



# Comprehensive Annual Financial Report

Fiscal Years Ended June 30, 2018 and 2017



**Kern County Employees' Retirement Association**

A defined benefit public pension plan

**Kern County Employees Retirement Association**  
A defined benefit public pension plan (California)

# **Comprehensive Annual Financial Report**

For Fiscal Years Ended June 30, 2018 and 2017

Issued by:

Dominic Brown, Executive Director

Sheryl Lawrence, Finance Officer

Angela Kruger, Accountant



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# TABLE OF CONTENTS

<b>Introductory Section</b>	<b>1</b>	<b>Actuarial Section</b>	<b>79</b>
Letter of Transmittal	3	Actuary's Certification Letter	81
Certificate of Achievement for Excellence in Financial Reporting	8	Summary of Actuarial Assumptions and Methods	84
Members of the Board of Retirement	9	Table 1: Assumed Rate of Salary Increase	86
Organizational Chart	10	Table 2: Probabilities of Separation from Active Service	87
Professional Consultants	11	Schedule of Active Member Valuation Data	88
		Schedule of Retirees and Beneficiaries	
<b>Financial Section</b>	<b>13</b>	Added to and Removed from Payroll	89
Independent Auditors' Report	14	Solvency Test	90
Management's Discussion and Analysis	17	Actuarial Analysis of Financial Experience	91
Basic Financial Statements		Schedule of Funding Progress	92
Statements of Fiduciary Net Position	22	Schedule of Employer Contributions	92
Statements of Changes in Fiduciary Net Position	23	Summary of Major Plan Provisions	93
Notes to Basic Financial Statements	24		
Required Supplementary Information		<b>Statistical Section</b>	<b>96</b>
Schedule of Changes in Net Pension Liability and Related Ratios	54	Statistical Section Overview	98
Schedule of Employer Contributions	55	Schedule of Changes in Fiduciary Net Position	99
Notes to Required Supplementary Information	56	Schedule of Benefit Expenses by Type	100
Schedule of Money-Weighted Rates of Return	56	Schedule of Retired Members by Type of Benefit	102
Other Supplemental Information		Schedule of Average Benefit Payment Amounts by Year of Retirement	103
Schedule of Administrative Expenses	57	Participating Employers and	
Schedule of Investment Expenses	59	Active Members	105
Schedule of Payments to Consultants	60		
<b>Investment Section</b>	<b>61</b>		
Investment Report	63		
Outline of Investment Policies	67		
Asset Allocation	68		
Investment Summary	69		
History of Performance	70		
History of Investment Earnings (Five-Year Smoothed Asset Valuation)	71		
Investment Results	72		
Investment Professionals	73		
Largest Stock and Bond Direct Holdings	74		
Assets Under Management	75		
Schedule of Investment Fees	76		

# **INTRODUCTORY**

## **Section**

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December 07, 2018

Dear Board Members:

As Executive Director of the Kern County Employees' Retirement Association (KCERA), I am pleased to present the Comprehensive Annual Financial Report (CAFR) for the fiscal years ended June 30, 2018 and 2017. This Letter of Transmittal is presented as a narrative introduction, overview and analysis in conjunction with the Management's Discussion and Analysis included in the Financial Section of the Comprehensive Annual Financial Report.

KCERA is a public employee retirement system that was established on January 1, 1945 by the County of Kern. The KCERA Plan provides retirement, disability, death, beneficiary, cost-of-living and supplemental retirement benefits. For the fiscal year ended June 30, 2018, KCERA had 10,281 active and deferred-vested members and paid retirement benefits to 8,296 retirees and their beneficiaries.



### **KCERA AND ITS SERVICES**

KCERA was established on January 1, 1945 to provide retirement allowances and other benefits to all permanent general and safety employees of the County of Kern and of participating special districts. As of June 30, 2018, fourteen districts participated in the retirement plan: Berrenda Mesa Water District, Buttonwillow Recreation and Park District, East Kern Cemetery District, Inyokern Community Services District, Kern County Hospital Authority, Kern County Superior Court, Kern County Water Agency, Kern Mosquito and Vector Control District, North of the River Sanitation District, San Joaquin Valley Air Pollution Control District, Shafter Recreation and Park District, West Side Cemetery District, West Side Mosquito and Vector Control District, and West Side Recreation and Park District.

The Plan is administered by the Kern County Board of Retirement (Board), which consists of nine members and two alternate members. The Board is responsible for establishing policies governing the administration of the retirement plan, determining benefit allowances and managing the investments of KCERA's assets. The Board oversees the Executive Director and the KCERA staff in the performance of their duties in accordance with the County Employees' Retirement Law of 1937 and the regulations, procedures and policies adopted by the KCERA Board.

## MAJOR INITIATIVES

### KCERA Reorganization and Recruitments

KCERA management engaged in a full-scale reorganization to better accomplish the mission of the organization. A multi-phase plan was developed with County Human Resources and approved by the County of Kern Board of Supervisors. As a result, the former Retirement Investment Officer was upgraded to Chief Investment Officer. In addition, a new Retirement Investment Officer position was created to assist in the management of the \$4.2 billion fund. General clerical positions were replaced with new classifications with job descriptions specific to KCERA, resulting in more successful recruitments. A new accountant position was added, as well as a paralegal to assist the General Counsel and the Member Services section.

### New Chief Investment Officer

Following a nationwide recruitment, KCERA announced the appointment of Daryn Miller as the plan's new Chief Investment Officer. Mr. Miller is responsible for overseeing KCERA's investment program, including risk management, investment manager oversight, due diligence, and investment policies and objectives. Before joining KCERA, Mr. Miller served as Interim Chief Investment Officer at the City of San Jose's two public pension plans. Mr. Miller also spent five years at Goldman Sachs as a vice president in equity research. He earned an MBA from the University of Southern California, a BA from Vanguard University and a Chartered Financial Analyst designation.

### Board Hires Executive Director

Following a nationwide recruitment, the Board of Retirement appointed Dominic Brown as KCERA's new Executive Director in March 2018. Mr. Brown, had previously served as KCERA's Assistant Executive Director. Before joining KCERA in 2016, he spent eight years as a division chief in the office of the Kern County Auditor-Controller. Earlier in his career, Mr. Brown was as Assistant Controller for a Fortune 500 construction company and previously worked at multiple CPA firms. He served one term on the KCERA board, including one year as Chairman. He earned a MS in Business Administration (Accounting) from Biola University, and is a Certified Public Accountant and Certified Fraud Examiner.

### Disability Application Process

As part of its ongoing effort to improve the effective and efficient processing of disability applications and to improve external communications, KCERA surveyed applicants and implemented many improvements. Furthermore, the Board actively approved outsourcing elements of the disability application process in the next fiscal year to further improve efficiency and resource management.

### KCERA Investment Program Highlights

In June 2018 the KCERA Board completed an asset liability study, and decided to maintain the current asset allocation. A review of portfolio implementation led to a number of initiatives including: repositioning the equity portfolio, reducing the investment manager line-up in the hedge fund program, adjusting policy benchmarks, and fine-tuning the commodity portfolio. In addition, KCERA committed additional capital into alternatives, specifically hedge funds, private credit and private real estate.

### KCERA Lean Six Sigma Initiatives

KCERA is actively participating in Kern County's Launch Kern program. Launch Kern is the application of Lean Six Sigma methods and tools to make county government faster, better, and stronger. KCERA conducted in-house training to educate staff in the identification and elimination of waste (Lean), as well as, process improvement (Six Sigma). Staff completed a total of thirteen "Quick-Win" projects, more than any other Kern County Department. Notable projects include introducing a Helpdesk IT ticketing system, implementing a phone auto attendant, and streamlining or eliminating a number of outdated reports.

## **FUNDING**

KCERA's funding objective is to meet long-term benefit obligations through level contributions to the Plan and the accrual and compounding of investment income. As of June 30, 2017, the funded ratio of the Plan was 63.2% using actuarial assets and actuarial liabilities of \$3,913,073,000 and \$6,191,433,000, respectively. The funded percentage decreased 0.2% from June 30, 2016 due primarily to the adoption of new actuarial assumptions and actual contributions less than expected.

Pursuant to provisions in the County Employees' Retirement Law of 1937, KCERA engages an independent actuarial consulting firm, Segal Consulting, to conduct annual actuarial valuations. Every three years, an experience study is performed to review all economic and demographic assumptions. The economic and demographic assumptions are updated at the time each triennial valuation is performed. Triennial valuations serve as the basis for changes in member and employer contribution rates necessary to properly fund the Plan. The last triennial analysis was performed as of June 30, 2016.

The triennial analysis covered several changes to economic and non-economic assumptions that were adopted by the Board of Retirement on July 12, 2017 for the June 30, 2017 actuarial valuation. The actuary recommended changes in the assumptions for inflation, investment return, promotional and merit salary increases, retirement from active employment, percent married, spousal age difference, mortality, termination, disability incidence, percent of members assumed to work under a reciprocal system, and reciprocal salary increases. The major changes included lowering the inflation assumption from 3.25% to 3.0%, lowering the investment return assumption from 7.5% to 7.25%, and changing the mortality tables to a headcount-weighted generational approach.

## **FINANCIAL INFORMATION**

The Comprehensive Annual Financial Report (CAFR) for the fiscal years June 30, 2018 and 2017 was prepared by KCERA's management, which is responsible for the accuracy, completeness, fair presentation of information and all disclosures in this report. The report has been prepared in accordance with accounting principles generally accepted in the United States of America as promulgated by the Governmental Accounting Standards Board (GASB).

KCERA maintains an internal control system to provide reasonable assurance that assets are properly safeguarded from loss, theft or misuse, and the fair presentation of the financial statements and supporting schedules. Further, it should be recognized that there are inherent limitations in the effectiveness of any system of internal controls due to changes in conditions. Moreover, the concept of reasonable assurance recognizes that the cost of a control should not exceed the benefits to be derived.



