d) The indemnification obligations provided for in this Agreement shall survive the termination of this Agreement.

Section VII. Resignation and Removal of Trust Administrator.

(a) Trust Administrator may resign at any time upon 90 days prior written notice to Employer, which notice may be waived by Employer. Employer may remove Trust Administrator upon 90 days prior written notice to Trust Administrator and the Trustee, which notice may be waived by Trust Administrator.

(b) Upon notice of Trust Administrator's resignation, Employer shall promptly designate a successor Trust Administrator qualified to act as Trust Administrator of the Trust under the laws of the State of California, such resignation to be effective upon acceptance of appointment by such successor Trust Administrator. Employer shall not remove the Trust Administrator unless Employer shall have designated such a successor Trust Administrator who shall have agreed with Employer and Trustee to act as Trust Administrator pursuant to this Agreement.

(c) Until a successor Trust Administrator is appointed and assumes its duties as Trust Administrator under this Agreement, Trust Administrator shall be entitled to compensation for its services in accordance with Section V(e)(1) of this Agreement.

(d) Any company into which the Trust Administrator may be merged or converted or with which it may be consolidated or any company resulting from any merger, conversion or consolidation to which it shall be a party or any company to which the Trust Administrator may sell or transfer all or substantially all of its investment advisory business, shall be, with the prior written consent of Employer, the successor to such Trust Administrator.

(e) A successor Trust Administrator shall have no duty to audit or otherwise inquire into the acts or transactions of its predecessor.

Section IX. Resignation and Removal of Trustee.

(a) Trustee may resign at any time upon 90 days prior written notice to Trust Administrator, which notice may be waived by Trust Administrator. Trust Administrator may remove Trustee as provided in Paragraph b below, upon 90 days prior written notice to Trustee, which notice may be waived by Trustee.

(b) Employer shall have the power upon written instructions to Trust Administrator to cause Trust Administrator to remove Trustee (or any successor trustee) and to replace Trustee (or any such successor trustee) with a corporate Trustee satisfactory to Trust Administrator in its sole judgment.

(c) Upon notice of Trustee's resignation or removal, Trust Administrator shall promptly designate a successor corporate Trustee qualified to act as Trustee of the Trust under the laws of the State of California, such resignation or removal to be effective upon acceptance of appointment by such successor corporate Trustee.

(d) If Trust Administrator does not designate a successor corporate Trustee, or if a successor corporate Trustee designated by Trust Administrator has not accepted its appointment within 90 days after Trustee gives notice of its resignation or receives notice of removal, Trustee may, at the expense of the Trust, apply to a court of competent jurisdiction to appoint a successor corporate Trustee.

(e) Until a successor corporate Trustee is appointed and assumes its duties, Trustee shall be entitled to compensation for its services according to its fee schedule then in effect for acting as Trustee in accordance with the Trust.

(f) Any company into which the Trustee may be merged or converted or with which it may be consolidated or any company resulting from any merger, conversion or consolidation to which it shall be a party or any company to which the Trustee may sell or transfer all or substantially all of its corporate trust business, shall be the successor to such Trustee without the execution or filing of any paper or any further act, anything herein to the contrary notwithstanding.

(g) A resigning Trustee shall transfer the Trust assets and shall deliver the books, accounts and records of the Trust to the successor corporate Trustee as soon as practicable.

(h) A resigning Trustee is authorized to reserve such amount as may be necessary for the payment of its fees and expenses incurred prior to its resignation or removal, and the Trust assets shall remain liable to reimburse the resigning or removed Trustee for any costs or fees payable to Trustee under the terms of this Agreement.

(i) A successor corporate Trustee shall have no duty to audit or otherwise inquire into the acts or transactions of its predecessor.

Section X. Amendment, Merger, Transfer or Termination.

(a) At any time that there is an existence any Trust created by Employer which satisfies the terms of Section II of this Agreement (“Qualified Trust”), at the direction of Employer, the Trust may be merged with a Qualified Trust, or all or part of its assets (net of any amount as may be reasonably necessary to pay the fees and expenses of Trust Administrator, Trustee and other expenses of the Trust) transferred to a Qualified Trust; provided, however, that no such merger may increase Trustee’s obligations under this Agreement without Trustee’s written approval, no such merger or transfer may render the Trust “revocable,” and no such merger or transfer may adversely affect the status of the Trust as described in the preamble to this Agreement.

