

**EMPLOYEES RETIREMENT SYSTEM  
OF THE CITY OF ST. LOUIS**

**FINANCIAL STATEMENTS**

**September 30, 2017 and 2016**

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

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## Independent Auditors' Report

The Board of Trustees  
Employees Retirement System of the City of St. Louis  
St. Louis, Missouri

### Report on the Financial Statements

We have audited the accompanying financial statements of the Employees Retirement System of the City of St. Louis (the System), a Pension Trust Fund of the City of St. Louis, Missouri, which comprise the statements of fiduciary net position as of September 30, 2017 and 2016, and the related statements of changes in fiduciary net position for the years then ended and the related notes to the financial statements.

### Management's Responsibility for the Financial Statements

The System's 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.

### Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits 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 of 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 auditors' 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 System'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 System'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.

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Other Locations

Belleville, IL • Carbondale, IL • Columbia, IL • Litchfield, IL • Harrisburg, IL • Springfield, IL • Cape Girardeau, MO • Milwaukee, WI

## Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the fiduciary net position of the Employees Retirement System of the City of St. Louis as of September 30, 2017 and 2016, and the changes in its fiduciary net position for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

## Other Matters

### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and the required supplementary information, as listed in the table of contents, be presented to supplement the 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 the 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.

### *Other Information*

Our audit was conducted for the purpose of forming an opinion on the System's financial statements as a whole. The Additional Financial Information, as listed in the table of contents, is presented for the purpose of additional analysis and is not a required part of the System's financial statements. Such information is the responsibility of the System's management and was derived from and relates directly to the underlying accounting and other records used to prepare the System's financial statements. The information has been subjected to the auditing procedures applied in the audit of the System's financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

*Kerber, Eck & Braeckel LLP*

St. Louis, Missouri  
February 26, 2018



# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## MANAGEMENT'S DISCUSSION AND ANALYSIS - UNAUDITED

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The following Management's Discussion and Analysis of the Employees Retirement System of the City of St. Louis (the System) provides an overview of the System's financial activities for the fiscal year ended September 30, 2017. This section should be read in conjunction with the System's financial statements and supplementary information.

### Financial Highlights

The System's investments continued their strong earnings by posting a 12.17% return for the fiscal year. This marked the fifth double-digit return in the last six years. All investment classes recorded positive returns except energy master limited partnerships' (-3.72%). This year's performance was again led by equities: international at 22.96% and domestic at 20.17%. Real estate came in with a solid 9.84% return. The System's fiduciary net position increased \$52.0 million to reach a new high of \$816.9 million.

Pension and retirement benefits increased 4.2% or \$2.56 million to \$63.5 million. The number of retirees and beneficiaries receiving a monthly benefit increased 1.9% to 4,572. Administrative expenses increased \$41,000 in the fiscal year to \$763,000. All employers are contributing at the rate specified by the actuary.

### Financial Statements

The financial report of the System consists of two financial statements: the Statement of Fiduciary Net Position and the Statement of Changes in Fiduciary Net Position. The Statement of Fiduciary Net Position provides the detail of the System's assets and related liabilities other than benefit obligations. The net position of the System reflects the resources available for future benefit payments. The Statement of Changes in Fiduciary Net Position provides the details of the System's activity during the year that lead to the change in plan fiduciary net position from the prior year.

In addition to the financial statements, the financial report contains the notes to the financial statements and supplemental information. These provide additional information for use in analyzing the financial statements and actuarial information related to the funded status of the System.

### Financial Analysis

Total assets at September 30, 2017 of \$817.6 million were comprised of cash, investments and receivables. Investments increased \$51.7 million or 6.8% to \$816.2 million. Receivables remained steady and consisted of employer contributions and interest and dividend income. Currency exchange contracts showed significant increases and ended FY 2017 as a net receivable. The System exited the securities lending program in June with its then master custodian, State Street Bank and Trust, in preparation of the transition to its new custodian, U.S. Bank, in November 2017. The System received \$9,030 of income from the assets on loan. The System incurred a loss of \$15,011 in its buyout in the securities lending program with State Street Bank and Trust.

Total liabilities at September 30, 2017 were \$715,525 and consisted of accounts payable. The net decrease in liabilities resulted from the previously discussed exit from securities lending.

Net assets held in trust for pension benefits increased \$52.0 million to \$816.9 million.

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## MANAGEMENT'S DISCUSSION AND ANALYSIS - UNAUDITED

### Condensed Statement of Fiduciary Net Position

|  | September 30,        |                       | Total change         |               |
|--|----------------------|-----------------------|----------------------|---------------|
|  | 2017                 | 2016                  | Amount               | Percentage    |
| <b>Assets</b>  |                      |                       |                      |               |
| Cash   | \$ 156,516           | \$ 78,502             | \$ 78,014            | 99.4%         |
| Receivables  | 926,657              | 881,785               | 44,872               | 5.1%          |
| Investments  | 816,207,252          | 764,509,199           | 51,698,053           | 6.8%          |
| Securities lending collateral                          | -                    | 2,201,107             | (2,201,107)          | -100.0%       |
| Currency exchange                                      | 340,750              | 33,914                | 306,836              | 100.0%        |
| <b>Total assets and deferred outflows</b>              | <b>817,631,175</b>   | <b>767,704,507</b>    | <b>49,926,668</b>    | <b>6.5%</b>   |
| <b>Liabilities</b>                                     |                      |                       |                      |               |
| Accounts payable                                       | 715,525              | 602,327               | 113,198              | 18.8%         |
| Securities lending collateral liability                | -                    | 2,201,107             | (2,201,107)          | -100.0%       |
| <b>Total liabilities and deferred inflows</b>          | <b>715,525</b>       | <b>2,803,434</b>      | <b>(2,087,909)</b>   | <b>-74.5%</b> |
| <b>Net position held in trust for pension benefits</b> | <b>\$816,915,650</b> | <b>\$ 764,901,073</b> | <b>\$ 52,014,577</b> | <b>6.8%</b>   |

### Revenues – Additions to Fiduciary Net Position

The assets needed to finance retirement benefits are accumulated through the receipt of employer contributions, member purchases of creditable service and earnings on investments. Net investment income was \$86.4 million for the fiscal year. A solid investment performance generated sufficient earnings to cover retirement benefits and administrative expenses. Net investment income included custodial and investment management fees of \$5.4 million.

Employer contributions decreased \$2.3 million or 7.3% in FY 2017, entirely from a reduction in the recommended employer contribution rate. This rate reduction was primarily due to changes in the actuarial assumptions and methods adopted by the Board of Trustees after the actuarial experience study in 2015 and new GASB standards. Member contributions included \$100,762 of purchase of creditable service by active members and \$33,486 receipt of a pension service transfer from another Missouri public pension plan with a portability agreement with the System.

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## MANAGEMENT'S DISCUSSION AND ANALYSIS - UNAUDITED

### Expenses – Deductions from Fiduciary Net Position

The major expenses of the System include the payment of pension benefits to retirees and beneficiaries and administrative expenses. Other expenses within retirement benefits include refunds of member contributions and pension service transfer payments to other public plans within the State of Missouri which have a portability agreement with the System. Service transfer payments were \$112,574 and contribution refunds were \$743 in FY 2017. Administrative expenses increased \$41,141 in FY 2017 to \$763,273.

### Condensed Statement of Changes in Fiduciary Net Position

|  | September 30,        |                      | Total change         |              |
|--|----------------------|----------------------|----------------------|--------------|
|  | 2017                 | 2016                 | Amount               | Percentage   |
| <b>Additions</b>                         |                      |                      |                      |              |
| Net investment income                    | \$ 86,394,236        | \$ 66,460,934        | \$ 19,933,302        | 30.0%        |
| Employer contributions                   | 29,782,200           | 32,127,591           | (2,345,391)          | -7.3%        |
| Member contributions                     | 134,248              | 10,093               | 124,155              | 1230.1%      |
| <b>Total additions</b>                   | <b>116,310,684</b>   | <b>98,598,618</b>    | <b>17,712,066</b>    | <b>18.0%</b> |
| <b>Deductions</b>                        |                      |                      |                      |              |
| Retirement benefits                      | 63,532,834           | 60,972,546           | 2,560,288            | 4.2%         |
| Administrative expenses                  | 763,273              | 722,132              | 41,141               | 5.7%         |
| <b>Total deductions</b>                  | <b>64,296,107</b>    | <b>61,694,678</b>    | <b>2,601,429</b>     | <b>4.2%</b>  |
| <b>Changes in fiduciary net position</b> | <b>\$ 52,014,577</b> | <b>\$ 36,903,940</b> | <b>\$ 15,110,637</b> | <b>40.9%</b> |

### Summary

The System's investments continued their growth with another year of strong earnings. Only the return of (-3.1%) in FY 2015 interrupted the string of positive investment returns dating back to FY 2010. Investment income and employer contributions exceeded retirement benefits and administrative expenses in each year except for FY 2015 and FY 2011. In those years the deficit was \$52.5 million in FY 2015 and \$7.5 million in FY 2011. The required employer rates recommended by the actuary are currently 12.22% for the City of St. Louis and 12.13% for the other participating employers for the period July 1, 2017 through June 30, 2018. The prior year's contribution rates were 12.51% and 12.43%, respectively. The dual contribution rates are a result of a legal settlement involving the Retirement System, the City of St. Louis and the other participating employers.