The Board of Retirement has established a finance committee to oversee the financial reporting process and to review the scope and results of independent audits. The independent auditors have unrestricted access to the finance committee to discuss their related findings as to the integrity of the financial reporting and adequacy of internal controls.

KCERA's external auditor, CliftonLarsonAllen, LLP, has conducted an audit of the basic financial statements in accordance with auditing standards generally accepted in the United States of America, performing such tests and other procedures as they deem necessary to express an opinion in their report to the Board of Retirement. The financial audit ensures that KCERA's financial statements are presented in conformity with accounting principles generally accepted in the United States of America and are free of material misstatements. Their opinion is that KCERA's financial statements present fairly, in all material respects, the Fiduciary Net Position of KCERA as of June 30, 2018 and 2017 and its Changes in Fiduciary Net Position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

## INVESTMENTS

The Board of Retirement has exclusive control of all investments of KCERA and is responsible for establishing investment policies, objectives and strategies. The Board is authorized to invest in any form or type of investment deemed "prudent" in the informed opinion of the Board. The members of the Board serve as fiduciaries for the members and beneficiaries of the retirement association and are held to a high standard of care in all transactions.

The Board operates under a standard of care in California commonly known as the "prudent person" rule, which allows the Board to invest or delegate the authority to invest the assets of the Plan when prudent in the informed opinion of the Board. In addition, the rule requires the Board to diversify the investments of the Plan, unless it is clearly prudent not to do so under the circumstances. The Board therefore makes basic policy decisions with respect to the Plan, including, but not limited to, the allocation of assets to various investment classes. The Board delegates much discretion to professional investment advisors to execute investment policy subject only to policy and guidelines provided by the Board.

KCERA's assets are managed exclusively by external, professional investment managers. The KCERA staff monitors the activity of these managers and assists the Board with the development and implementation of investment policies and long-term investment strategies. These policies and guidelines are outlined in KCERA's Investment Policy Statement, which states the investment philosophy, investment guidelines, performance objectives and asset allocation of the Plan. The Board employs the services of independent investment consultants Verus Investments and Albourne America to assist the Board in formulating policies, setting goals and manager guidelines, and selecting and monitoring the performance of the money managers.

For fiscal year 2018, the investments of the Plan returned 6.5%\* (net of fees). KCERA's annualized rate of return, net of fees, was 5.8% in the past three years, 6.9% in the past five years, and 5.1% in the past ten years. The investment expenses of the fund are linked to the performance of the investment portfolio and other factors and therefore vary year to year.

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\* References in this document to KCERA's investment rate of return assume a time-weighted rate of return unless otherwise specified as a money-weighted rate of return, per GASB 67 guidelines.

## PROFESSIONAL SERVICES

The Board retains professional consultants and investment managers to provide professional services essential to the effective and efficient operation of KCERA. These entities are included in the Schedule of Investment Fees on pages 76-78.

Opinions from the certified public accountant and the actuary for the Plan are included in this report. The consultants and investment managers retained by the Board are listed on page 73 of this report.

## CERTIFICATE OF ACHIEVEMENTS

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to KCERA for its Comprehensive Annual Financial Report for the fiscal year ended June 30, 2017. The Certificate of Achievement is a prestigious national award recognizing excellence in the preparation of state and local government financial reports.

In order to be awarded the Certificate of Achievement, a government unit must publish an easily readable and well-organized comprehensive annual financial report. This report must satisfy both accounting principles generally accepted in the United States of America and applicable legal requirements.

The Certificate of Achievement is valid for a period of one year only. We believe that our current Comprehensive Annual Financial Report continues to meet the Certificate of Achievement Program's requirements, and we will again submit it to the GFOA for appraisal.

## ACKNOWLEDGMENTS

The compilation of this report reflects the combined effort of the KCERA staff. This report is intended to provide complete information as a basis for management decisions, as a means for establishing compliance with legal requirements, and as a means for determining the responsible stewardship of the KCERA fund.

I wish to take this opportunity to thank the members of KCERA for their confidence in KCERA and to express my gratitude to the Board of Retirement for your support of the KCERA administration and the best interests of the beneficiaries of the Plan throughout the fiscal year. I also wish to thank the consultants and staff for their continued commitment to KCERA and their diligent work to ensure the successful administration of the Plan.

Respectfully submitted,



Dominic D. Brown  
*Executive Director*



Government Finance Officers Association

**Certificate of  
Achievement  
for Excellence  
in Financial  
Reporting**

Presented to

**Kern County  
Employees' Retirement Association  
California**

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended

**June 30, 2017**

*Christopher P. Morill*

Executive Director/CEO

Each year, a Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose Comprehensive Annual Financial Reports (CAFRs) achieve the highest standards in government accounting and reporting.

CAFRs must satisfy Generally Accepted Accounting Principles (GAAP) and applicable legal requirements.

KCERA has earned this prestigious award yet again, this time for its 2017 Comprehensive Annual Financial Report.

KCERA believes its Fiscal Year 2018 CAFR continues to meet the Certificate of Achievement Program's requirements and will submit it to the Government Finance Officers Association to determine its eligibility for another certificate.



**David Couch**  
Appointed by Board of Supervisors  
Present term expires 12/31/2018



**Dustin Dodgin**  
*Chairman of the Board*  
Appointed by Board of Supervisors  
Present term expires 12/31/2019



**Phil Franey**  
Elected by Retired Members  
Present term expires 12/31/2019



**Juan Gonzalez**  
Elected by General Members  
Present term expires 12/31/2018



**Marko Horvat**  
Appointed by Board of Supervisors  
Present term expires 12/31/2019



**Bob Jefferson**  
Elected by General Members  
Present term expires 12/31/2019



**Jordan Kaufman**  
County Treasurer-Tax Collector  
Ex-Officio Member



**Thad Kennedy, *Alternate***  
*Vice-Chairman of the Board*  
Elected by Safety Members  
Present term expires 12/31/2018



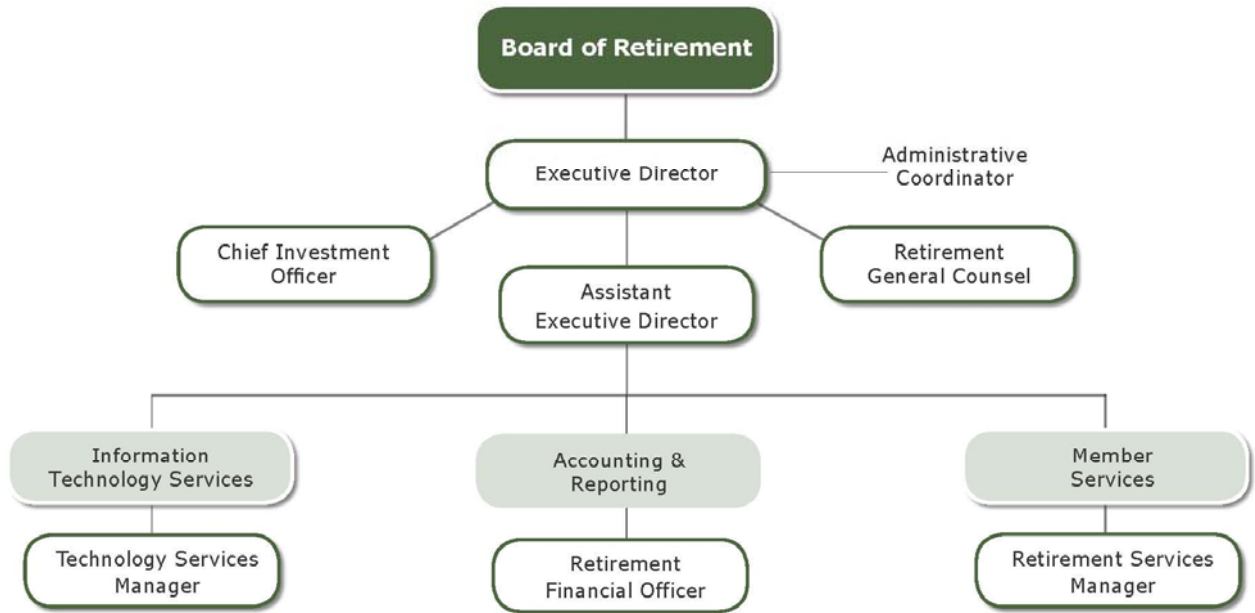
**Rick Kratt**  
Elected by Safety Members  
Present term expires 12/31/2018



**John Mattly, *Alternate***  
Elected by Retired Members  
Present term expires 12/31/2019



**Lauren Skidmore**  
Appointed by Board of Supervisors  
Present term expires 12/31/2018



**Actuary**

The Segal Company, Inc.

**Auditor**

CliftonLarsonAllen, LLP

**Custodian**

The Northern Trust Company

**Investment Consultants**

Verus Investments  
Albourne America LLC

**Legal**

Foley & Lardner, LLP  
Hanson Bridgett, LLP  
Ice Miller, LLP  
Nossaman, LLP  
Reed Smith, LLP



**Other Specialized Services**

Agility Recovery Solutions  
Cortex Applied Research, Inc.  
Glass, Lewis & Co., LLC  
Deutsche Bank

*Refer to the Investment Section for a list of Investment Managers and the Schedule of Investment Management Fees.*

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# **FINANCIAL**

## **Section**





CliftonLarsonAllen LLP  
CLAAconnect.com

## INDEPENDENT AUDITORS' REPORT

Board of Retirement and the Finance Committee  
Kern County Employees' Retirement Association  
Bakersfield, California

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the Kern County Employees' Retirement Association, which comprise the statement of fiduciary net position and statement of changes in fiduciary net position, as of and for the years ended June 30, 2018 and 2017, and the related notes to the financial statements, which collectively comprise the Kern County Employees' Retirement System's basic financial statements as listed in the table of contents.

### ***Management's Responsibility for the Financial Statements***

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

### ***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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the 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 entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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



Board of Retirement and the Finance Committee  
Kern County Employees' Retirement Association

***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Kern County Employees' Retirement Association as of June 30, 2018 and 2017, and the respective changes in financial 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 schedules of changes in the net pension liability and related ratios, employer contributions, and money-weighted rate of return, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

***Other Information***

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Kern County Employees' Retirement Association's basic financial statements. The other supplementary information listed in the table of contents is presented for purposes of additional analysis and are not a required part of the basic financial statements.