(b) At any time that the fair value of the assets of the Trust does not exceed the Benefits then payable under the Plans, or at any time that there is in existence a Qualified Trust, the Trust and this Agreement may be terminated at any time in writing by Trust Administrator or Employer; provided the termination does not render the Trust “revocable” or adversely affect retroactively the status of the Trust as described in the preamble to this Agreement. Upon termination of the Trust, Trust assets shall be paid out at the direction of Trust Administrator in the following order of priority: (1) payment of reasonable administrative expenses (including taxes and termination costs), (2) payment of Benefits currently payable under the Plans, and (3) to a Qualified Trust.

(c) Neither Trust Administrator nor Employer nor any entity related to any of them shall have any beneficial interest in the Trust or receive any amounts upon termination of the Trust.

(d) The Trust shall remain in existence until all assets have been distributed.

(e) Upon termination of the Trust, Trust Administrator and Trustee shall continue to have all powers provided in this Agreement as are necessary or desirable for the orderly liquidation and distribution of Trust assets in accordance with the provisions hereof.

Section XI. Miscellaneous.

(a) The Trust shall be governed by, and interpreted in a manner consistent with, the laws of the State of California and, to the extent applicable, the Internal Revenue Code.

(b) This Agreement is not a joint exercise of powers agreement, does not create a joint powers or joint action authority, and the obligations of Employer and the Trust are several and not joint. Neither Trustee nor Trust Administrator shall be responsible for any contributions, costs, Benefits, distributions, acts or omissions of Employer.

(c) Each party to this Agreement represents and warrants that the person or persons signing this Agreement on behalf of such party is authorized and empowered to sign and deliver this Agreement for such party.

(d) Employer shall notify Trust Administrator and Trustee in a separate writing of the person or persons, by office or other position of employment, who are authorized to act on behalf of Employer in all matters relating to the Trust.

(e) Trust Administrator shall notify Trustee and Employer in a separate writing of all those who are authorized to act on behalf of Trust Administrator in all matters relating to the Trust.

(f) If there is any conflict between the Plans and this Agreement, this Agreement shall control.

(g) In the event any provision of this Agreement is held to be invalid for any reason, such invalidity shall not affect any other provisions of this Agreement and this Agreement shall be construed and enforced as if the invalid provision had never been included.

(h) This Agreement may be executed in any number of counterparts, each of which shall be considered as an original.

(i) All communications under this Agreement shall be in writing and shall be deemed

to have been duly given (1) on the date of receipt if served personally or by confirmed facsimile or other similar communication; (2) on the first business day after sending if sent for guaranteed next day delivery by a next-day courier service; or (3) on the fourth business day after mailing if mailed to the party or parties to whom notice is to be given by registered or certified mail, return receipt requested, postage prepaid, and properly addressed as follows:

If to Employer:

[ADD EMPLOYER NOTICE ADDRESS:

If to Trust Administrator:

PFM Asset Management LLC
Two Logan Square, Suite 1600
18th and Arch Streets
Philadelphia, PA 19103
Attention:_____

If to Trustee:

U.S. Bank Association
P. O. Box 64488
St. Paul, MN 55164-0488
Attention:_____

IN WITNESS WHEREOF, and as evidence of establishment of the Trust created hereunder, the parties have caused this Agreement to be executed as of the date first above written:

[EMPLOYER]

By: _____

Name: _____

Title: _____

PFM ASSET MANAGEMENT LLC,
As Trust Administrator

By: _____

Name: _____

Title: _____

U.S. BANK NATIONAL ASSOCIATION,

By: _____

Name: _____

Title: _____

EXHIBIT A

PLANS

**[ATTACH COPY OR OTHER DESCRIPTION OF THE PLANS
INCLUDE DEFINITIONS OF “BENEFICIARIES,” “PLANS”
AND “BENEFITS”]**

EXHIBIT B

EMPLOYER'S INITIAL CONTRIBUTION

Employer's initial contribution to the Trust of \$_____ was deposited with Trustee on [date].