The System remains in a position to meet its current pension obligations, as confirmed by the recent actuarial valuation.

The System is a qualified governmental plan under Section 401(a) of the Internal Revenue Code.

# **EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS**

## **MANAGEMENT'S DISCUSSION AND ANALYSIS - UNAUDITED**

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### **Requests for Information**

This financial report is designed to provide the Board of Trustees, our members and other users of our financial report with a general overview of the System's finances and to demonstrate the System's accountability for its funds. If you have any questions about this report or need additional financial information, contact the Employees Retirement System of the City of St. Louis, 1114 Market Street, Suite 900, St. Louis, MO 63101.

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## STATEMENTS OF FIDUCIARY NET POSITION

September 30,

|   | <u>2017</u>           | <u>2016</u>           |
|---|-----------------------|-----------------------|
| <b>ASSETS</b>   |                       |                       |
| Cash  | \$ 156,516            | \$ 78,502             |
| Receivables   |                       |                       |
| Accrued interest receivable                                     | 581,245               | 532,408               |
| Accrued dividend receivable                                     | 180,001               | 180,499               |
| Employers contribution receivable                               | 165,411               | 168,878               |
| Total receivables   | <u>926,657</u>        | <u>881,785</u>        |
| Investments at fair value                                       |                       |                       |
| Temporary cash investments                                      | 9,362,307             | 9,649,768             |
| Fixed income securities   | 87,458,023            | 85,844,979            |
| Common stocks   | 198,735,935           | 183,836,061           |
| Managed master limited partnerships                             | 76,567,189            | 72,050,815            |
| Managed international equity funds                              | 193,611,240           | 162,718,734           |
| Real estate funds   | 88,420,092            | 92,764,744            |
| Domestic bond funds   | 86,173,017            | 83,983,870            |
| Managed hedge fund of funds                                     | 75,879,449            | 73,660,228            |
| Total investments   | <u>816,207,252</u>    | <u>764,509,199</u>    |
| Securities lending collateral                                   | -                     | 2,201,107             |
| Total assets  | <u>817,290,425</u>    | <u>767,670,593</u>    |
| <b>DEFERRED OUTFLOWS OF RESOURCES</b>                           |                       |                       |
| Receivable under forward<br>foreign currency exchange contracts | 340,750               | 33,914                |
| Total deferred outflows of resources                            | <u>340,750</u>        | <u>33,914</u>         |
| <b>LIABILITIES</b>  |                       |                       |
| Accounts payable  | 715,525               | 602,327               |
| Securities lending collateral liability                         | -                     | 2,201,107             |
| Total liabilities   | <u>715,525</u>        | <u>2,803,434</u>      |
| Net position held in trust for pension benefits                 | <u>\$ 816,915,650</u> | <u>\$ 764,901,073</u> |

See notes to financial statements.

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## STATEMENTS OF CHANGES IN FIDUCIARY NET POSITION

Year ended September 30,

|  | 2017                  | 2016                  |
|--|-----------------------|-----------------------|
| <b>ADDITIONS</b>                                       |                       |                       |
| Contributions  |                       |                       |
| Employer contributions                                 | \$ 29,782,200         | \$ 32,127,591         |
| Member contributions                                   | 134,248               | 10,093                |
| Total contributions                                    | <u>29,916,448</u>     | <u>32,137,684</u>     |
| Investment activity                                    |                       |                       |
| Interest and dividends                                 | 10,417,956            | 9,380,928             |
| Net appreciation in fair value of investments          | 81,403,948            | 62,058,510            |
|  | <u>91,821,904</u>     | <u>71,439,438</u>     |
| Less investment expenses                               | 5,427,668             | 4,978,504             |
| Net investment income                                  | <u>86,394,236</u>     | <u>66,460,934</u>     |
| Total additions  | 116,310,684           | 98,598,618            |
| <b>DEDUCTIONS</b>                                      |                       |                       |
| Retirement benefits                                    | 63,532,834            | 60,972,546            |
| Administrative expenses                                | 763,273               | 722,132               |
| Total deductions                                       | <u>64,296,107</u>     | <u>61,694,678</u>     |
| NET INCREASE IN NET POSITION                           | 52,014,577            | 36,903,940            |
| <b>NET POSITION HELD IN TRUST FOR PENSION BENEFITS</b> |                       |                       |
| Beginning of year                                      | <u>764,901,073</u>    | <u>727,997,133</u>    |
| End of year  | <u>\$ 816,915,650</u> | <u>\$ 764,901,073</u> |

See notes to financial statements.



# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

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### NOTE 1 – DESCRIPTION OF PLAN

The following description of the Employees Retirement System of the City of St. Louis is provided for general information purposes only. Participants should refer to the *Employees Retirement System Handbook* for a more complete description of the System's provisions.

#### General

The System is a cost-sharing, multiple-employer, defined benefit public employees' retirement system for all non-uniformed employees of the City of St. Louis and certain other public entities funded by or providing services to residents of the City of St. Louis. These additional employee groups covered by the System are the employees of the St. Louis Public Library, the Art Museum of St. Louis, the St. Louis Zoological Park, the City of St. Louis Water Division, the Airport Authority, the City Mental Health Board, the Metropolitan Taxicab Commission, Tower Grove Park, the System, and civilian employees of the police department and police and fireman's retirement systems. The System became operative April 1, 1960 by municipal ordinance establishing the System under the authority of Senate Bill No. 329 of the 70<sup>th</sup> General Assembly of the State of Missouri. Responsibility for operation and administration of the System is vested in its Board of Trustees. The Board of Trustees consists of the Comptroller of the City of St. Louis, two members appointed by the Mayor of the City of St. Louis, two members elected by the membership of the System, and one member elected by the retired members of the System.

#### Membership

Membership consisted of the following at September 30,:

|  | <u>2017</u>          | <u>2016</u>          |
|--|----------------------|----------------------|
| Retirees and beneficiaries   |                      |                      |
| Currently receiving benefits                                       | 4,572                | 4,486                |
| Terminated employees entitled to but<br>not yet receiving benefits | 2,499                | 2,516                |
| Current employees  |                      |                      |
| Fully vested   | 3,587                | 3,573                |
| Non-vested   | <u>1,692</u>         | <u>1,730</u>         |
| Total membership   | <u><u>12,350</u></u> | <u><u>12,305</u></u> |

#### Benefits

The System provides for defined benefit payments for retirement, death, or disability to eligible employees or their beneficiaries based upon creditable service, final average compensation, and a benefit compensation base. Benefits vest to employees covered by the System after the employee has attained five years creditable service.

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

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Employees retire with full retirement benefits after the age of 65 or if an employee's age and creditable service combined equal or exceed 85 years. Employees may retire and receive a reduced benefit after age 60 with five years of creditable service, age 55 with at least 20 years of creditable service, or any age with 30 years of creditable service.

The monthly pension benefits of all retirees or their beneficiaries are adjusted according to the changes in the Consumer Price Index of the U.S. Department of Labor. Increases are limited each year, with total increases to retirees or their beneficiaries limited to 25%.

### **Contributions**

Employer contribution rates are established annually by the Board of Trustees based on an actuarial study. The required employer contribution rate recommended by the actuary is currently 12.22% for the City of St. Louis and 12.13% for the other participating employers for the period July 2017 through June 2018. Previously the contribution rates were 12.51% and 12.43% for July 2016 through June 2017 and 13.93% and 13.86% for July 2015 through June 2016. The dual contribution rates are a result of a legal settlement involving the System, the City of St. Louis and the other participating employers.