The other supplementary information, which includes the schedules of administrative expenses, investment expenses, and payments to consultants, as listed in the table of contents, is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the other supplementary information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

The introductory, investment, actuarial and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Board of Retirement and the Finance Committee  
Kern County Employees' Retirement Association

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated December 7, 2018, on our consideration of the Kern County Employees' Retirement Association's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the result of that testing, and not to provide an opinion on the effectiveness of Kern County Employees' Retirement Association's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Kern County Employees' Retirement Association's internal control over financial reporting and compliance.



**CliftonLarsonAllen LLP**

Denver, Colorado  
December 7, 2018

This section presents management's discussion and analysis of the Kern County Employees' Retirement Association's (KCERA) financial statements and the significant events and conditions that affected the operations and performance during the years ended June 30, 2018 and 2017. It is presented as a narrative overview and analysis in conjunction with the Executive Director's *Letter of Transmittal* included in the Introductory Section of the Comprehensive Annual Financial Report.

### Financial Highlights

- KCERA's net position increased by \$236.0 million during the fiscal year ended June 30, 2018, a 6.0% increase from the last fiscal year. The increase was principally due to financial markets, notably KCERA's U.S. and non-U.S. equities, and commodities allocations.
- Member contributions increased by \$1.1 million, or 2.1%, mainly as a result of scheduled member contribution rate changes and other demographic changes. Employer contributions increased by \$18.2 million, or 8.1%, the increase in 2018 employer contributions was primarily due to discontinuing the prepayment for the County of Kern, Hospital Authority, Kern County Superior Court and the San Joaquin Valley Air Pollution Control District. The average employer contribution rate decreased from 45.11% of payroll for fiscal year 2017-16 to 44.79% for fiscal year 2018-17.
- The total fund's investment performance did not meet the actuarial assumed rate of return for the fiscal year. The investment portfolio reported a total return of 6.5% (net of fees)\* versus the actuarial assumed rate of return of 7.25% for the fiscal year ended June 30, 2018. The total fund underperformed by 0.5% of the total fund's policy return of 7.0%. The underperformance was mainly driven by an overweight to fixed income in a strong equity market environment.
- Vested pension benefits increased by \$16.0 million, or 5.6%, over the prior year. The increase is attributable to a 2.5% increase in retired members and beneficiaries receiving pension benefits, and a 3.0% increase in the average monthly benefit, which rose to \$3,065 in the fiscal year. In 2017 the rate of inflation picked up and all pensioners received the maximum COLA of 2.5% in April 2018.
- As of June 30, 2017, the date of the most recent actuarial valuation, the funded ratio for KCERA was 63.2% compared to the funded ratio of 63.4% as of June 30, 2016. The decrease in the ratio is mainly due to the adoption of new actuarial assumptions, the investment loss on a valuation value of assets basis, and actual contributions less than expected, offset to some extent by the lower than expected salary increases, lower than expected COLA increases and other actuarial gains.

### Overview of Basic Financial Statements and Accompanying Information

- 1) **The Statement of Fiduciary Net Position** is the basic statement of position for a defined benefit pension plan. This statement presents asset and liability account balances at fiscal year-end. The difference between assets and liabilities represents the net position available for future payments to retirees and their beneficiaries. Assets and current liabilities of the Plan reflect full accruals. The statement reflects investments at fair value and accounting liabilities as distinct from actuarial liabilities.
- 2) **The Statement of Changes in Fiduciary Net Position** is the basic operating statement for a defined benefit pension plan. Changes in plan net position are recorded as additions or deductions from the Plan. All additions and deductions are reported on a full accrual basis.

\* References in this document to KCERA's investment rate of return assume a time-weighted rate of return unless otherwise specified as a money-weighted rate of return, per GASB 67 guidelines.

## Overview of Basic Financial Statements and Accompanying Information (*cont.*)

- 3) **Notes to the Basic Financial Statements** are an integral part of the financial statements and provide important additional information.
- 4) **Required Supplementary Information** consists of three required schedules and their related notes: Schedule of Changes in Net Pension Liability and Related Ratios, Schedule of Employer Contributions, and Schedule of Money- Weighted Rates of Return.
- 5) **Other Supplemental Information** includes schedules of administrative expenses, investment manager fees, other investment expenses, and payments to consultants.

The required financial statements and disclosures have been prepared in accordance with accounting principles generally accepted in the United States of America and are in compliance with Governmental Accounting Standards Board (GASB) Statements.

## Financial Analysis

### Fiduciary Net Position Restricted for Pension Benefits

KCERA provides pension benefits to the employees and their beneficiaries of the County of Kern and other public agencies. KCERA's benefits are funded by member and employer contributions, and by investment income. KCERA's fiduciary net position— restricted for pension benefits at June 30, 2018 was \$4.2 billion, an increase of \$236.0 million, or 6.0%, from June 30, 2017. KCERA's fiduciary net position-restricted for pension benefits at June 30, 2017 was \$4.0 billion, an increase of \$391.3 million, or 11.0%, from June 30, 2016. Key elements of the increase in net position are described below and in Tables 1 and 2 on page 20.

### Contributions and Investment Income

Additions to net position include member and employer contributions and investment income.

Member contributions were approximately \$52.5 million, \$51.4 million and \$33.3 million for the years ended June 30, 2018, 2017 and 2016, respectively. Employer contributions were \$242.5 million, \$224.4 million and \$234.7 million for the years ended June 30, 2018, 2017 and 2016, respectively.

Member contributions increased by \$1.1 million (2.1%) in 2018 and increased by \$18.1 million (54.5%) in 2017. The increase in member contributions in 2018 and 2017 was mainly the result of scheduled member contribution rate increases, other demographic changes and reclassifying employer paid member contributions.

Employer contributions increased approximately \$18.2 million (8.1%) in 2018 and decreased approximately \$10.4 million (4.4%) in 2017. The increase in 2018 employer contributions was primarily due to discontinuing the prepayment for the County of Kern, Hospital Authority, Kern County Superior Court and the San Joaquin Valley Air Pollution Control District. The decrease in 2017 was the result of reclassifying employer paid member contributions.

Net investment and securities lending income was \$267.7 million, \$426.6 million and -\$27.5 million for the years ended June 30, 2018, 2017 and 2016, respectively. The increase in 2018 can be attributed to strong corporate earnings growth with favorable returns in the equity markets, private markets and commodities.

For the fiscal years ended June 30, 2018, 2017 and 2016, the KCERA portfolio returned (net of fees) 6.5%, 11.8% and -0.5%, respectively. More information on KCERA's investment portfolio is contained in the investment section of this report.

### Benefits, Refunds and Expenses

Deductions to plan fiduciary net position include pension benefits, lump sum payments, supplemental benefits, refunds of member contributions, and administrative expenses. The pension benefits (annuity, pension and cost-of-living allowances) were \$304.8 million, \$288.8 million and \$272.3 million for the years ended June 30, 2018, 2017 and 2016, respectively. Pension benefits increased by approximately \$16.0 million (5.6%) in 2018 and \$16.5 million (6.1%) in 2017.

**Financial Analysis (cont.)**

**Benefits, Refunds and Expenses (cont.)**

These increases were mainly due to a consistently growing population of retired members and beneficiaries receiving pension benefits and an increase in the average monthly benefit, attributable to higher final average compensations and the maximum 2.5% cost-of-living adjustment. Retired members and beneficiaries increased by 2.5% in 2018 and by 3.4% in 2017. The average monthly benefit for retirees and beneficiaries increased by 3.1% in 2018 and 3.0% in 2017.

KCERA previously adopted California Government Code Section 31618, which provides for the establishment of the Supplemental Retiree Benefit Reserve (SRBR). In fiscal year 2018, SRBR provides retirees with 80% purchasing power parity and a \$5,000 death benefit. In addition to pension benefits, the supplemental retirement benefits paid were \$13.1

million, \$13.1 million and \$13.2 million for the years ended June 30, 2018, 2017 and 2016, respectively. Refunds of member contributions were \$3.7 million, \$3.9 million and \$3.3 million for the years ended June 30, 2018, 2017 and 2016, respectively.

KCERA’s administrative expenses were \$5.1 million, \$5.2 million and \$5.2 million for the years ended June 30, 2018, 2017 and 2016, respectively.

Average aggregate monthly defined benefit payments, excluding SRBR benefits, AND total number of retirees and beneficiaries:		
<u>June 2018</u>	<u>June 2017</u>	<u>June 2016</u>
\$25.4 million	\$24.1 million	\$22.7 million
8,296	8,092	7,824

**STATEMENT OF FIDUCIARY NET POSITION**

Table 1

(In thousands)

	2018	Increase (Decrease) Amount	2017	Increase (Decrease) Amount	2016
<b>Assets</b>					
Current Assets	\$ 254,252	\$ 6,451	\$ 247,801	\$ 72,899	\$ 174,902
Investments	4,237,296	236,812	4,000,484	412,622	3,587,862
Securities Lending Collateral	140,081	16,927	123,154	47,154	76,000
Capital Assets	3,180	(625)	3,805	(674)	4,479
<b>Total Assets</b>	<b>4,634,809</b>	<b>259,565</b>	<b>4,375,244</b>	<b>532,002</b>	<b>3,843,243</b>
<b>Liabilities</b>					
Current Liabilities	295,866	6,671	289,195	93,539	195,656
Liabilities for Security Lending	140,081	16,927	123,154	47,154	76,000
<b>Total Liabilities</b>	<b>435,947</b>	<b>23,598</b>	<b>412,349</b>	<b>140,694</b>	<b>271,656</b>
<b>Fiduciary Net Position – Restricted for Pension Benefits</b>	<b>\$ 4,198,862</b>	<b>\$ 235,967</b>	<b>\$ 3,962,895</b>	<b>\$ 391,308</b>	<b>\$ 3,571,587</b>