EXHIBIT C
CERTIFICATE OF EMPLOYER
[PER SECTION V(A)]

Duplicate Original

INVESTMENT ADVISORY AGREEMENT

THIS AGREEMENT, entered into as of the 20th day of July, 2010 (the "Agreement"), by and between City of Sunnyvale, Santa Clara County, California (hereinafter the "Client") and PFM ASSET MANAGEMENT LLC, a Delaware limited liability company with an office in San Francisco, California (hereinafter the "Advisor").

WITNESSETH

WHEREAS, the Client maintains the Sunnyvale Retiree Medical Trust (the "Fund") in order to satisfy the City's long-term liability for retiree medical costs; and

WHEREAS, the Fund has funds available for investment purposes; and

WHEREAS, the Client desires to avail itself of the experience, sources of information, advice, assistance and facilities available to the Advisor; to have the Advisor undertake certain duties and responsibilities; and to perform certain services as investment advisor on behalf of the Fund, as provided herein; and

WHEREAS; the Advisor is willing to provide such services on the terms and conditions hereinafter set forth.

NOW, THEREFORE, in consideration of the premises and mutual covenants herein contained, the parties hereto, intending to be legally bound, agree as follows:

1. SERVICES OF ADVISOR.

The Client hereby engages the Advisor to serve as investment advisor with respect to the Fund under the terms of this Agreement, and the Advisor accepts such engagement. The Advisor will determine the asset allocation of investments for the Fund (the "Investment Strategy" of the Fund) on the basis of information provided by the Client or other service providers, including the anticipated amounts of cash required by the Fund for distributions and other

expenses, and the appropriate risk tolerance for the Fund based upon the cash needs of the Fund and the Client's resources. The Advisor will then execute the Investment Strategy of the Fund by buying and selling shares of the investment funds. Initially the Fund shall be invested in investment funds in specified proportions as set forth in a separate schedule delivered to the Client by the Advisor at or prior to the time the Fund is initially funded (as the same may be revised by the Advisor from time to time, the "Schedule").

The Advisor will reassess and may alter the Investment Strategy asset allocation at least annually and "rebalance" the investment funds as reflected in the Schedule at least annually to maintain the ratios of the Investment Strategy, and will consult with the Client at least annually to determine whether there are reasons to revise the Investment Strategy. The Advisor will conduct a review at least annually of the performance of the investment funds held by the Fund and, in its judgment, will add to or reduce allocations to each investment fund and will add or delete investment funds (within the parameters of the Investment Strategy). The Advisor will promptly advise the Client in writing of any revision of the Fund's Investment Strategy and any additions to or deletions from the investment funds held by the Fund. In addition, the Advisor will provide to the Client a quarterly analysis of the performance of the investment funds in which the Fund is invested together with notice of any reallocation of assets among investment funds; the asset balances and market values for such analysis shall be as supplied to the Advisor by the Custodian (as hereinafter defined). In connection with all of the foregoing, the Advisor will promptly give the Client written notice of any changes to the Schedule.

The Client agrees to legally appoint a custodian (the "Custodian") to take and have custody of cash, assets and securities of the Fund. The Custodian shall not be the Advisor and shall be independent of the Advisor. The Client agrees to enter, or that it has entered, into a custodian agreement with the Custodian. The Advisor is authorized to give instructions to the Custodian with respect to the Fund as to deliveries of securities and payments of cash for the payment of securities and as otherwise provided in Section 2(b) of this Agreement. The Advisor shall not take possession of or act as custodian for the cash, securities or other assets of the Fund and shall have no responsibility in connection therewith. The Advisor agrees to recommend and to monitor the Custodian so that the Client's custodial and transaction costs are appropriate

for the level and nature of services rendered by the Custodian to the Fund, the Client and the Advisor.

Authorized investments shall include only those investments which are permissible under applicable statutes and regulations and the Fund's written investment policy, if any, as provided by the Client to the Advisor. The Custodian or an affiliate of the Custodian may be the investment advisor of investment funds selected by the Advisor.

2. COMPENSATION.

(a) For all services provided by the Advisor to the Fund pursuant to this Agreement, the Fund shall incur an annual fee based on net assets under management in the Fund determined on a monthly basis as defined in the Investment Advisory Fee Schedule below. For purposes of this section, "net assets" means the net market value of all cash and investments assets as of the end of the most recent month.