Employees who became members of the System prior to October 14, 1977 and continued to make contributions may make voluntary contributions to the System equal to 3% of their compensation until the compensation equals the maximum annual taxable earnings under the Federal Social Security Act. Thereafter, employees may contribute 6% of their compensation for the remainder of the calendar year.

### **Funding Policy**

The System's funding policy provides for periodic employer contributions at actuarially determined rates that, expressed as percentages of annual covered payroll, are sufficient to accumulate assets to pay benefits when due. If contributions are necessary, level percentage of payroll employer contribution rates are determined using the entry age normal actuarial cost method.

### **Subsequent Events**

Management has evaluated subsequent events through February 26, 2018, the date which the financial statements were available to be issued, for possible recognition or disclosure in the financial statements.

During the year ended September 30, 2017 the System entered into a custody agreement with US Bank, N.A. On November 1, 2017, the assets of the system were transferred from the custody of State Street Bank and Trust Co. to US Bank, N.A. The transfer of the plan assets did not have a material effect on the net position of the System.

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

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### NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following are the significant accounting policies followed by the System.

#### **Basis of Accounting**

The accompanying financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as set forth by Governmental Accounting Standards Board (GASB).

The financial statements were prepared using the accrual basis of accounting except that retirement benefits are recorded when due to the beneficiary. Employee contributions are recognized as additions in the period in which employer payroll is paid. Administrative deductions are recorded when the corresponding liabilities are incurred, regardless of when payment is made.

#### **Tax Status**

The System has been determined to be exempt from federal income taxes under Section 115 of the Internal Revenue Code. In 2005, the System became a qualified retirement plan in accordance with Internal Revenue Service regulations.

#### **Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of System assets and liabilities, disclosure of contingent assets and liabilities at the date of financial statements and reported amounts of additions and deductions to System net position during the reporting period. Actual results could differ from those estimates.

#### **Investments**

A list of allowable investments is included in Note 3. Investments are reported at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date and in the principal and most advantageous market for the asset or liability. See Note 4 for a discussion of fair value measurement. Security transactions and any resulting realized gains or losses are accounted for on a completed transaction basis.

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

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The System participated in a securities lending program administered by State Street Bank and Trust, the custodian. Brokers who borrow the securities provide collateral equal to 102% for domestic securities loaned, resulting in no credit risk for the System. Effective June 21, 2017, the System executed as custodial agreement with US Bank, N.A. At that time the System began the wind-down of the securities lending program with State Street Bank and Trust. At September 30, 2017, the System had no securities on loan. At September 30, 2016, the System had the following securities on loan at market value:

|                                       |                     |
|---------------------------------------|---------------------|
| U.S. corporate bonds and equity       |                     |
| Corporate bonds and equity            | \$ 1,927,372        |
| Non-cash                              | 226,931             |
| Total U.S. corporate bonds and equity | <u>2,154,303</u>    |
| <br>                                  |                     |
| U.S. Government                       |                     |
| Treasury                              | 19,032              |
|                                       | <u>19,032</u>       |
| <br>                                  |                     |
| Total securities on loan              | <u>\$ 2,173,335</u> |

### **Furniture and Equipment**

Acquisitions of furniture and equipment are charged to administrative expense.

### **Derivatives**

The System currently retains Payden & Rygel Investment Counsel as a global fixed income investment manager. The System permits Payden & Rygel to utilize financial derivative instruments such as forwards, futures, and options. The use of these financial derivatives is defensive in nature; that is, used only to manage duration and foreign currency exposure and bond exposure. The System's investment policy requires that open currency exposure shall not exceed 10 percent of the global fixed income portfolio.

The System had receivables under forward foreign currency exchange contracts of \$340,750 and \$33,914 at September 30, 2017 and 2016, respectively.

The System utilizes forward contract hedging to reduce the volatility in foreign currencies. Hedging techniques are traditionally used to limit exposure to price fluctuations. Management recognizes that fluctuations in foreign currencies could have a negative effect on the System's financial statements. Accordingly, the System entered into forward contracts in order to hedge this exposure.

### **Reclassifications**

Investment management fees of \$1,751,456, previously included in net appreciation in fair value of investments have been reclassified to investment expenses for the year ended September 30, 2016 to conform to the 2017 financial statement presentation.

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

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### NOTE 3 – CASH AND INVESTMENTS

The System is authorized to invest in:

- Short-term securities with a maximum maturity of one year including institutional liquid assets, U.S. Treasury obligations, Federal Agency obligations, discount and interest-bearing notes from corporations, and certificates of deposit;
- Fixed income securities including:
  - U.S. government securities;
  - Non-U.S. government fixed income securities; and
  - Publicly-issued corporate bonds, debentures, notes, or other evidences of indebtedness assumed or guaranteed by corporations organized under the laws of the United States with ratings of “A” or better by Moody’s Investors Service;
- Common stocks of corporations organized under the laws of the United States;
- Managed master limited partnerships composed primarily of domestic midstream or energy infrastructure publicly traded on U.S. equity exchanges;
- Common stocks of foreign corporations through separate accounts as commingled vehicles;
- Real estate through discretionary commingled vehicles;
- Hedge funds through either separate or commingled fund of funds vehicles.

It is the System’s current policy to invest in each of the asset classes as indicated below:

| <u>Asset class</u>                      | <u>Target allocation</u> | <u>Long-term* expected real rate of return</u> |
|---|--------------------------|--|
| Large cap                               | 17.00%                   | 7.30%  |
| Small cap                               | 4.00%                    | 7.00%  |
| International large cap                 | 15.30%                   | 7.30%  |
| Emerging markets                        | 6.20%                    | 9.30%  |
| High Yield                              | 5.00%                    | 5.30%  |
| Master limited partnerships             | 7.50%                    | 10.80%   |
| Private equity                          | 5.00%                    | 9.80%  |
| Core fixed income                       | 12.50%                   | 3.80%  |
| International fixed income              | 4.00%                    | 3.50%  |
| Core real estate                        | 10.00%                   | 6.50%  |
| Treasury inflation protected securities | 3.50%                    | 3.50%  |
| Hedge funds                             | 10.00%                   | 5.00%  |
|   | <u>100.00%</u>           | <u>7.20%</u>                                   |

\* *Geometric return*

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

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The bank balances of the System at September 30, 2017 and 2016 were \$1,516,637 and \$802,985, respectively. These balances were insured by the Federal Deposit Insurance Corporation up to \$250,000. The remaining balances were collateralized by securities held by the pledging financial institution's trust department in the System's name.

All investments at September 30, 2017 and 2016 were held by the System's agent in the System's name.

The System has the following concentrations, defined as "investments (other than those issued or guaranteed by the U.S. government)" in any one organization, that represent five percent or more of fiduciary net position at September 30,:

|  | <u>2017</u>  |        |
|--|--------------|--------|
| Acadian Asset Management - Emerging Markets Fund II                        | \$59,031,533 | 7.23%  |
| Twin Capital Management - Domestic Equity                                  | 53,703,103   | 6.57%  |
| PNC Capital Advisors - U.S. Broad Market Core Fixed Income                 | 54,600,077   | 6.68%  |
| Principal Global Investors - Real Estate Group Annuity Contract            | 88,420,093   | 10.82% |
| Silchester International Advisors - International Value Equity Group Trust | 93,145,776   | 11.40% |
| Evanston Weatherlow Offshore - Hedge Fund                                  | 41,302,502   | 5.06%  |
| Walter Scott & Partners Limited Group Trust-<br>International Equity Fund  | 41,433,930   | 5.07%  |
|  | <u>2016</u>  |        |
| Acadian Asset Management - Emerging Markets Fund II                        | \$46,633,058 | 6.10%  |
| INTECH Investment Management - U.S. Large Cap Core Equity                  | 48,399,784   | 6.33%  |
| LSV Asset Management - U.S. Large Cap Value Equity                         | 38,927,513   | 5.09%  |
| PNC Capital Advisors - U.S. Broad Market Core Fixed Income                 | 54,811,330   | 7.17%  |
| Principal Global Investors - Real Estate Group Annuity Contract            | 92,764,744   | 12.13% |
| Silchester International Advisors - International Value Equity Group Trust | 75,518,115   | 9.87%  |
| Evanston Weatherlow Offshore - Hedge Fund                                  | 39,676,400   | 5.19%  |
| Walter Scott & Partners Limited Group Trust-<br>International Equity Fund  | 40,567,561   | 5.30%  |



# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

### Foreign Currency Risk

Foreign currency risk is the risk that the change in exchange rates will adversely impact the fair value of an investment. The System does not have a formal policy to limit foreign currency risk. The following table demonstrates the System's level of foreign currency exposure as of September 30,:

| Currency                 | 2017              |                      |                             |                              |                      |
|--------------------------|-------------------|----------------------|-----------------------------|------------------------------|----------------------|
|                          | Short-Term        | Debt                 | Managed international funds | Managed limited partnerships | Total                |
| Japanese Yen             | \$ 28,467         | \$ 4,960,009         | \$ 37,481,501               | \$ 9,426,018                 | \$ 51,895,995        |
| Euro                     | 23,709            | 5,926,734            | 23,920,913                  | 10,515,512                   | 40,386,868           |
| British Pound            | 37,966            | 1,880,091            | 20,132,817                  | 5,153,020                    | 27,203,894           |
| Hong Kong Dollar         | -                 | -                    | 19,694,181                  | 672,786                      | 20,366,967           |
| Swiss Franc              | -                 | -                    | 15,292,708                  | 836,966                      | 16,129,674           |
| South Korean Won         | -                 | -                    | 12,977,612                  | -                            | 12,977,612           |
| New Taiwan Dollar        | -                 | -                    | 7,793,028                   | -                            | 7,793,028            |
| Thai Baht                | -                 | -                    | 5,353,640                   | -                            | 5,353,640            |
| Indian Rupee             | -                 | -                    | 4,979,818                   | -                            | 4,979,818            |
| Singapore Dollar         | -                 | -                    | 3,319,149                   | 1,648,033                    | 4,967,182            |
| Brazilian Real           | -                 | -                    | 4,570,669                   | 341,145                      | 4,911,814            |
| Turkish New Lira         | -                 | -                    | 3,998,296                   | -                            | 3,998,296            |
| Canadian Dollar          | 14,992            | 767,289              | 1,640,634                   | 1,205,353                    | 3,628,268            |
| Danish Krone             | 4,132             | 71,197               | 3,250,222                   | -                            | 3,325,551            |
| South Africa Rand        | -                 | -                    | 2,419,741                   | -                            | 2,419,741            |
| Mexican Peso             | 16,435            | 109,453              | 1,848,900                   | -                            | 1,974,788            |
| Malaysian Ringgit        | -                 | -                    | 1,797,388                   | -                            | 1,797,388            |
| Australian Dollar        | 4,855             | 360,686              | 1,419,406                   | -                            | 1,784,947            |
| Swedish Krona            | -                 | -                    | 1,510,924                   | -                            | 1,510,924            |
| Indonesian Rupiah        | -                 | -                    | 1,504,932                   | -                            | 1,504,932            |
| Polish Zloty             | 6,035             | 59,770               | 1,060,886                   | -                            | 1,126,691            |
| Norwegian Krone          | -                 | -                    | 247,303                     | 715,640                      | 962,943              |
| Various other currencies | -                 | -                    | 526,941                     | -                            | 526,941              |
| <b>Total</b>             | <b>\$ 136,591</b> | <b>\$ 14,135,229</b> | <b>\$ 176,741,609</b>       | <b>\$ 30,514,473</b>         | <b>\$221,527,902</b> |

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

| Currency                 | 2016              |                      |                             |                              |                      |
|--------------------------|-------------------|----------------------|-----------------------------|------------------------------|----------------------|
|                          | Short-Term        | Debt                 | Managed international funds | Managed limited partnerships | Total                |
| Japanese Yen             | \$ 44,696         | \$ 6,598,615         | \$ 29,981,894               | \$ 25,020,730                | \$ 61,645,935        |
| Euro                     | 134,542           | 6,241,997            | 21,336,223                  | 227,906                      | 27,940,668           |
| British Pound            | 80,321            | 1,752,722            | 19,192,552                  | 101,939                      | 21,127,534           |
| Hong Kong Dollar         | -                 | -                    | 19,287,735                  | 161,822                      | 19,449,557           |
| Swiss Franc              | -                 | -                    | 14,196,349                  | 35,037                       | 14,231,386           |
| South Korean Won         | -                 | -                    | 9,431,489                   | -                            | 9,431,489            |
| Indian Rupee             | -                 | -                    | 4,886,573                   | -                            | 4,886,573            |
| New Taiwan Dollar        | -                 | -                    | 4,428,248                   | -                            | 4,428,248            |
| Thai Baht                | -                 | -                    | 4,333,647                   | -                            | 4,333,647            |
| Brazilian Real           | -                 | -                    | 4,244,749                   | 19,423                       | 4,264,172            |
| Singapore Dollar         | -                 | -                    | 2,807,264                   | 79,031                       | 2,886,295            |
| South Africa Rand        | -                 | -                    | 2,728,593                   | -                            | 2,728,593            |
| Turkish New Lira         | -                 | -                    | 2,612,734                   | -                            | 2,612,734            |
| Australian Dollar        | 25,786            | 556,146              | 1,590,436                   | -                            | 2,172,368            |
| Danish Krone             | 2,869             | 70,191               | 1,777,403                   | -                            | 1,850,463            |
| Canadian Dollar          | 4,197             | 745,092              | 749,217                     | 62,429                       | 1,560,935            |
| Malaysian Ringgit        | -                 | -                    | 1,424,686                   | -                            | 1,424,686            |
| Swedish Krona            | -                 | -                    | 1,405,857                   | -                            | 1,405,857            |
| Mexican Peso             | 8,629             | 106,467              | 1,172,196                   | -                            | 1,287,292            |
| Indonesian Rupiah        | -                 | -                    | 901,154                     | -                            | 901,154              |
| Norwegian Krone          | -                 | -                    | 606,713                     | 154,462                      | 761,175              |
| Polish Zloty             | 3,002             | 58,474               | 639,731                     | -                            | 701,207              |
| Various other currencies | -                 | -                    | 506,963                     | -                            | 506,963              |
| <b>Total</b>             | <b>\$ 304,042</b> | <b>\$ 16,129,704</b> | <b>\$ 150,242,406</b>       | <b>\$ 25,862,779</b>         | <b>\$192,538,931</b> |

### Credit Risk of Debt Securities

Credit risk is the risk that an issuer or other counter party to an investment will not fulfill its obligation to the System. Below is a list of fixed income credit quality ratings as of September 30,:

| Quality rating           | 2017                  | 2016                  |
|--------------------------|-----------------------|-----------------------|
|                          | Fair value            | Fair Value            |
| Aaa/U.S. Governments     | \$ 80,328,519         | \$ 84,319,481         |
| Aa                       | 6,702,413             | 8,196,529             |
| A                        | 25,984,121            | 25,521,778            |
| Baa                      | 3,919,671             | 4,446,259             |
| Below Baa                | 55,756,649            | 47,545,868            |
| Not rated                | 301,513               | 277,890               |
| <b>Total credit risk</b> | <b>\$ 172,992,886</b> | <b>\$ 170,307,805</b> |

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

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### Interest Rate Risk

The System does not have a formal policy to limit interest rate risk. Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Duration is a measure of a debt instrument's exposure to a change in interest rates and the related sensitivity of market price to parallel shifts in the yield curve. It uses the present value of cash flows, weighted for those cash flows as a percentage of the instruments' full price. The following schedule provides a summary of interest risk assumed by the System as of September 30,:

| Investment               | 2017                  |                    | 2016                  |                    |
|--------------------------|-----------------------|--------------------|-----------------------|--------------------|
|                          | Fair value            | Effective duration | Fair value            | Effective duration |
| Payden and Rygel         | \$ 32,219,790         | 6.56 years         | \$ 31,764,183         | 6.58 years         |
| Allegiant (PNC)          | 54,600,077            | 6.49 years         | 54,559,755            | 6.58 years         |
| SSGA                     | 35,754,259            | 5.98 years         | 35,722,077            | 5.52 years         |
| Loomis                   | 30,141,314            | 4.23 years         | 27,789,116            | 4.36 years         |
| Vanguard                 | 20,267,446            | 8.00 years         | 20,472,674            | 6.80 years         |
| Total interest rate risk | <u>\$ 172,982,886</u> |                    | <u>\$ 170,307,805</u> |                    |

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

### NOTE 4 – INVESTMENTS AND DERIVATIVE INSTRUMENTS MEASURED AT FAIR VALUE

The System categorizes its fair value measurements within the fair value hierarchy established by accounting principles generally accepted in the United States of America. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs.