**STATEMENT OF CHANGES IN FIDUCIARY NET POSITION**

Table 2

(In thousands)

	2018	Increase (Decrease) Amount	2017	Increase (Decrease) Amount	2016
<b>Additions</b>					
Member Contributions*	\$ 52,503	\$ 1,093	\$ 51,410	\$ 18,132	\$ 33,278
Employer Contributions*	242,534	18,183	224,351	(10,363)	234,714
Net Investment Income (Loss)	267,659	(158,948)	426,607	454,142	(27,535)
<b>Total Additions</b>	<b>562,696</b>	<b>(139,672)</b>	<b>702,368</b>	<b>461,911</b>	<b>240,457</b>
<b>Deductions</b>					
Pension Benefits	304,784	16,034	288,750	16,481	272,269
Supplemental Retirement Benefits	13,139	(4)	13,143	(44)	13,187
Refunds of Member Contributions	3,690	(234)	3,924	642	3,282
Administrative Expenses	5,116	(127)	5,243	18	5,225
<b>Total Deductions</b>	<b>326,729</b>	<b>15,669</b>	<b>311,060</b>	<b>17,097</b>	<b>293,963</b>
<b>Increase (Decrease) in Net Position</b>	<b>235,967</b>	<b>(155,341)</b>	<b>391,308</b>	<b>444,814</b>	<b>(55,506)</b>
<b>Fiduciary Net Position – Restricted for Pension Benefits</b>					
<b>At Beginning of Year</b>	<b>\$ 3,962,895</b>	<b>\$ 391,308</b>	<b>\$ 3,571,587</b>	<b>\$ (53,506)</b>	<b>\$ 3,625,093</b>
<b>At End of Year</b>	<b>\$ 4,198,862</b>	<b>\$ 235,967</b>	<b>\$ 3,962,895</b>	<b>\$ 391,308</b>	<b>\$ 3,571,587</b>

\*The current fiscal year's financial statements reclassified employer paid member contributions as member contributions.

**Reserves**

KCERA’s reserves are established for the purpose of managing benefit operations in accordance with the County Employees Retirement Law of 1937 (CERL). The total amount of reserves equals KCERA’s Fiduciary Net Position – Restricted for Pension Benefits at the end of the year.

Investments are stated at fair value instead of at cost and include the recognition of unrealized gains and losses. Unrealized gains and losses effect the reserves indirectly through an actuarial asset “smoothing” process and are held in the Market Stabilization Reserve with a portion allocated to all other reserves. KCERA uses a five-year smoothing methodology to recognize unrealized gains and losses. The five-year smoothing is calculated by subtracting the expected return of the actuarial assumed interest rate of 7.25% at June 30, 2018 and 7.50% at December 31, 2017 and fiscal years ended June 30, 2017 and 2016, from the total

Fund’s actual return on net position. The Market Stabilization Reserve was (\$92.3) million, (\$74.4) million and (\$235.3) million for the years ended June 30, 2018, 2017 and 2016, respectively.

Interest at the actuarial rate of 7.25%, or at the highest rate possible if net earnings are not sufficient to credit the full actuarial rate, is credited semiannually on December 31 and June 30. Interest is credited to all reserves, except the contingency reserve. KCERA credited the reserves 6.82% in fiscal year 2018 and 6.62% in fiscal year 2017. In addition, in fiscal year 2018, no funds were credited to reduce the negative contingency reserve, in accordance with the Board of Retirement’s Interest Crediting Policy. As investment returns improve, resulting in positive changes in net position, the Contingency and Market Stabilization Reserves will turn to a positive position.

(In thousands)

<b>KCERA Reserves</b>			
	<b>2018</b>	<b>2017</b>	<b>2016</b>
Member Reserve	\$ 387,376	\$ 351,592	\$ 320,400
Employer Reserve	888,042	786,356	724,857
Cost of Living Reserve	1,278,088	1,178,952	1,085,752
Retired Member Reserve	1,576,955	1,558,678	1,512,898
Supplemental Retiree Benefit Reserve	177,089	178,079	179,365
Contingency Reserve	(16,355)	(16,355)	(16,355)
Market Stabilization Reserve	(92,333)	(74,407)	(235,330)
<b>Total</b>	<b>\$ 4,198,862</b>	<b>\$ 3,962,895</b>	<b>\$ 3,571,587</b>

**Fiduciary Responsibilities**

The Board of Retirement and management staff are fiduciaries of the pension trust fund. Under the California Pension Protection Act of 1992, the Board of Retirement has plenary authority and fiduciary responsibility for the investment of monies and for the administration of KCERA. The Board of Retirement has the sole and exclusive fiduciary responsibility over the assets of the Plan. The assets are held for the exclusive purpose of providing benefits to KCERA members and their survivors, as mandated.

**Requests for Information**

This financial report is designed to provide a general overview of KCERA’s finances and accountability for the plan sponsors and members. Questions concerning any of the information provided in this report or requests for additional information should be directed to Sheryl Lawrence, KCERA’s financial officer, at (661) 381-7700.



As of June 30, 2018 and 2017

(In thousands)

	2018	2017
<b>Assets</b>		
Cash and Cash Equivalents	\$ 103,722	\$ 84,238
Receivables:		
Investments Sold	123,709	153,925
Interest and Dividends	8,592	6,621
Contributions and Other Receivables	<u>18,204</u>	<u>2,949</u>
Total Receivables	150,505	163,495
Investments at Fair Value:		
Domestic Debt Securities and Bonds	1,270,324	1,313,639
International Bonds	266,375	257,854
Domestic Equities	909,836	788,828
International Equities	806,215	737,122
Real Estate Investments	242,065	229,250
Alternative Investments	561,410	513,713
Commodities	175,300	155,853
Swaps/Options	5,771	4,225
Collateral Held for Securities Lending	<u>140,081</u>	<u>123,154</u>
Total Investments at Fair Value	4,377,377	4,123,638
Capital Assets:		
Computer Software	6,298	6,298
Equipment/Computers	609	562
Accumulated Depreciation	<u>(3,727)</u>	<u>(3,055)</u>
Total Capital Assets	3,180	3,805
Prepaid Expenses	25	68
Total Assets	<u>4,634,809</u>	<u>4,375,244</u>
<b>Liabilities</b>		
Securities Purchased	289,417	286,618
Collateral Held for Securities Lent	140,081	123,154
Other Liabilities	<u>6,449</u>	<u>2,577</u>
Total Liabilities	435,947	412,349
<b>Fiduciary Net Position – Restricted for Pension Benefits</b>	<b>\$ 4,198,862</b>	<b>\$ 3,962,895</b>

See accompanying notes to the financial statements.

(In thousands)

	2018	2017
<b>Additions</b>		
Contributions:		
Employer	\$ 242,534	\$ 224,351
Member	<u>52,503</u>	<u>51,410</u>
Total Contributions	295,037	275,761
Investment Income:		
Net Appreciation in Fair Value of Investments	252,139	400,655
Interest	33,734	30,913
Dividends	13,681	13,106
Real Estate Investments	<u>(1,332)</u>	<u>6,042</u>
Total Investment Income	298,222	450,716
Less: Investment Expenses	<u>31,322</u>	<u>24,609</u>
Net Investment Income	266,900	426,107
Securities Lending Income:		
Earnings:	843	555
Less: Rebates & Bank Fees	<u>84</u>	<u>55</u>
Net Securities Lending Income	759	500
Total Additions	<u>562,696</u>	<u>702,368</u>
<b>Deductions</b>		
Retirement and Survivor Benefits	304,784	288,750
Supplemental Retirement Benefits	13,139	13,143
Refunds of Member Contributions	3,690	3,924
Administrative Expenses	<u>5,116</u>	<u>5,243</u>
Total Deductions	326,729	311,060
<b>Net Increase</b>	<b>235,967</b>	<b>391,308</b>
<b>Fiduciary Net Position – Restricted for Pension Benefits At Beginning of Year</b>	<b>3,962,895</b>	<b>3,571,587</b>
<b>Fiduciary Net Position – Restricted for Pension Benefits At End of Year</b>	<b>\$ 4,198,862</b>	<b>\$ 3,962,895</b>

See accompanying notes to the financial statements.

**NOTE 1 – DESCRIPTION OF PLAN**

The Kern County Employees’ Retirement Association (KCERA) was established on January 1, 1945 by the County of Kern Board of Supervisors under the provisions of the County Employees’ Retirement Law of 1937 (CERL). KCERA is a cost-sharing, multiple-employer defined benefit plan (the Plan) covering all permanent employees of the County of Kern, Berranda Mesa Water District, Button-willow Recreation and Park District, East Kern Cemetery District, Inyokern Community Services District,

Kern County Hospital Authority, Kern County Superior Court, Kern County Water Agency, Kern Mosquito and Vector Control District, North of the River Sanitation District, San Joaquin Valley Air Pollution Control District, Shafter Recreation and Park District, West Side Cemetery District, West Side Mosquito and Vector Control District, and West Side Recreation and Park District. The Plan is administered by the Kern County Board of Retirement, which consists of nine members and two alternate members.

As of June 30, 2018, employee membership data related to the pension plan was as follows:

	General	Safety	Total
Active – Vested	4,159	1,434	5,593
Active – Non-Vested	2,992	337	3,329
<b>Total Active Members</b>	<b>7,151</b>	<b>1,771</b>	<b>8,922</b>
Terminated – Deferred Vested	1,132	227	1,359
Retirees and Beneficiaries	6,349	1,947	8,296
<b>Total Members</b>	<b>14,632</b>	<b>3,945</b>	<b>18,577</b>

As of June 30, 2017, employee membership data related to the pension plan was as follows:

	General	Safety	Total
Active – Vested	4,078	1,383	5,461
Active – Non-Vested	2,893	384	3,277
<b>Total Active Members</b>	<b>6,971</b>	<b>1,767</b>	<b>8,738</b>
Terminated – Deferred Vested	806	124	930
Retirees and Beneficiaries	6,184	1,908	8,092
<b>Total Members</b>	<b>13,961</b>	<b>3,799</b>	<b>17,760</b>

**Benefit Provisions**

KCERA provides service retirement, disability, death, survivor and supplemental benefits to eligible employees. All regular full-time employees of the County of Kern or contracting districts who work 50% or more of the regular standard hours required become members of KCERA effective on the first day of the payroll period following the date of hire. Safety membership includes those in active law

enforcement, fire suppression, criminal investigation and probation officers. General members (excluding Tier III) are eligible to retire at age 70 regardless of service or at age 50 with 10 or more years of retirement service credit. A member with 30 years of service is eligible to retire regardless of age. General Tier III members are eligible to retire at age 70 regardless of service or at age 52 with 5 or more years of retirement service credit.