Investment Advisory Fee Schedule:

With a minimum investment of \$25 million within first six months:

First \$50 million in net assets.....	0.29%
Thereafter for assets above \$50 million.....	0.20%

With a minimum investment of less than \$25 million within first six months:

Net assets.....	0.36%
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until such time as investments exceed \$25 million, after which time the preceding fee schedule applies.

Included in this fee is PFM's direct payment of expenses associated with obtaining a federal IRS private letter ruling on its OPEB trust. Alternatively the Client may elect to pay one-half of those expenses directly and the above fee on the first \$50 million of assets invested will be reduced by one basis point (0.01%) to 28 basis points (0.28%).

(b) At the end of each calendar month, the Advisor will prepare and submit to the Client for approval a monthly invoice for its fee. Such invoice will

include a statement of the basis upon which the fee was calculated. Unless instructed otherwise within 15 calendar days of the postmark on the invoices, the Client authorizes the Advisor to charge such invoices to the Fund's account and authorizes and instructs the Custodian to disburse funds from such account for the payment of the fees and costs to the Advisor. If sufficient funds are not available, the Client agrees to compensate the Advisor from other sources within 30 calendar days of the postmark date. If the Advisor shall serve for less than the whole month, the compensation shall be pro-rated.

(c) If and to the extent that the Client shall request the Advisor to render services other than those to be rendered by the Advisor hereunder, such additional services shall be compensated separately on terms to be agreed upon between the Advisor and the Client.

(d) Assets invested by the Advisor under the terms of this agreement may from time to time be invested in a money market mutual fund or local government investment pool managed by the Advisor (either, a "Pool"), or in individual securities. Average daily net assets subject to the fees described in this section shall not take into account any funds invested in the Pool. Expenses of the Pool, including compensation for the Advisor and the Pool custodian, are described in the relevant prospectus or information statement and are paid from the Pool.

3. EXPENSES.

(a) The Advisor shall furnish at its own expense all necessary administrative services, office space, equipment, clerical personnel, telephone and other communication facilities, investment advisory facilities, and executive and supervisory personnel for managing the investments, inclusive of reasonable costs required to attend meetings with the Client.

(b) Except as expressly provided otherwise herein, the Fund shall pay all of its expenses including, without limitation, taxes, expenses (including front- or back-end charges) of an investment fund, fees and expenses of the Fund's independent auditors and legal counsel, if any, insurance premiums, fees and expenses of the Custodian appointed by the Client, as provided in Section 1, and the keeping of books and accounts.

4. REGISTERED ADVISOR; DUTY OF CARE.

The Advisor hereby represents it is a registered investment advisor under the Investment Advisers Act of 1940. The Advisor shall immediately notify the Client if at any time during the term of this Agreement it is not so registered or if its registration is suspended. The Advisor agrees to perform its duties and responsibilities under this Agreement with reasonable care. The federal securities laws impose liabilities under certain circumstances on persons who are required to act in good faith. Nothing herein shall in any way constitute a waiver or limitation of any rights which the Client, the Fund, or the Advisor may have under any federal securities laws. The Client hereby authorizes the Advisor to sign an Internal Revenue Service Form W-9 on behalf of the Client and to deliver such form to broker-dealers or others from time to time as required in connection with securities transactions pursuant to this Agreement.

5. ADVISOR'S OTHER CLIENTS.

The Client understands that the Advisor performs investment advisory services for various other clients which may include investment companies, commingled trust funds and/or individual portfolios. The Client agrees that the Advisor, in the exercise of its professional judgment, may give advice or take action with respect to any of its other clients which may differ from advice given or the timing or nature of action taken with respect to the Fund. The Advisor shall not have any obligation to purchase, sell or exchange any security for the Client solely by reason of the fact that the Advisor, its principals, affiliates, or employees may purchase, sell or exchange such security for the account of any other client or for itself or its own accounts.

6. TERM.

This Agreement may be terminated by the Client in the event of any material breach of its terms immediately upon notice by certified mail, return receipt requested. This Agreement may be terminated by the Client at any time, on not less than thirty (30) days' written notice to the Advisor. The Advisor may terminate this Agreement immediately upon any material breach of its terms by the Client, or at any time after one year upon thirty (30) days' written notice.