The System has the following recurring fair value measurements at September 30, 2017:

|   | <u>Total</u>          | <u>Level 1</u>        | <u>Level 2</u>       | <u>Level 3</u> |
|---|-----------------------|-----------------------|----------------------|----------------|
| Investments by fair value level                   |                       |                       |                      |                |
| Fixed income securities                           |                       |                       |                      |                |
| U.S. Government securities                        | \$ 23,427,866         | \$ 20,388,612         | \$ 3,039,254         | \$ -           |
| Corporate bonds                                   | 30,335,607            | -                     | 30,335,607           | -              |
| Domestic bond funds                               | 11,406,226            | 11,406,226            | -                    | -              |
| International bonds and securities                | 31,650,630            | 1,630,402             | 30,020,228           | -              |
| Other debt obligations                            | 20,267,446            | 20,267,446            | -                    | -              |
| Equity securities                                 |                       |                       |                      |                |
| Common stocks                                     | 198,735,935           | 198,735,935           | -                    | -              |
| Managed master limited partnerships               | 44,792,227            | 44,792,227            | -                    | -              |
| Total investments by fair value level             | 360,615,937           | <u>\$ 297,220,848</u> | <u>\$ 63,395,089</u> | <u>\$ -</u>    |
| Investments measured at the net asset value (NAV) |                       |                       |                      |                |
| Loomis High Yield Conservative Trust (B)          | 30,151,313            |                       |                      |                |
| SSGA Passive Bond Market Index (NL) Fund          | 35,754,259            |                       |                      |                |
| Principal Real Estate Group Annuity Contract      | 88,420,093            |                       |                      |                |
| Acadian Emerging Markets Mutual Equity Fund II    | 59,031,533            |                       |                      |                |
| Silchester International Value Equity Group Trust | 93,145,776            |                       |                      |                |
| Walter Scott Group Trust International            | 41,433,930            |                       |                      |                |
| Kabouter International Opportunites Fund II       | 31,774,962            |                       |                      |                |
| Entrust Capital Diversified Fund                  | 34,576,947            |                       |                      |                |
| Weatherlow Offshore Fund I                        | 41,302,502            |                       |                      |                |
| Total investments measured at NAV                 | <u>455,591,315</u>    |                       |                      |                |
| Total investments measured at fair value          | <u>\$ 816,207,252</u> |                       |                      |                |
| Investment derivative instruments                 |                       |                       |                      |                |
| Foreign exchange contracts                        | <u>\$ 340,750</u>     |                       | <u>\$ 340,750</u>    |                |

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

The System has the following recurring fair value measurements at September 30, 2016:

|   | <u>Total</u>          | <u>Level 1</u>        | <u>Level 2</u>       | <u>Level 3</u> |
|---|-----------------------|-----------------------|----------------------|----------------|
| Investments by fair value level                   |                       |                       |                      |                |
| Fixed income securities                           |                       |                       |                      |                |
| U.S. Government securities                        | \$ 23,680,590         | \$ 20,438,688         | \$ 3,241,902         | \$ -           |
| Corporate bonds                                   | 29,987,239            | -                     | 29,987,239           | -              |
| Domestic bond funds                               | 20,472,674            | 20,472,674            | -                    | -              |
| International bonds and securities                | 31,538,093            | 1,275,993             | 30,262,100           | -              |
| Other debt obligations                            | 10,288,825            | 10,288,825            | -                    | -              |
| Equity securities                                 |                       |                       |                      |                |
| Common stocks                                     | 183,836,061           | 183,836,061           | -                    | -              |
| Managed master limited partnerships               | 46,154,213            | 46,154,213            | -                    | -              |
| Total investments by fair value level             | 345,957,695           | <u>\$ 282,466,454</u> | <u>\$ 63,491,241</u> | <u>\$ -</u>    |
| Investments measured at the net asset value (NAV) |                       |                       |                      |                |
| Loomis High Yield Conservative Trust (B)          | 27,789,119            |                       |                      |                |
| SSGA Passive Bond Market Index (NL) Fund          | 35,722,077            |                       |                      |                |
| Principal Real Estate Group Annuity Contract      | 92,764,744            |                       |                      |                |
| Acadian Emerging Markets Mutual Equity Fund II    | 46,633,058            |                       |                      |                |
| Kabouter International Opportunities Fund II      | 25,896,602            |                       |                      |                |
| Silchester International Value Equity Group Trust | 75,518,115            |                       |                      |                |
| Walter Scott Group Trust International            | 40,567,561            |                       |                      |                |
| Entrust Capital Diversified Fund                  | 33,983,828            |                       |                      |                |
| Weatherlow Offshore Fund I                        | 39,676,400            |                       |                      |                |
| Total investments measured at NAV                 | <u>418,551,504</u>    |                       |                      |                |
| Total investments measured at fair value          | <u>\$ 764,509,199</u> |                       |                      |                |
| Investment derivative instruments                 |                       |                       |                      |                |
| Foreign exchange contracts                        | <u>\$ 33,914</u>      |                       | <u>\$ 33,914</u>     |                |

The following is a description of the valuation methodologies used by the System to measure assets at estimated fair value. There were no changes in the methodologies used at September 30, 2017 and 2016.

Fixed income and equity securities classified in Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities.

Fixed income securities classified in Level 2 of the fair value hierarchy are valued using matrix pricing based on quotes from independent pricing services using recent trading activity information including market interest rate curves, dealer quotes, the U.S. Treasury yield curve and bond terms and conditions. Derivative instruments classified in Level 2 of the fair value hierarchy are valued using a market approach that considers foreign exchange rates.

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

The valuation methods for investments measured at the net asset value (NAV) per share (or its equivalent) as provided by the investee entity or fund manager is presented on the following table.

|   | Fair<br>value<br>2017 | Fair<br>value<br>2016 | Unfunded<br>commitments | Redemption<br>frequency (if<br>currently eligible) | Redemption<br>notice<br>period |
|---|-----------------------|-----------------------|-------------------------|--|--------------------------------|
| Loomis High Yield Conservative Trust (B)          | \$ 30,151,313         | \$ 27,789,119         | n/a                     | Daily  | Daily                          |
| SSGA Passive Bond Market Index (NL) Fund          | 35,754,259            | 35,722,077            | n/a                     | Monthly  | 15 days                        |
| Principal Real Estate Group Annuity Contract      | 88,420,093            | 92,764,744            | n/a                     | Daily  | 7 days                         |
| Acadian Emerging Markets Mutual Equity Fund II    | 59,031,533            | 46,633,058            | n/a                     | Daily  | 30 days                        |
| Kabouter International Opportunities Fund II      | 31,774,962            | 25,896,602            | n/a                     | Daily  | 15 - 30 days                   |
| Silchester International Value Equity Group Trust | 93,145,776            | 75,518,115            | n/a                     | Monthly  | 5 - 10 days                    |
| Walter Scott Group Trust International            | 41,433,930            | 40,567,561            | n/a                     | Daily  | 10 days                        |
| Entrust Capital Diversified Fund                  | 34,576,947            | 33,983,828            | n/a                     | Quarterly  | 90 days                        |
| Weatherlow Offshore Fund I                        | 41,302,502            | 39,676,400            | n/a                     | Quarterly  | 65 days                        |
| Total investments measured at NAV                 | <u>\$455,591,315</u>  | <u>\$418,551,504</u>  |                         |  |                                |

*Loomis High Yield Conservative Trust (B).* The fund may invest up to 100% of its market value in fixed income securities of any credit quality, including lower rated fixed income securities and up to 20% of its market value in non-U.S. currencies. The fund may also invest in fixed income securities of any maturity. The fair values of the investments in this fund have been determined using the NAV per share (or its equivalent) of the underlying investments.

*State Street Global Advisors Passive Bond Market Index (NL) Fund.* The investment objective of the fund is to approximate as closely as practicable, before expenses, the performance of the Barclays U.S. Aggregate Bond Index over the long term. The fund attempts to achieve its investment objective by investing in other collective investment funds, each an underlying fund, managed by the Trustee, which have characteristics consistent with the fund's overall investment objective. The fair values of the investments in this fund have been determined using the NAV per share (or its equivalent) of the underlying investments.