**NOTE 1 – DESCRIPTION OF PLAN**

**Benefit Provisions (cont.)**

Safety members are eligible to retire at age 70 regardless of service or at age 50 with 10 or more years of retirement service credit. A member with 20 years of service is eligible to retire regardless of age.

The retirement benefit the member will receive is based on age at retirement, final average compensation (FAC), years of retirement service credit and retirement benefit tier.

General member benefits for Tier I and Tier II are calculated pursuant to California Gov. Code Sections 31676.17 and 31676.01, respectively. The monthly allowance is equal to 1/50<sup>th</sup> of FAC times years of accrued retirement service credit times age factor from Section 31676.17 (Tier I) or 1/90<sup>th</sup> of FAC times years of accrued retirement service credit times age factor from Section 31676.01 (Tier II). General Tier III member benefits are calculated pursuant to the provisions found in California Government Code Section 7522.20(a).

The monthly allowance is equal to the FAC multiplied by years of accrued retirement credit multiplied by the age factor from Section 7522.20(a).

Safety member benefits for Tier I and Tier II are calculated pursuant to California Gov. Code Sections 31664.1 and 31664, respectively. The monthly allowance is equal to 3% of FAC times years of accrued retirement service credit times age factor from Section 31664.1 (Tier I) or 1/50<sup>th</sup> (2%) of FAC times years of accrued retirement service credit times age factor from Section 31664 (Tier II).

For members in Tier I or Tier II, the maximum monthly retirement allowance is 100% of FAC. There is no FAC limit on the maximum retirement benefit for General Tier III members.

The maximum amount of compensation earnable that can be taken into account for 2018 for members with membership dates on or after July 1, 1996 but before January 1, 2013 is \$275,000. The maximum amount of compensation earnable that was taken into account for 2017 was \$270,000. For General Tier III members enrolled in Social Security who joined on or after January 1, 2013, the maximum pensionable compensation for 2018 is \$121,388. The maximum pensionable compensation for 2017 was \$118,775. These limits are adjusted on an annual basis. Members are exempt from paying member contributions and employers are exempt from paying employer contributions on compensation in excess of the annual cap.

FAC consists of the highest 12 consecutive months of pay for a General Tier I or Tier IIA member or a Safety Tier I or Tier IIA member, and the highest 36 consecutive months of pay for a General Tier IIB or Tier III member or a Safety Tier IIB member.

The member may elect an unmodified retirement allowance or an optional retirement allowance. The unmodified option provides the highest monthly benefit and a 60% continuance to an eligible surviving spouse or domestic partner. An eligible spouse or partner is one married to or registered with the member for at least one year prior to the effective retirement date. Certain surviving spouses or partners may also be eligible if marriage or partnership occurred at least two years prior to the date of death and the surviving spouse or partner is age 55 as of the date of death. There are also four optional retirement allowances the member may choose. Each option requires a reduction in the unmodified allowance to grant the member the ability to provide certain benefits to a surviving spouse, domestic partner or named beneficiary having an insurable interest in the life of the member.

**NOTE 1 – DESCRIPTION OF PLAN**

***Death Benefits:***

Death Before Retirement

An active member’s beneficiary is entitled to receive death benefits, which consist of accumulated contributions and interest and one month of salary for each full year of service, up to a maximum of six months’ salary.

If a member is vested and his/her death is not the result of job-caused injury or disease, the spouse or registered domestic partner will be entitled to receive, for life, a monthly allowance equal to 60% of the retirement allowance they would have been entitled to receive if they had retired for a non-service-connected disability on the date of their death. This same choice is given to their minor children under the age of 18 (continuing to age 22 if enrolled full time in an accredited school).

If a member dies in the performance of duty, his/her spouse or registered domestic partner receives, for life, a monthly allowance equal to at least 50% of the member’s final average salary. This can also apply to minor children under age 18 (continuing to age 22 if enrolled full time in an accredited school).

Death After Retirement

If a member dies after retirement, a death benefit of \$5,000 is payable to his/her designated beneficiary or estate. If the retirement was for a nonservice-connected disability and the member chose the unmodified allowance option, the surviving spouse, registered domestic partner or minor children will receive a monthly continuance equal to 60% of the benefit. If the retirement was for a service-connected disability, the spouse, registered domestic partner or minor children will receive a 100% continuance of the member’s benefit.

***Disability Benefit:***

A member with five years of service, regardless of age, who becomes permanently incapacitated for the performance of duty will be eligible for a nonservice-connected disability retirement. Any member who becomes permanently incapacitated for the performance of duty as a result of injury or disease arising out of and in the course of employment, is eligible for a service-connected disability, regardless of service length or age.

***Cost-of-Living Adjustment:***

An annual cost-of-living adjustment (COLA) of up to 2.0% was adopted for all retirees and continuance beneficiaries as of April 1, 1973. An additional 0.5% COLA was granted by the Ventura Settlement as of April 1, 2002, resulting in a maximum COLA of 2.5%, depending on the rate of inflation.

***Supplemental Benefits:***

The Board of Retirement and the Board of Supervisors adopted Government Code Section 31618 on April 23, 1984, which provides for the establishment of the Supplemental Retiree Benefit Reserve (SRBR). The SRBR is used only for the benefit of future and current retired members and their beneficiaries. The supplemental benefit is not a guaranteed benefit. The distribution of the SRBR is determined by the Board of Retirement. In fiscal year 2018, SRBR provided for 80% purchasing power protection and a \$5,000 death benefit.

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Reporting Entity**

KCERA, with its own governing board, is an independent governmental entity separate and distinct from the County of Kern.

**Basis of Accounting**

KCERA follows Governmental Accounting Standards Board (GASB) accounting principles and reporting guidelines. The financial statements are prepared using the accrual basis of accounting and reflect the overall operations of KCERA. Employer and member contributions are recognized in the period in which the contributions are due, and benefits and refunds of prior contributions are recognized when due and payable in accordance with the terms of the Plan. Investment income is recognized as revenue when earned. The net appreciation (depreciation) in the fair value of investments is recorded as an increase (decrease) to investment income based on investment valuations, which includes both realized and unrealized gains and losses on investments.

**Administrative Expenses**

KCERA's board annually adopts the operating budget for the administration of KCERA. Costs of administering the Plan are charged against the Plan's earnings. KCERA's administrative budget is calculated pursuant to Government Code Section

31580.2(a), which provides that the administrative expenses incurred in any year may not exceed the greater of either twenty-one-hundredths of 1 percent (0.21%) of the actuarial accrued liability of the system or \$2,000,000, as adjusted annually by the amount of the annual cost-of-living adjustment computed in accordance with Article 16.5. Government Code Section 31580.2(b) provides that expenditures for computer software, hardware and computer technology consulting services in support of the computer products shall not be considered a cost of administrative expenses in the calculation.

**Cash Equivalents**

Cash equivalents are assets that are readily convertible into cash, such as short-term government bonds or Treasury bills and commercial paper. Cash equivalents are distinguished from other investments through their short-term existence; they mature within 3 months. A cash equivalent must also be an investment with an insignificant risk of change in value. Although cash equivalents are not cash, they are presented on the Statement of Fiduciary Net Position together with cash using the title "Cash and Cash Equivalents."

**Valuation of Investments**

Fair value for investments are derived by various methods as indicated in the following table:

<b>Publicly traded stocks</b>	Most recent exchange closing price. International securities reflect currency exchange rates in effect at June 30, 2018 and 2017.
<b>Short-term investments and bonds</b>	Institutional evaluations or priced at par.
<b>OTC securities</b>	Evaluations based on good faith opinion as to what a buyer in the marketplace would pay for a security.
<b>Commingled funds</b>	Net asset value provided by the investment manager.
<b>Alternative investments</b>	Net asset value provided by the Fund manager based on the underlying financial statements and fair value of the Fund.
<b>Real estate investments</b>	Estimated based on price that would be received to sell an asset in an orderly transaction between marketplace participants at the measurement date. Investments without a public market are valued based on assumptions made and multiple valuation techniques or appraisals used by the investment manager. The KCERA property is valued based on an annual appraisal.

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Risks and Uncertainties**

KCERA invests in various investment securities, which are exposed to various risks, including interest rate, market 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 that such changes could materially affect the amounts reported in the Statement of Fiduciary Net Position.

**Capital Assets**

Assets shall be recorded at historical cost or, if that amount is not practicably determined, at estimated historical cost. Accumulated depreciation shall be summarized and reflected on KCERA's annual financial statements. Capital assets shall be depreciated over their estimated useful lives using the straight-line depreciation method. Intangible assets with limited useful lives (e.g., by legal or contractual provisions) should be amortized over their estimated useful lives. Amortization of computer software should begin when the program is placed into service.

**Capitalization Thresholds and Useful Life**

Capital Asset	Thresholds	Useful Life
Furniture	\$2,500	5-15 years
Equipment/Computers	\$5,000	3-10 years
Internally generated computer software	\$1,000,000	5-12 years
Computer software	\$100,000	3-10 years

**Income Taxes**

The Plan qualifies under Section 401(a) of the Internal Revenue Code and is therefore not subject to tax under present income tax laws. No provision for income taxes has been made in the accompanying financial statements, as the Plan is exempt from federal and state income taxes under the provisions of Internal Revenue Code, Section 501 and California Revenue and Taxation Code, Section 23701, respectively.