7. FORCE MAJEURE.

The Advisor shall have no liability for any losses arising out of the delays in performing or inability to perform the services which it renders under this Agreement which result from events beyond its control, including interruption of the business activities of the Advisor or other financial institutions due to acts of God, acts of governmental authority, acts of war, terrorism, civil insurrection, riots, labor difficulties, or any action or inaction of any carrier or utility, or mechanical or other malfunction.

8. DISCIPLINARY ACTIONS.

The Advisor shall promptly give notice to the Client if the Advisor shall have been found to have violated any state or federal securities law or regulation in any criminal action or civil suit in any state or federal court or in any disciplinary proceeding before the Securities and Exchange Commission or any other agency or department of the United States, any registered securities exchange, the Financial Industry Regulatory Authority, or any regulatory authority of any State based upon the performance of services as an investment advisor.

9. INDEPENDENT CONTRACTOR.

The Advisor, its employees, officers and representatives, shall not be deemed to be employees, agents (except as to the purchase or sale of securities described in Section 1), partners, servants, and/or joint ventures of the Client or the Fund by virtue of this Agreement or any actions or services rendered under this Agreement.

10. BOOKS.

The Advisor shall maintain appropriate records of all its activities hereunder. The Advisor shall use its best efforts to cause the Custodian to provide the Client with a statement, no less frequently than quarterly, showing deposits, withdrawals, purchases and sales (or maturities) of investments, earnings received, and the value of assets held on the last business day of the month all as provided for in the Custodian agreement between the Client and the Custodian.

11. ADVISOR'S DISCLOSURE STATEMENT.

The Advisor warrants that it has delivered to the Client, at least 48 hours prior to the execution of this Agreement, the Advisor's current Securities and Exchange Commission Form ADV, Part II, including, without limitation, Schedule H thereto (disclosure statement). The Client acknowledges receipt of such disclosure statement at least 48 hours prior to the execution of this Agreement.

12. MODIFICATION.

This Agreement shall not be changed, modified, terminated or discharged in whole or in part, except by an instrument in writing signed by both parties hereto, or their respective successors or assigns.

13. SUCCESSORS AND ASSIGNS.

The provisions of this Agreement shall be binding on the Advisor and its respective successors and assigns, provided, however, that the rights and obligations of the Advisor may not be assigned without the consent of the Client.

14. NOTICE.

Written notices required under this Agreement shall be sent by regular mail, certified mail, overnight delivery or courier, and shall be deemed given when received at the parties' respective addresses shown below. Either party must notify the other party in writing of a change in address.

Client's Address

City of Sunnyvale
650 W. Olive Ave.
Sunnyvale, CA 94086
Attn: Grace Leung, Acting Director of Finance

Advisor's Address

PFM Asset Management LLC
50 California Street
Suite 2300
San Francisco, CA 94111
Attn: Girard Miller, Senior Strategist

With a Copy to:

PFM Asset Management LLC
Two Logan Square, Suite 1600
18th & Arch Streets
Philadelphia, PA 19103-2770
Attn: Controller

15. APPLICABLE LAW.

This Agreement shall be construed, enforced, and administered according to the laws of the State of California. The Advisor and the Client agree that, should a disagreement arise as to the terms or enforcement of any provision of this Agreement, each party will in good faith attempt to resolve said disagreement prior to filing a lawsuit.

16. APPROVAL; EXECUTION; SEVERABILITY.

(a) This Agreement has been approved by the City Council (the "Governing Body") of the Client. The Governing Body hereby authorizes each designated person (a "Designated Person") identified on Annex I hereto, acting on behalf of the Client, to interact with the Advisor regarding the Fund, and the Advisor may rely on any instructions received from such Designated Person; provided however, that this Agreement may not be amended without the prior approval of the Governing Body. The City Manager may designate additional Designated Persons or remove Designated Persons from time to time by written notice to the Advisor.

(b) Each party to this Agreement represents and warrants that the person or persons signing this Agreement on behalf of such party is authorized and empowered to sign and deliver this Agreement for such party.

(c) The invalidity in whole or in part of any provision of this Agreement shall not void or affect the validity of any other provision.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed by their authorized representatives as of the date set forth in the first paragraph of this Agreement.