*Principal Global Investors Real Estate Group Annuity Contract.* Is a pooled separate account for investment and reinvestment in owned real estate, such as office buildings, industrial buildings, shopping centers, retail stores and similar property and in accordance with applicable law. The fair values of the investments in this fund have been determined using the NAV per share (or its equivalent) of the underlying investments as reported by the fund manager. The fund reserves the right to defer payments that would exceed the amount of cash and other liquid assets held by the fund, reduced by amounts committed to purchase properties or needed for operating expenses. The fund will not defer requested payments for longer than three years.

*Acadian Emerging Markets Mutual Equity Fund II.* The fund's objective is to seek long-term capital appreciation by investing primarily in common stocks of emerging markets issuers. The fair values of the investments in this fund have been determined using the NAV per share (or its equivalent) of the underlying investments.



# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

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*Kabouter International Opportunities Fund II.* The primary purpose of the fund is to provide diversification while still providing the opportunity for capital appreciation. A low correlation between stocks, bonds, hedge funds, and real estate creates reduced portfolio volatility. The fair values of the investments in this fund have been determined using the NAV per share (or its equivalent) of the underlying investments.

*Silchester International Value Equity Group Trust.* The trust principally invests in a diversified portfolio of equity securities of companies ordinarily incorporated in any country other than the United States. The fair values of the investments in this fund have been determined using the NAV per share (or its equivalent) of the underlying investments. The trust may delay payment if the investment manager determines that such delay is reasonably necessary to prevent such redemption from having a material adverse impact on the group trust and/or the remaining participating trusts.

*Walter Scott Group Trust International.* The investment manager is authorized to allocate the assets without limitation among geographic regions and individual countries (other than the United States) based on its analysis of global economic, political and financial conditions. Not more than 5% of the fund's assets shall be invested in stocks domiciled or listed on exchanges in countries not included in the MSCI World index other than Canada, the republic of South Africa and Chinese stocks listed on the Hong Kong exchange. The fair values of the investments in this fund have been determined using the NAV per share (or its equivalent) of the underlying investments. Under certain circumstances (including the inability of a fund to liquidate positions or the default or delay in payments due to a fund from brokers, banks, or other persons), a fund may delay payment to an investor requesting redemption of the proportionate part of the NAV of the units being redeemed which represents sums which are the subject of such default or delay, or the fund may distribute property in kind as determined by the investment manager in payment of a redemption of units.

*Entrust Capital Diversified Fund.* The Fund seeks to achieve above-average rates of return and long-term capital growth. The Fund seeks to achieve this objective by employing a multi-manager approach, maintaining investments through private investment entities and/or separately managed accounts with a broadly diversified group of investment management professionals specializing in alternative investment strategies. The Fund does not follow a rigid asset allocation policy but seeks diversification through a combination of managers trading a range of strategies, including but not limited to, hedging, distressed securities, arbitrage, and special situations. The fair values of the investments in this fund have been determined using the NAV per share (or its equivalent) of the underlying investments.

*Weatherlow Offshore Fund I.* The fund's investment objective is to achieve long-term returns commensurate with long term returns from a portfolio invested in the general equity markets, while experiencing volatility more like that of a portfolio invested in the general debt markets. The fund seeks to achieve this objective by investing predominantly in interests in portfolio funds - i.e., limited partnerships and similar pooled invested vehicles often referred to as "hedge funds" - managed by portfolio managers. The fair values of the investments in this fund have been determined using the NAV per share (or its equivalent) of the underlying investments.

# **EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS**

## **NOTES TO THE FINANCIAL STATEMENTS**

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### **NOTE 5 – PLAN TERMINATION**

The System is administered in accordance with the provisions of the Revised Code of the City of St. Louis. There are currently no plans to terminate the System.

### **NOTE 6 – DEFERRED RETIREMENT OPTION PLAN**

On June 8, 2000, the Mayor of the City of St. Louis approved an ordinance passed by the Board of Alderman, authorizing a Deferred Retirement Option Plan (DROP), which became effective January 1, 2001. This plan allows for members to work for an additional 5 years after reaching retirement age and defer receipt of their retirement allowance. The calculation of average salary for retirement benefits will not include the additional years of service after normal retirement age. The amount that would have been received as retirement benefit is put in a special DROP account monthly. Total DROP expense was \$10,010,958 and \$9,589,688 for the years ended September 30, 2017 and 2016, respectively. The DROP account will not be adjusted for cost of living increases.

The DROP account earns interest at the actuarial valuation rate of return and at the 10-year U.S. Treasury Bond yield as of each September 30, for DROP participants enrolling February 1, 2003 and thereafter.

After a member completely terminates employment, the member can withdraw amounts from the DROP account in a lump sum or according to a deferred retirement payment plan. At September 30, 2017 and 2016, approximately 798 and 795 members, respectively, have elected DROP participation and have DROP account balances of approximately \$50,902,700 and \$53,279,800, respectively.

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

### NOTE 7 – ACTUARIAL METHODS AND SIGNIFICANT ASSUMPTIONS

| Valuation date         | October 1, 2017  | October 1, 2016  |
|------------------------|--|--|
| Timing                 | Actuarially determined contribution rates are calculated based on the actuarial valuation at the beginning of the year   | Actuarially determined contribution rates are calculated based on the actuarial valuation at the beginning of the year   |
| Actuarial cost method  | Entry age normal   | Entry age normal   |
| Asset valuation method | 5 year smoothing   | 5 year smoothing   |
| Amortization method    | Layered 20 year amortization of unfunded liability   | Layered 20 year amortization of unfunded liability   |
| Discount rate          | 7.50%  | 7.50%  |
| Inflation              | 2.50%  | 2.50%  |
| Salary increases       | Varies by service, ranging from 3.00% to 4.25%   | Varies by service, ranging from 3.00% to 4.25%   |
| Mortality              | Healthy: RP-2000 Healthy Mortality 3-year set-forward with generational projections using Scale AA<br>Disabled: RP-2000 Disabled Mortality 3-year set-forward with generational projections using Scale AA | Healthy: RP-2000 Healthy Mortality 3-year set-forward with generational projections using Scale AA<br>Disabled: RP-2000 Disabled Mortality 3-year set-forward with generational projections using Scale AA |

A single discount rate of 7.50% was used to measure the pension liability. This single discount rate was based on the expected rate of return on the System's investments of 7.50%. This single discount rate is net of investment expenses (investment manager and custodial fees). The projection of cash flows used to determine this single discount rate assumed the City of St. Louis and other participating employers would make the required contributions as defined by Statute. Based on these assumptions, the System's fiduciary net position was projected to be available to make all projected future benefit payments of current members and their beneficiaries. Therefore, the long-term expected rate of return on the System's investments was applied to all periods of projected benefit payments to determine the total pension liability.

GASB 67 requires the disclosure of the sensitivity of the net pension liability to changes in the discount rate. For calculations of total pension liability, the actuary has used an assumed long-term expected rate of return of 7.50%. The table below presents the net pension liability if the discount rate were 1% lower or 1% higher than the current rate.

|   | 1% decrease<br>6.50%  | Current<br>discount rate<br>7.50% | 1% increase<br>8.50% |
|---|-----------------------|-----------------------------------|----------------------|
| Total pension liability   | \$ 1,089,567,901      | \$ 990,630,355                    | \$ 905,982,281       |
| Fiduciary net position  | 816,915,650           | 816,915,650                       | 816,915,650          |
| Net pension liability   | <u>\$ 272,652,251</u> | <u>\$ 173,714,705</u>             | <u>\$ 89,066,631</u> |
| System fiduciary net position as a<br>percentage of total pension liability | 75.0%                 | 82.5%                             | 90.2%                |

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE FINANCIAL STATEMENTS

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### NOTE 8 – COMMITMENTS AND CONTINGENCIES

The System has been served with a complaint filed by the unsecured creditor's committee of the bankrupt Tribune Company regarding the System's sale of Tribune Company securities during a leveraged takeover of the Tribune Company by an ESOP (Employee Stock Ownership Plan). The total proceeds of the sale were approximately \$306,000. The unsecured creditor's committee or its trustee has filed a petition alleging the sale of the securities to the ESOP or its affiliates worked a fraud upon the creditors who lent the ESOP the funds to purchase the securities based upon fraudulent or misrepresented information from other parties to the litigation. Certain senior note-holders of the Tribune Company and certain Tribune Company retirees have joined the litigation and made claims substantially similar to the unsecured creditor's committee. These claims have been consolidated into a federal multi-jurisdictional case in the U.S. District Court for the Southern District of New York. The note-holder's claims have been dismissed by the Court and that decision was upheld by the U.S. Second Circuit Court of Appeals. This decision is currently on appeal to the U.S. Supreme Court, which has yet to grant certiorari. Should the appeal by the note-holders be successful, the claims of the note-holders would be reinstated in the multi-jurisdictional case. The remaining bankruptcy claims have been dismissed by the Court for lack of scienter and the failure to state a claim upon which relief can be granted. However, this recent decision may be taken up on appeal. The System has engaged Armstrong Teasdale, LLP to represent the System's interests. Any evaluation of the potential outcome of such litigation would be speculative. However, in the event of an unlikely outcome most favorable to the plaintiffs, the System expects that the plaintiff's damages would be limited to the proceeds of the sales plus interest from date of judgement.