**Management's 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. These affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

**Reclassification**

Reclassifications of certain prior year balances have been made to conform to the current year's financial statement presentation. The employer paid member contributions are excluded from employer contributions in the determination of Actuarially Determined Contributions. The estimated amount of employer paid member contributions are reclassified as member contributions. Such reclassification had no material effect on fiduciary net position as reported.

**NOTE 3 – DEPOSITS AND INVESTMENTS**

The Board of Retirement (the Board) has the fiduciary responsibility and authority to oversee the investment portfolio. The Board is governed by the County Employees’ Retirement Law of 1937. It is also governed by California Government Code Sections 31594 and 31595, which provide for prudent person governance of the Plan. Under this law, the type and amount of plan investments as well as the quality of securities are not specifically delineated; rather, the investments made are assumed to be in the best interest of the Plan such that others with similar information would acquire similar investments. The Board is required to diversify the investments of the Plan so as to minimize the risk of loss and to maximize the rate of return, unless it is clearly prudent not to do so. The investments shall be made for the exclusive purpose of providing benefits to the participants and their beneficiaries and defraying reasonable expenses to the Plan.

The Board maintains a formal Investment Policy Statement, which addresses guidelines for the investment process. The primary investment objectives for KCERA’s assets shall be:

1. Funding benefits
2. Long-term growth of capital
3. Preservation of purchasing power

A specific investment objective for KCERA’s assets is for the asset value, exclusive of contributions or withdrawals, to grow over the long run. Another objective is for the assets to earn, through a combination of investment income and capital appreciation, a rate of return (net of fees) in excess of the established benchmarks over a full market cycle (typically 3-5 years).

The Board retains a number of professional investment managers. Investment manager selection is an important decision involving complex due diligence. The Board’s investment policy requires independent performance measurement of investment managers and establishes total return objectives for the total portfolio and major categories of investments.

The Board adopts investment guidelines for KCERA’s investment managers which are included within their respective investment management agreements.

KCERA’s policy regarding the allocation of invested assets is established and may be amended by the Board. It is the policy of the Board to pursue an investment strategy that reduces risk through the prudent diversification of the portfolio across a broad selection of distinct asset classes. The following was the Board’s adopted asset allocation as of June 30, 2018:

<u>Asset Class</u>	<u>Target</u>
Domestic Equity	19%
International Equity	18%
Fixed Income	29%
Real Estate	10%
Hedge Funds	10%
Private Equity	5%
Private Credit	5%
Commodities	4%

For the year ended June 30, 2018, the annual money-weighted rate of return on pension plan investments, net of pension investment expenses, was 6.8%. For the year ended June 30, 2017, it was 12.0%. The money-weighted rate of return expresses investment performance, net of investment expense, adjusted for the changing amounts actually invested.

**Deposits**

Cash and cash equivalents are carried at cost plus accrued interest, which approximates fair value. All cash and cash equivalents are held as follows: by the County of Kern as part of Kern County’s treasury pool; by Wells Fargo Bank as cash for benefit payments and KCERA Property, Inc.; and by KCERA’s master global custodian, The Northern Trust Company. The County Treasury Oversight Committee is responsible for regulatory oversight of the Kern County Treasury Pool. Substantially all of the cash held at The Northern Trust Company is swept daily into collective, short-term investment funds.



**NOTE 3 – DEPOSITS AND INVESTMENTS**

**Deposits (cont.)**

Below is a summary of cash, deposits and short-term investments as of June 30, 2018 and 2017:

(In thousands)

Held by	2018	2017
County of Kern	\$ 12,313	\$ 10,186
Wells Fargo	4,279	1,288
Northern Trust	85,778	72,688
Disbursements in excess of cash balances	1,352	76
<b>Total</b>	<b>\$ 103,722</b>	<b>\$ 84,238</b>

*Custodial Credit Risk - Deposits*

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the Plan will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. KCERA does not have a formal policy for custodial credit risk but limits custodial credit risk for deposits by maintaining cash in an external investment pool managed by the County of Kern and cash and short-term investments managed by The Northern Trust Company. Deposits held at The Northern Trust Company that were uninsured and uncollateralized were \$1.8 million and \$2.4 million for the years ended June 30, 2018 and 2017, respectively.

**Investments**

Investments of the Plan are reported at fair value. In fulfilling its responsibilities, the Board of Retirement has contracted with investment managers and a master global custodian. For the year ended June 30, 2018, The Northern Trust Company is the global custodian for the majority of the investments of the Plan.

*Credit Risk*

Credit risk is the risk that an issuer or other counterparty to a debt investment will not fulfill its obligations. The KCERA investment policy's minimum average credit quality rating for fixed income, with the exception of high yield, shall be at least A- and the minimum issue quality shall be B-rated. The minimum overall average credit quality for high yield shall be at least B.

At June 30, 2018 and 2017, KCERA's assets consisted of securities with credit quality ratings issued by nationally recognized statistical rating organizations, as shown on the next page.

**NOTE 3 – DEPOSITS AND INVESTMENTS**
**Standard & Poor's (S&P) Credit Quality by Investment Type**

As of June 30, 2018

(In thousands)

Type of Investment	S&P Credit Quality							Total
	AAA	AA	A	BBB-B	CCC-C	D-NR	Agency*	
Asset-Backed Securities	\$ 4,629	\$ 4,726	\$ 2,116	\$ 1,619	\$ 3,752	\$ 4,813	\$ -	\$ 21,655
Bank Loans	-	-	-	12,919	1,401	1,519	-	15,839
Commercial Mortgage-Backed Securities	1,407	1,045	-	396	-	10,128	-	12,976
Corporate Bonds	9,186	3,932	32,011	266,432	13,106	24,155	-	348,822
Corporate Convertible Bonds	-	-	-	1,732	599	2,357	-	4,688
Government Agencies	-	3,497	-	514	-	-	101	4,112
Government Bonds	-	2,329	8,747	28,956	652	10,640	-	51,324
Government Mortgage-Backed Securities	-	-	-	-	-	2,666	182,476	185,142
Government-Issued Commercial Mortgage-Backed Securities	-	-	-	-	-	-	321	321
Municipal / Provincial Bonds	-	1,130	1,842	1,178	-	325	-	4,475
Non-Government-Backed C.M.O.s	521	12	-	2,774	94	4,188	-	7,589
Collective / Commingled Funds	-	504,572	139,827	6,733	-	-	73,283	724,415
<b>Total</b>	<b>\$ 15,743</b>	<b>\$ 521,243</b>	<b>\$ 184,543</b>	<b>\$ 323,253</b>	<b>\$ 19,604</b>	<b>\$ 60,791</b>	<b>\$ 256,181</b>	<b>\$ 1,381,358</b>
U.S. Treasuries & Notes								155,341
<b>Total Fixed Income</b>								<b>\$1,536,699</b>

\* "Agency" refers to a position for which an issue is implicitly guaranteed by the U.S. Government.

**NOTE 3 – DEPOSITS AND INVESTMENTS**
**Standard & Poor's (S&P) Credit Quality by Investment Type**

As of June 30, 2017

(In thousands)

Type of Investment	S&P Credit Quality							Total
	AAA	AA	A	BBB-B	CCC-C	D-NR	Agency*	
Asset-Backed Securities	\$ 6,258	\$ 2,267	\$ 1,311	\$ 1,894	\$ 3,029	\$ 2,766	\$ -	\$ 17,525
Bank Loans	-	-	-	9,426	107	3,437	-	12,970
Collateralized Bonds	-	-	-	-	-	800	-	800
Commercial Mortgage-Backed Securities	1,336	638	-	976	-	10,513	-	13,463
Corporate Bonds	9,575	5,061	28,867	252,384	17,469	28,452	-	341,808
Corporate Convertible Bonds	-	-	-	2,605	187	518	-	3,310
Government Agencies	-	3,421	-	3,741	-	-	115	7,277
Government Bonds	-	1,066	6,817	32,563	634	3,083	-	44,163
Government Mortgage-Backed Securities	-	-	-	-	-	878	136,515	137,393
Government-Issued Commercial Mortgage-Backed Securities	-	-	-	-	-	-	564	564
Municipal / Provincial Bonds	-	940	2,040	546	-	1,321	-	4,847
Non-Government-Backed C.M.O.s	169	1,523	335	1,073	501	7,239	-	10,840
Collective / Commingled Funds	97,957	649,054	-	8,454	-	75,649	-	831,114
<b>Total</b>	<b>115,295</b>	<b>663,970</b>	<b>39,370</b>	<b>313,662</b>	<b>21,927</b>	<b>134,656</b>	<b>137,194</b>	<b>1,426,074</b>
U.S. Treasuries & Notes								145,419
<b>Total Fixed Income</b>								<b>\$1,571,493</b>

\* "Agency" refers to a position for which an issue is implicitly guaranteed by the U.S. Government.

**NOTE 3 – DEPOSITS AND INVESTMENTS**
**Investments (cont.)**
*Custodial Credit Risk – Investments*

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the Plan will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. KCERA does not have a formal policy for limiting custodial credit risk. As of June 30, 2018 and 2017, there were no investment securities exposed to custodial credit risk.

*Concentration of Credit Risk*

The KCERA investment policy limits exposure to any single investment manager or product. The maximum allocation to a single active manager is up to 12% of the aggregate fair value of the Fund. The maximum allocation to a single active management product is 8%. This limitation applies to any non-index investment vehicle. With the exception of any sovereign entity (both U.S.

and non-U.S.) U.S. agency-backed and U.S. agency issued mortgages, portfolios may not invest more than 5% per investment-grade issuer. Securities of a single noninvestment-grade issuer should not represent more than 2% of the fair value of the portfolio. KCERA's investment portfolio contained no investments in any one single investment-grade issuer greater than 5% of plan net position as of June 30, 2018 and 2017 (other than the exceptions listed above).