PFM ASSET MANAGEMENT LLC

By: Valentine J. Link, Jr.
Name: VALENTINE J. LINK, JR.
Title: MANAGING DIRECTOR

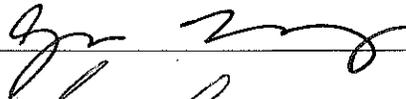
CLIENT

By: 
Name: Gary Luebbers
Title: City Manager

ANNEX I

DESIGNATED PERSONS

The following are Designated Persons pursuant to Section 16 of the foregoing Investment Advisory Agreement, and each such person's signature is set forth below.

<u>Name of Designated Person</u>	<u>Title</u>	<u>Signature</u>
Grace Leung	Acting Director of Finance	
Gary Luebbers	City Manager	



October 21, 2010

Memorandum

To: Grace Leung, Finance Director
City of Sunnyvale

From: Girard Miller, CFA, Senior OPEB Strategist
Carlos Oblites, Senior Managing Consultant
PFM Asset Management LLC

Re: City of Sunnyvale OPEB Trust Asset-Liability Analysis and Asset Allocation
Recommendation

Liability Analysis

Based on the latest OPEB plan actuarial information provided to PFM by the city, the retiree medical benefits plan has 900 active employees with an average age of 44 and average past service of 10 to 13 years, and 678 retirees with an average age of 66. Retirees are roughly equally divided between Medicare-eligible and pre-Medicare populations. The present value of the actuarial accrued liability was divided for our analysis into three segments: 29 percent was attributable to retirees over the age of 65, 30 percent was attributable to retirees under age 65, and 41 percent was associated with active employees. Life expectancy for the average retiree is approximately 17 years.

Given the large percentage of liabilities associated with retirees, and their general age ranges, a moderately conservative initial asset allocation is appropriate. Although retirees constitute 59% of the liabilities, their ages are sufficiently low and distributed normally that investments aligned with that population can include some additional equity exposure to associate initial assets with the pre-Medicare retirees with life expectancies of 20 year or more. Accordingly an initial asset allocation of more than 41% equities is justified and reasonable, whereas a traditional pension-like 60/40% stock bond split is not justified by the liability analysis.

With an actuarially required contribution (ARC) of almost double the level of benefits payments, the plan will be expected to grow through net new contributions by \$3 million or more annually if the ARC is fully funded, and these new funds derived from normal actuarial funding should be invested in a manner consistent with the active members' age distribution, more along the lines of 65/35% for incoming funds.

Risk Tolerance Analysis

PFM reviewed with city personnel the risk-return metrics of various asset allocation combinations, and specifically reviewed possible outcomes for asset allocations ranging from 40-60% to 60/40% equities-to-fixed. With an expected return of 7.73% before fees and a 52% probability of exceeding



a gross return of 7.75% over a 10-year projection period with a reasonable and moderate standard deviation of 8.91%, the 50-50 mix was selected by PFM as the recommended initial position. City staff members attending the fiduciary training session were presented other mixes and expressed an aversion to higher levels of risk during the initial funding phase, which comports with the objective data.

Initial Asset Allocation

The initial asset allocation would consist of a target level for domestic equity of 28%, international equity of 17%, 5% in other equity including real estate and inflation-oriented securities (commodities and TIPS, for example) and 50% in fixed income. The investment policy statement will provide a range around these general strategic target levels which enables the discretionary portfolio manager to adjust positions in accordance with its best professional judgment under changing market conditions, and without excessive trading costs from rebalancing activities in volatile markets.

Dollar Cost Averaging

During the fiduciary training session, PFM discussed with city staff the various options for mitigating initial funding risk. A dollar-cost-averaging strategy of three to six months was recommended, and the staff determined that it would be preferable to average the portfolio on a monthly basis through the end of the fiscal year in June 2011. Upon further review PFM recommends that an initial investment of 25% of the initial first-year's funding be made at the outset in order to efficiently populate the initial trust. The remaining assets will be invested in equal amounts for the remainder of the fiscal year.