During the year ended September 30, 2017, the System, the members of its Board of Trustees and the City of St. Louis were served with an Amended Petition by a city employee, who alleges that in December, 1988 the System's Board of Trustees wrongfully adopted a resolution determining that certain City of St. Louis elected positions could no longer be a member of the System. The plaintiff asserts the Board resolution violates a state statute which would allow certain elected positions to receive pension benefits from both the statewide and local plans. Subsequent to the original filing of the petition, another plaintiff joined the suit. The petitioners are seeking payment of the pension benefits believed due to them. The System has made a claim for indemnification and defense from its fiduciary insurer (with the permission of its fiduciary insurer) and engaged Bryan Cave, LLP to vigorously defend the System and the members of its Board of Trustees. It is important to note that the System did not receive any employer contributions attributable to the petitioners' compensation after the date of the resolution of the Board of Trustees and the System filed a counterclaim against the City of St. Louis averring that in the event the System is liable to the petitioners, the City of St. Louis owes the System the employer contributions (plus interest) attributable to the petitioners' compensation while serving the City in the elected positions by the City.

**EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS**

**NOTES TO THE FINANCIAL STATEMENTS**

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**NOTE 9 – RISKS AND UNCERTAINTIES**

The System invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, foreign currency, regulatory, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term, and such changes could materially affect the amounts reported in the statements of fiduciary net position.

Total pension liability is reported based on certain assumptions pertaining to interest rates, inflation rates, and employee demographics, all of which are subject to change. Due to uncertainties inherent in the estimations and assumptions process, it is at least reasonably possible that changes in these estimates and assumptions in the near term would be material to the financial statements.

## EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

### SCHEDULE OF CHANGES IN EMPLOYER NET PENSION LIABILITY - UNAUDITED

|  | September 30,  |                |                |                |
|--|----------------|----------------|----------------|----------------|
|  | 2017           | 2016           | 2015           | 2014           |
| Total pension liability  |                |                |                |                |
| Service cost   | \$ 13,185,412  | \$ 13,703,072  | \$ 13,067,553  | \$ 10,591,910  |
| Interest   | 71,206,835     | 69,893,488     | 73,825,307     | 72,012,146     |
| Difference between expected and actual experience                      | (4,372,137)    | (3,601,576)    | (2,701,109)    | (3,664,735)    |
| Change of assumptions  | -              | -              | (5,107,330)    | -              |
| Benefit payments   | (63,532,834)   | (60,972,546)   | (59,065,812)   | (56,317,073)   |
| Net change in total pension liability                                  | 16,487,276     | 19,022,438     | 20,018,609     | 22,622,248     |
| Total pension liability, beginning                                     | 974,143,079    | 955,120,641    | 935,102,032    | 912,479,784    |
| <br>   |                |                |                |                |
| Total pension liability, ending (a)                                    | 990,630,355    | 974,143,079    | 955,120,641    | 935,102,032    |
| <br>   |                |                |                |                |
| Plan fiduciary net position  |                |                |                |                |
| Employer contributions   | 29,782,200     | 32,127,591     | 35,436,141     | 36,788,260     |
| Member contributions   | 134,248        | 10,093         | 289,810        | 129,164        |
| Net investment income  | 86,394,236     | 66,460,934     | (28,435,882)   | 70,076,027     |
| Benefit payments   | (63,532,834)   | (60,972,546)   | (59,065,812)   | (56,317,073)   |
| Administrative expenses  | (763,273)      | (722,132)      | (722,758)      | (670,957)      |
| Net change in plan fiduciary net position                              | 52,014,577     | 36,903,940     | (52,498,501)   | 50,005,421     |
| Plan fiduciary net position, beginning                                 | 764,901,073    | 727,997,133    | 780,495,634    | 730,490,213    |
| Plan fiduciary net position, ending (b)                                | 816,915,650    | 764,901,073    | 727,997,133    | 780,495,634    |
| <br>   |                |                |                |                |
| Net pension liability, ending = (a) - (b)                              | \$ 173,714,705 | \$ 209,242,006 | \$ 227,123,508 | \$ 154,606,398 |
| <br>   |                |                |                |                |
| Plan fiduciary net position as a percentage of total pension liability | 82.46%         | 78.52%         | 76.22%         | 83.47%         |
| Covered employee payroll   | 239,583,848    | 237,354,364    | 238,385,100    | 237,794,875    |
| Net pension liability as a percentage of covered employee payroll      | 72.51%         | 88.16%         | 95.28%         | 65.02%         |

Note: Schedule is intended to show information for 10 years. Additional years will be displayed as they become available.

See accompanying independent auditors' report and notes to the schedules of required supplementary information.



**EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS**

**SCHEDULE OF NET PENSION LIABILITY - UNAUDITED**

|   | September 30,         |                       |                       |                       |
|---|-----------------------|-----------------------|-----------------------|-----------------------|
|   | 2017                  | 2016                  | 2015                  | 2014                  |
| Total pension liability   | \$ 990,630,355        | \$ 974,143,079        | \$ 955,120,641        | \$ 935,102,032        |
| Plan fiduciary net position   | 816,915,650           | 764,901,073           | 727,997,133           | 780,495,634           |
| Net pension liability   | <u>\$ 173,714,705</u> | <u>\$ 209,242,006</u> | <u>\$ 227,123,508</u> | <u>\$ 154,606,398</u> |
| Plan fiduciary net position as a percentage<br>of total pension liability | 82.46%                | 78.52%                | 76.22%                | 83.47%                |
| Covered employee payroll  | \$ 239,583,848        | \$ 237,354,364        | \$ 238,385,100        | \$ 237,794,875        |
| Net pension liability as a percentage<br>of covered employee payroll      | 72.51%                | 88.16%                | 95.28%                | 65.02%                |

*Note: Schedule is intended to show information for 10 years. Additional years will be displayed as they become available.*

See accompanying independent auditors' report and notes to the schedules of required supplementary information.

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## SCHEDULE OF EMPLOYER CONTRIBUTIONS - UNAUDITED

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| <u>System year ended<br/>September 30,</u> | <u>Actuarially<br/>determined<br/>contribution</u> | <u>Contribution<br/>in relation to<br/>the actuarially<br/>determined<br/>contribution</u> | <u>Contribution<br/>deficiency<br/>(excess)</u> | <u>Covered<br/>employee<br/>payroll</u> | <u>Contribution<br/>as a percentage<br/>of covered<br/>payroll</u> |
|--|--|--|---|---|--|
| 2014                                       | \$34,060,798                                       | \$36,788,260   | \$(2,727,462)                                   | \$237,794,875                           | 15.47%   |
| 2015                                       | 31,605,493   | 35,436,141   | (3,830,648)                                     | 238,385,100                             | 14.87%   |
| 2016                                       | 28,534,042   | 32,127,591   | (3,593,549)                                     | 237,354,364                             | 13.54%   |
| 2017                                       | 27,684,090   | 29,782,200   | (2,098,110)                                     | 239,583,848                             | 12.43%   |

*Note: Schedule is intended to show information for 10 years. Additional years will be displayed as they become available.*

See accompanying independent auditors' report and notes to the schedules of required supplementary information.