*Interest Rate Risk*

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. KCERA's investment policy requires active managers to be within 20% of their benchmark. The overall Fund duration is expected to be within 20% of the Fund's benchmark duration. At June 30, 2018 and 2017, the segmented time distribution of the fixed income portfolio, by investment type, was as follows:

(In thousands)

Investment Type	Fair Value	Investment Maturities (in years) as of June 30, 2018					Maturity Not Determined
		Less Than 1	1-5	6-10	More Than 10		
Asset-Backed Securities	\$ 21,655	\$ -	\$ 1,990	\$ 5,935	\$ 13,730	\$ -	
Bank Loans	15,839	-	11,247	4,592	-	-	
Commercial Mortgage-Backed	12,976	-	-	-	12,976	-	
Corporate Bonds	348,822	14,283	134,549	147,148	49,986	2,856	
Corporate Convertible Bonds	4,688	-	1,171	982	2,535	-	
Government Agencies	4,112	-	2,452	800	860	-	
Government Bonds	199,500	700	61,477	69,802	67,521	-	
Government Mortgage-Backed	185,142	89	603	1,651	56,017	126,782	
Government-Issued Commercial Mortgage-Backed	321	-	131	-	190	-	
Index-Linked Government Bonds	7,165	-	1,609	4,302	1,254	-	
Municipal / Provincial Bonds	4,475	-	1,205	1,178	2,092	-	
Non-Government-Backed C.M.O.s	7,589	-	-	827	6,762	-	
Collective / Commingled Funds	724,415	-	-	-	-	724,415	
<b>Total</b>	<b>\$1,536,699</b>	<b>\$ 15,072</b>	<b>\$ 216,434</b>	<b>\$ 237,217</b>	<b>\$ 213,923</b>	<b>\$ 854,053</b>	

**NOTE 3 – DEPOSITS AND INVESTMENTS**
**Investments (cont.)**

Investment Type	Fair Value	Investment Maturities (in years) as of June 30, 2017				Maturity Not Determined
		Less Than 1	1-5	6-10	More Than 10	
Asset-Backed Securities	\$ 17,525	\$ -	\$ 537	\$ 7,201	\$ 9,787	\$ -
Bank Loans	12,970	1,484	6,629	4,857	-	-
Collateralized Bonds	800	-	-	800	-	-
Commercial Mortgage-Backed	13,463	-	244	-	13,219	-
Corporate Bonds	341,808	15,042	142,140	132,805	49,886	1,935
Corporate Convertible Bonds	3,310	-	736	831	1,743	-
Government Agencies	7,277	-	2,322	3,731	1,224	-
Government Bonds	165,404	1,630	50,489	43,404	69,881	-
Government Mortgage-Backed	137,393	-	621	1,041	51,348	84,383
Government-Issued Commercial Mortgage-Backed	564	-	191	342	31	-
Index-Linked Government Bonds	24,178	-	5,472	16,751	1,955	-
Municipal / Provincial Bonds	4,847	-	178	1,303	3,366	-
Non-Government-Backed C.M.O.s	10,840	818	499	885	8,638	-
Collective / Commingled Funds	831,114	-	-	-	-	831,114
<b>Total</b>	<b>\$ 1,571,493</b>	<b>\$ 18,974</b>	<b>\$ 210,058</b>	<b>\$ 213,951</b>	<b>\$ 211,078</b>	<b>\$ 917,432</b>

(In thousands)

**Foreign Currency Risk**

Foreign currency risk is the risk that changes in exchange rates will adversely affect the value of an investment.

The Board of Retirement considers the currency risk exposure when setting the asset allocation targets of the Plan. KCERA's investment policy permits an 18% allocation to non-U.S. equities

and a 4% allocation to emerging market debt. In addition, the core fixed income and high yield managers invest in a diversified portfolio, which can include up to 10% in foreign currency exposure and 30% in non-dollar securities.

The direct holdings shown on the following page represent KCERA's foreign currency risk exposure as of June 30, 2018 and 2017.

**NOTE 3 – DEPOSITS AND INVESTMENTS**

As of June 30, 2018

(In thousands, USD)

	Foreign Currency	Fair Value	
<b>Cash</b>	Argentine Peso	\$ 100	
	Brazilian Real	31	
	Canadian Dollar	8,620	
	Swiss Franc	5	
	Chinese Yuan Renminbi	152	
	Euro	149	
	British Pound Sterling	354	
	Hungarian Forint	115	
	Japanese Yen	125	
	Mexican Peso	360	
	New Zealand Dollar	49	
	Russian Ruble	45	
	Singapore Dollar	6	
	Turkish Lira	81	
	<b>Cash Collateral / Variation Margin</b>	Canadian Dollar	15
		Euro	619
British Pound Sterling		80	
Japanese Yen		94	
Mexican Peso		295	
<b>Equities</b>	Australian Dollar	10,591	
	Canadian Dollar	12,409	
	Swiss Franc	11,574	
	Danish Krone	4,642	
	Euro	46,014	
	British Pound Sterling	24,310	
	Hong Kong Dollar	13,252	
	New Israeli Shekel	2,095	
	Japanese Yen	43,633	
	South Korean Won	8,940	
	Norwegian Krone	664	
	Swedish Krona	2,892	
	Singapore Dollar	2,355	
	South African Rand	4,597	
	<b>Fixed Income</b>	Argentine Peso	1,462
Brazilian Real		5,510	
Chilean Peso		319	
Chinese Yuan Renminbi		72	
Colombian Peso		963	
Danish Krone		7,109	
Dominican Peso		918	
Euro		1,413	
British Pound Sterling		1,396	
Mexican Peso		7,023	
Malaysian Ringgit		1,378	
Polish Zloty		2,606	
Russian Ruble		7,213	
South African Rant		1,668	
<b>Swaps / Options</b>	Canadian Dollar	29	
	Euro	9	
	British Pound Sterling	(50)	
	Japanese Yen	(98)	
	Mexican Peso	(288)	
<b>Total Foreign Cash &amp; Investments</b>		<b>\$ 237,915</b>	

As of June 30, 2017

(In thousands, USD)

	Foreign Currency	Value
<b>Cash</b>	Argentine Peso	\$ 39
	Australian Dollar	41
	Brazilian Real	301
	Canadian Dollar	6,473
	Swiss Franc	179
	Chinese Yuan Renminbi	146
	Euro	464
	British Pound Sterling	320
	Hong Kong Dollar	102
	Hungarian Forint	81
	Japanese Yen	137
	Mexican Peso	219
	New Zealand Dollar	1
	Russian Ruble	216
	Swedish Krona	7
	Turkish Lira	30
<b>Cash Collateral / Variation Margin</b>	Canadian Dollar	(184)
	Euro	942
	British Pound Sterling	140
	Japanese Yen	78
<b>Equities</b>	Australian Dollar	10,115
	Canadian Dollar	11,770
	Swiss Franc	9,891
	Danish Krone	4,286
	Euro	44,486
	British Pound Sterling	22,232
	Hong Kong Dollar	14,388
	New Israeli Shekel	1,744
	Japanese Yen	36,302
	South Korean Won	4,998
	Norwegian Krone	471
	Swedish Krona	3,011
	Singapore Dollar	1,491
	South African Rand	4,099
	<b>Fixed Income</b>	Argentine Peso
Brazilian Real		4,389
Canadian Dollar		545
Chilean Peso		320
Chinese Yuan Renminbi		69
Colombian Peso		469
Danish Krone		7,869
Euro		757
British Pound Sterling		1,125
Hungarian Forint		1,520
Mexican Peso		5,187
Malaysian Ringgit		405
Polish Zloty		1,630
Russian Ruble		3,777
Turkish Lira	1,527	
<b>Swaps / Options</b>	Canadian Dollar	217
	Euro	159
	British Pound Sterling	(84)
<b>Total Foreign Cash &amp; Investments</b>		<b>\$ 210,167</b>

**NOTE 3 – DEPOSITS AND INVESTMENTS**

**Highly Sensitive Investments**

KCERA utilizes investments that are highly sensitive to interest rate changes in its fixed income, separately managed investment accounts. Highly sensitive investments include mortgage-backed securities, asset-backed securities, collateralized mortgage obligations, and collateralized bond obligations (CBO). Mortgage-backed securities, collateralized mortgage obligations and asset-backed securities are created from pools of mortgages

or other assets (receivables). A CBO is an investment-grade, asset-based security comprised of low-rated bonds that are transferred to a special purpose vehicle that manages the issue.

Such securities are subject to credit and interest rate risks, including uncollectible mortgages or receivables backing a security, home mortgages that are prepaid at the option of the homeowner, and the duration and maturity of the issues.

**Fair Value**

(In thousands)

	June 30, 2018	June 30, 2017
Mortgage-Backed Securities	\$ 198,439	\$ 151,420
Asset-Backed Securities	21,655	17,525
Collateralized Mortgage Obligation Securities	7,589	10,840
Collateralized Bond Obligations	-	800
<b>Total</b>	<b>\$ 227,683</b>	<b>\$ 180,585</b>

**NOTE 4 – FAIR VALUE MEASUREMENT**

KCERA’s investments are measured and reported within the fair value hierarchy established by generally accepted accounting principles. The fair value hierarchy, which has three levels, is based on the valuation inputs used to measure an asset’s fair value:

- Level 1 – Investments reflect prices quoted in active markets.
- Level 2 – Investments reflect prices that are based on a similar observable asset, either directly or indirectly, which may include inputs in markets that are not considered to be active.
- Level 3 – Investments reflect prices based on unobservable sources.

The categorization of investments within the hierarchy is based upon the pricing transparency of the instrument and should not be perceived as the particular investment’s risk.

Debt, equities and investment derivatives classified in Level 1 of the fair value hierarchy are valued directly from a predetermined primary external pricing vendor. Assets classified in Level 2 are subject to pricing by an alternative pricing source due to lack of information available by the primary vendor. Assets classified in Level 3, due to lack of an independent pricing source, are valued using an internal fair value as provided by the investment manager.