Recommended Transition Plan

During the fiduciary training session, PFM presented two strategies to migrate the plan from the initial more-conservative asset allocation toward a higher-equity asset allocation over time in recognition of expected income cash flows and the normally expected growth of equity portfolios over fixed income. Data were subsequently provided to model the risk-return characteristics of a migration path from 50/50% to 60/40% equities/fixed over a 5-year and a 10-year transition period.

In light of the substantial expected incoming cash flows and the relatively minor risk differentials in years 3-7 with additional expected returns, PFM recommended a 5-year migration strategy. This will be accomplished through subsequent annual or biennial adjustments to the target asset allocations, and will be authorized in general terms by the investment policy statement without providing specific year-by-year bandwidths which would become excessively detailed and complex to administer. PFM would expect to advise the city when the asset allocation bands in the initial plan would require adjustment in order to continue the migration toward the 5-year target allocation structure of 60/40% equity/fixed.

INVESTMENT POLICY STATEMENT

FOR

CITY OF SUNNYVALE

OTHER POST-EMPLOYMENT BENEFITS TRUST

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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 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, 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 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 through asset appreciation and income generation, while maintaining a reasonable investment risk profile.
4. To minimize principal fluctuations 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

Time Horizon

The Trust's investment objectives are based on a 20-year investment horizon ("Time Horizon"). 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

The Trust will generally will hold 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 fund, 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 securities 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>
Domestic Equity	18% - 38%	28%
International Equity	7% - 27%	17%
REITs	0% - 10%	2.5%
Inflation Hedge	0% - 10%	2.5%
Fixed Income	35% - 75%	50%
Cash Equivalent	0% - 20%	0%

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, the Advisor will rebalance, and cause the Managers to rebalance, the assets within the specified ranges.

Risk Tolerance

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 year period, the performance objective for Trust will be to achieve 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 approximate 7% 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 Investments and blended benchmark comparisons for the Trust in its entirety.

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, 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 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 Investments that have investment objectives and policies that are consistent with this Policy Statement (as outlined in following sub-sections of the “Guidelines for Portfolio Holdings”). However, given the nature of the Investments, it is recognized that there may be deviations between this Policy Statement and the objectives of these Investments.

Limitations on Managers’ Portfolios

EQUITIES

Domestic Equities. No more than 5% of the Manager’s total equity portfolio valued at market may be invested in the equity of any one corporation, ownership of the shares of one company shall not exceed 2% of those outstanding, and not more than 25% of equity valued at market may be held in any one sector, as defined by the Industry Classification Benchmark universe database. Other than these 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. No more than 5% of the 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 2% of those outstanding, and not more than 25% of equity valued at market may be held in any one sector, as defined by the Industry Classification Benchmark universe database. 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. The emerging markets exposure, as defined by Morgan Stanley Capital International Inc. (“MSCI”), should be limited to 35% of the non-U.S. portion of the portfolio.

REIT

Real estate assets will be held only in diversified Investments, primarily holding Real Estate Investment Trusts and servicing companies.

INFLATION HEDGE ASSETS

Inflation hedging assets will include only Investments holding among other assets: Treasury Inflation Protected Securities (“TIPS”), commodities or commodity derivative contracts, index-linked derivative contracts, the equity of companies in generally accepted businesses believed to hedge inflation.

FIXED INCOME

Fixed income investments shall be high quality with a preponderance of the investments in (1) U.S. Treasury, federal agencies and U.S. Government guaranteed obligations, (2) investment grade corporate issues including convertibles, and (3) sovereign debt of foreign countries.

Fixed income securities of any one issuer shall not exceed 5% of a 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 shall be at least "A", based on the rating of one of the three rating agencies (Fitch, Moody's or Standard & Poor's). In cases where the yield spread adequately compensates for additional risk, high yield securities (BB+ or lower), can be purchased or held up to a maximum of 20% of total market value of fixed income securities of the Trust.

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 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, private placements (with the exception of Rule 144A securities), or venture capital funds, private equity, or hedge funds. Further, derivatives, options, 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 S&P 500 Index for large cap equities, Russell 2000 Index for small cap equities, MSCI Europe, Australasia, and Far East (EAFE) Index for international equities, Barclays Capital Aggregate Bond Index for fixed income securities, and the U.S. 91 Day T-bill for cash equivalents.

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.

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:

Chair

Date