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## SCHEDULE OF ANNUAL MONEY-WEIGHTED RATE OF RETURN ON INVESTMENTS - UNAUDITED

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| <u>System year<br/>ended September 30,</u> | <u>Annual money weighted rate of return<br/>net of investment expense</u> |
|--|---|
| 2014                                       | 9.71  |
| 2015                                       | -3.79%  |
| 2016                                       | 9.45%   |
| 2017                                       | 11.90%  |

*Note: Schedule is intended to show information for 10 years. Additional years will be displayed as they become available.*

See accompanying independent auditors' report and notes to the schedules of required supplementary information.

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE SCHEDULES OF REQUIRED SUPPLEMENTARY INFORMATION

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### NOTE 1 – METHODS AND ASSUMPTIONS USED IN CALCULATIONS OF ACTUARIALLY DETERMINED CONTRIBUTIONS

#### Actuarial Methods and Assumptions

The actuarially determined contribution rates in the schedule of the System's contributions are calculated based on the actuarial valuation at the beginning of the plan year. The following actuarial methods and assumptions were used to determine contribution rates reported in that schedule.

|                        | <u>September 30, 2017</u>  |
|------------------------|--|
| Actuarial cost method  | Entry age normal   |
| Asset valuation method | 5 year smoothing   |
| Amortization method    | Layered 20-year amortization of unfunded liability   |
| Discount rate          | 7.50%  |
| Inflation              | 2.50%  |
| Salary increases       | 3% plus merit component based on years of service  |
| Mortality              | Healthy: RP-2000 Healthy Mortality 3-year set-forward with generational projections using Scale AA<br>Disabled: RP-2000 Disabled Mortality 3-year set-forward with generational projections using Scale AA |
|                        | <u>September 30, 2016</u>  |
| Actuarial cost method  | Entry age normal   |
| Asset valuation method | 5 year smoothing   |
| Amortization method    | Layered 20-year amortization of unfunded liability   |
| Discount rate          | 7.50%  |
| Inflation              | 2.50%  |
| Salary increases       | 3% plus merit component based on years of service  |
| Mortality              | Healthy: RP-2000 Healthy Mortality 3-year set-forward with generational projections using Scale AA<br>Disabled: RP-2000 Disabled Mortality 3-year set-forward with generational projections using Scale AA |
|                        | <u>September 30, 2015</u>  |
| Actuarial cost method  | Projected unit credit method   |
| Asset valuation method | 5 year smoothing   |
| Amortization method    | Rolling 30-year level dollar amortization of unfunded liability  |
| Discount rate          | 8.00%  |
| Inflation              | 3.125%   |
| Salary increases       | 3.50% plus merit component based on years of service   |
| Mortality              | Healthy: 1994 Group Annuity Mortality Table<br>Disabled: 1983 Railroad Retirement Board Disabled Life Mortality Table  |

# EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

## NOTES TO THE SCHEDULES OF REQUIRED SUPPLEMENTARY INFORMATION

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**September 30, 2014**

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|                        |   |
|------------------------|---|
| Actuarial cost method  | Projected unit credit method  |
| Asset valuation method | 5 year smoothing  |
| Amortization method    | Rolling 30-year level dollar amortization of unfunded liability   |
| Discount rate          | 8.00%   |
| Inflation              | 3.125%  |
| Salary increases       | Varies by age from 3.50% to 7.017%  |
| Mortality              | Healthy: 1994 Group Annuity Mortality Table<br>Disabled: 1983 Railroad Retirement Board Disabled Life Mortality Table |

*Note: Periods prior to September 30, 2016 were audited by other auditors and this information from these actuary report were not obtained.*

## EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

### ANALYSIS OF FINANCIAL EXPERIENCE

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**Gain and loss in unfunded actuarial liability during years ended September 30 resulting from  
differences between assumed experience and actual experience**

|   | Year Ending September 30, |                     |                      |                      |                     |                       |
|---|---------------------------|---------------------|----------------------|----------------------|---------------------|-----------------------|
|   | 2017                      | 2016                | 2015                 | 2014                 | 2013                | 2012                  |
| Investment experience                             | \$(3,004,069)             | \$ 553,258          | \$ (2,743,842)       | \$ 17,899,526        | \$ (87,586)         | \$(42,041,794)        |
| Liability experience                              | 4,322,571                 | 3,695,678           | 6,114,189            | 7,265,891            | 8,391,763           | 7,779,666             |
| Gain (loss) during year from financial experience | 1,318,502                 | 4,248,936           | 3,370,347            | 25,165,417           | 8,304,177           | (34,262,128)          |
| Non-recurring gain items                          | -                         | -                   | 20,389,054           | -                    | -                   | -                     |
| Composite gain (loss) during year                 | <u>\$ 1,318,502</u>       | <u>\$ 4,248,936</u> | <u>\$ 23,759,401</u> | <u>\$ 25,165,417</u> | <u>\$ 8,304,177</u> | <u>\$(34,262,128)</u> |

See accompanying independent auditors' report.

## EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

### SOLVENCY TEST - AGGREGATE ACTUARIAL LIABILITIES

| Valuation date<br>October 1, | Active member contributions | Retirees & beneficiaries | Active member employer financed contributions | Actuarial value of reported assets | Portion of actuarial liabilities covered by reported assets |      |     |
|------------------------------|-----------------------------|--------------------------|---|------------------------------------|---|------|-----|
|                              | (1)                         | (2)                      | (3)   |                                    | (1)   | (2)  | (3) |
| 2017                         | \$ -                        | \$ 540,747,179           | \$ 449,883,176                                | \$ 818,839,562                     | 100%  | 100% | 62% |
| 2016                         | -                           | 517,161,890              | 456,981,189                                   | 797,664,391                        | 100%  | 100% | 61% |
| 2015                         | -                           | 501,123,197              | 453,997,444                                   | 770,006,025                        | 100%  | 100% | 59% |
| 2014                         | -                           | 494,664,459              | 417,314,687                                   | 737,967,928                        | 100%  | 100% | 58% |
| 2013                         | -                           | 475,937,321              | 413,511,258                                   | 685,397,323                        | 100%  | 100% | 51% |
| 2012                         | -                           | 460,581,077              | 406,310,985                                   | 653,001,852                        | 100%  | 100% | 47% |
| 2011                         | -                           | 441,520,555              | 400,242,766                                   | 661,932,240                        | 100%  | 100% | 55% |
| 2010                         | -                           | 419,717,802              | 400,951,838                                   | 671,608,995                        | 100%  | 100% | 63% |

*Note: Schedule is intended to show information for 10 years. Additional years will be displayed as they become available.*

See accompanying independent auditors' report.

## EMPLOYEES RETIREMENT SYSTEM OF THE CITY OF ST. LOUIS

### SCHEDULE OF FUNDING PROGRESS

| Actuarial<br>valuation date<br>October 1, | Actuarial<br>value of<br>assets | Actuarial<br>liability | Unfunded<br>actuarial<br>liability | Funded<br>ratio | Covered<br>pension payroll | Percentage of<br>covered<br>pension payroll |
|---|---------------------------------|------------------------|------------------------------------|-----------------|----------------------------|---|
| 2017                                      | \$ 818,839,562                  | \$ 990,630,355         | \$ 171,790,793                     | 82.66%          | \$ 227,253,901             | 75.59%                                      |
| 2016                                      | 797,664,391                     | 974,143,079            | 176,478,688                        | 81.88%          | 226,907,701                | 77.78%                                      |
| 2015                                      | 770,006,025                     | 955,120,641            | (185,114,616)                      | 80.62%          | 228,422,585                | 81.04%                                      |
| 2014                                      | 737,967,928                     | 911,979,146            | (174,011,218)                      | 80.92%          | 227,039,143                | 76.64%                                      |
| 2013                                      | 685,397,323                     | 889,448,579            | (204,051,256)                      | 77.06%          | 224,623,445                | 90.84%                                      |
| 2012                                      | 653,001,852                     | 866,890,445            | (213,888,593)                      | 75.33%          | 224,822,252                | 95.14%                                      |
| 2011                                      | 661,932,240                     | 841,763,321            | (179,831,081)                      | 78.64%          | 223,060,719                | 80.62%                                      |
| 2010                                      | 671,608,995                     | 820,669,641            | (149,060,646)                      | 81.84%          | 232,451,661                | 64.13%                                      |
| 2009                                      | 667,667,205                     | 794,686,379            | (127,019,174)                      | 84.02%          | 240,409,390                | 52.83%                                      |
| 2008                                      | 674,016,719                     | 765,842,026            | (91,825,307)                       | 88.01%          | 238,701,628                | 38.47%                                      |

See accompanying independent auditors' report.