**NOTE 4 – FAIR VALUE MEASUREMENT**
**Investments Measured at Fair Value**

(In thousands)

	6/30/2018	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observ- able Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Investments by Fair Value</b>				
<i>Debt Securities:</i>	<b>\$ 930,763</b>	<b>\$ 155,341</b>	<b>\$ 761,316</b>	<b>\$ 14,106</b>
Asset-Backed Securities	226,530	-	222,304	4,226
Bank Loans	15,839	-	15,839	-
Bond Funds	118,479	-	118,479	-
Collateralized Debt Obligations	4,650	-	-	4,650
Corporate Debt Securities	353,507	-	349,236	4,271
Government Debt Securities	202,499	148,176	54,323	-
State & Local Government Debt Secur.	2,092	-	1,135	957
Structured Debt	7,165	7,165	-	-
Escrow	2	-	-	2
<i>Equity Investments:</i>	<b>653,675</b>	<b>651,408</b>	<b>1,552</b>	<b>715</b>
Common Stock	472,088	471,373	-	715
Convertible Equity	1,552	-	1,552	-
Equity Funds	173,473	173,473	-	-
Preferred Stock	5,500	5,500	-	-
Stapled Securities	1,062	1,062	-	-
<i>Real Assets:</i>	<b>4,275</b>	<b>-</b>	<b>-</b>	<b>4,275</b>
Real Estate	4,275	-	-	4,275
<b>Investments Measured at the Net Asset Value (NAV)</b>	<b>2,642,812</b>	<b>-</b>	<b>-</b>	<b>-</b>
Real Estate Funds	237,790	-	-	-
Hedge Funds	387,203	-	-	-
Private Asset Funds	174,207	-	-	-
Commingled Commodity Fund	175,300	-	-	-
Commingled Equity Fund	1,062,376	-	-	-
Commingled Bond Fund	605,936	-	-	-
<b>Derivatives</b>	<b>5,771</b>	<b>2,884</b>	<b>2,887</b>	<b>-</b>
Credit Contracts	(222)	-	(222)	-
Interest Rate Contracts	3,519	(32)	3,551	-
Other	2,474	2,916	(442)	-
<b>Invested Securities Lending Collateral</b>	<b>140,081</b>	<b>-</b>	<b>140,081</b>	<b>-</b>
Indemnified Repurchase Agreements	140,081	-	140,081	-
<b>Total</b>	<b>\$ 4,377,377</b>	<b>\$ 809,633</b>	<b>\$ 905,836</b>	<b>\$ 19,096</b>



**NOTE 4 – FAIR VALUE MEASUREMENT**
**Investments Measured at Fair Value**

(In thousands)

	6/30/2017	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observ- able Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Investments by Fair Value</b>				
<i>Debt Securities:</i>	<b>\$ 823,242</b>	<b>\$ 145,419</b>	<b>\$ 656,748</b>	<b>\$ 21,075</b>
Asset-Backed Securities	177,266	-	165,066	12,200
Bank Loans	12,971	-	12,971	-
Bond Funds	82,862	-	82,862	-
Collateralized Debt Obligations	6,740	-	-	6,740
Corporate Debt Securities	344,264	-	342,984	1,280
Government Debt Securities	172,061	121,241	50,820	-
State & Local Government Debt Secur.	2,045	-	2,045	-
Structured Debt	24,178	24,178	-	-
Escrow	855	-	-	855
<i>Equity Investments:</i>	<b>576,843</b>	<b>574,546</b>	<b>2,236</b>	<b>61</b>
Common Stock	404,199	403,304	834	61
Convertible Equity	1,834	432	1,402	-
Equity Funds	163,960	163,960	-	-
Preferred Stock	5,214	5,214	-	-
Stapled Securities	1,636	1,636	-	-
<i>Real Assets:</i>	<b>4,317</b>	<b>-</b>	<b>-</b>	<b>4,317</b>
Real Estate	4,317	-	-	4,317
<b>Investments Measured at the Net Asset Value (NAV)</b>	<b>2,591,857</b>	<b>-</b>	<b>-</b>	<b>-</b>
Real Estate Funds	224,933	-	-	-
Hedge Funds	348,133	-	-	-
Private Equity	165,580	-	-	-
Commingled Commodity Fund	155,853	-	-	-
Commingled Equity Fund	949,107	-	-	-
Commingled Bond Funds	748,251	-	-	-
<b>Derivatives</b>	<b>4,225</b>	<b>2,364</b>	<b>1,861</b>	<b>-</b>
Credit Contracts	115	-	115	-
Interest Rate Contracts	1,879	82	1,797	-
Other	2,230	2,282	(51)	-
<b>Invested Securities Lending Collateral</b>	<b>123,154</b>	<b>-</b>	<b>123,154</b>	<b>-</b>
Indemnified Repurchase Agreements	123,154	-	123,154	-
<b>Total</b>	<b>\$ 4,123,638</b>	<b>\$ 722,329</b>	<b>\$ 783,999</b>	<b>\$ 25,453</b>

**NOTE 4 – FAIR VALUE MEASUREMENT**

The valuation method for investments measured at the net asset value (NAV) per share, or equivalent, is presented in the table below.

(In thousands)

Investments Measured at Net Asset Value (NAV)	6/30/2018	Redemption Frequency	Redemption Notice Period	Unfunded Commitments
Commingled Bond Funds <sup>(1)</sup>	\$ 605,936	Daily, Quarterly, None,	2-30 Days	\$ -
Commingled Commodity Funds <sup>(1)</sup>	175,300	Daily, Monthly	1-30 Days	-
Commingled Equity Fund Domestic <sup>(1)</sup>	646,767	Daily, Quarterly	1-60 Days	-
Commingled Equity Fund Non-US <sup>(1)</sup>	415,609	Daily, Monthly	1-15 Days	-
Hedge Funds:				
CTA <sup>(2)</sup>	21,366	Monthly	30 Days	-
Directional <sup>(3)</sup>	44,923	Monthly	30-60 Days	-
Equity Long/Short <sup>(4)</sup>	26,583	Quarterly	45 Days	-
Event-Driven <sup>(5)</sup>	81,367	Quarterly, Annually, 36 Months	45-90 Days	-
Multi-Strategy <sup>(6)</sup>	99,975	Quarterly, Annually	60-90 Days	-
Relative Value <sup>(7)</sup>	112,989	Monthly, Quarterly, Semi-annually	45-120 Days	-
Real Estate Funds <sup>(8)</sup>	237,790	Quarterly, None	30-45 Days	71,504
Private Asset Funds <sup>(8)</sup>	174,207	N/A	N/A	112,794
<b>Total</b>	<b>\$ 2,642,812</b>			<b>\$ 184,298</b>

<sup>(1)</sup> *Commingled Bond Funds, Commodity Funds and Equity Funds*: Four bond funds, three commodity funds and five equity funds are considered to be commingled in nature. Each is valued at the net asset value (NAV) of units held at the end of the period based upon the fair value of the underlying investments.

<sup>(2)</sup> *CTA*: The objective of this fund is to provide consistent long-term appreciation of assets through implementation of a systematic trading model or portfolio of systematic trading models that trade in a number of debt, equity, foreign exchange and commodity instruments and derivative contracts. The fund is valued at NAV.

<sup>(3)</sup> *Directional*: The three global macro funds utilizing this strategy seek to generate consistent long-term appreciation through active, direct and indirect, leveraged trading and investment on a global basis in multiple investment strategies. All three funds are valued at NAV.

<sup>(4)</sup> *Equity Long/Short Hedge Fund*: Consisting of one fund utilizing both long and short strategies seeking risk-adjusted returns principally through investment in the Asian-Pacific region. The fund is valued at NAV.

<sup>(5)</sup> *Event-Driven Hedge Funds*: Consisting of two funds, this strategy seeks to gain an advantage from pricing inefficiencies that may occur in the onset or aftermath of a corporate action or related event. These investments are valued at NAV per share.

<sup>(6)</sup> *Multi-Strategy Hedge Funds*: The three funds that make up this group aim to pursue varying strategies in order to diversify risks and reduce volatility. These investments are valued at NAV per share.

<sup>(7)</sup> *Relative Value Hedge Funds*: Consisting of five funds, this strategy's main focus is to benefit from valuation discrepancies that may be present in related financial instruments by simultaneously purchasing or selling these instruments. All five funds are valued at NAV.

<sup>(8)</sup> *Private Asset and Real Estate Funds*: KCERA's Private Asset portfolio consists of eight private equity funds with exposure to funds investing in buyouts, venture capital and special situations and three private credit funds directly investing in distressed credit, special situations and real estate. The Real Estate portfolio, comprised of five funds, invests mainly in U.S. commercial real estate and utilizes a combination of Core open-end commingled funds and closed-end Value-Added funds. The open-end funds are eligible for redemption on a quarterly basis. Distributions are received from the closed-end funds as underlying investments within the funds are liquidated. Individual holdings contained in the funds are valued at NAV using a combination of the income, cost and sales comparison approaches.

**NOTE 4 – FAIR VALUE MEASUREMENT**

The valuation method for investments measured at the net asset value (NAV) per share, or equivalent, is presented in the table below.

(In thousands)

Investments Measured at Net Asset Value (NAV)	6/30/2017	Redemption Frequency	Redemption Notice Period	Unfunded Commitments
Commingled Bond Funds <sup>(1)</sup>	\$ 748,251	Daily, Quarterly, None	2-30 Days	\$ -
Commingled Commodity Funds <sup>(1)</sup>	155,853	Daily, Monthly	1-30 Days	-
Commingled Equity Fund Domestic <sup>(1)</sup>	559,691	Daily, Quarterly	1-60 Days	-
Commingled Equity Fund Non-US <sup>(1)</sup>	389,416	Daily, Monthly	1-15 Days	-
Hedge Funds:				
CTA <sup>(2)</sup>	21,258	Monthly	30 Days	-
Directional <sup>(3)</sup>	42,547	Monthly	30-60 Days	-
Equity Long/Short <sup>(4)</sup>	22,619	Quarterly	45 Days	-
Event-Driven <sup>(5)</sup>	46,965	Quarterly, Annually, 36 Months	45-90 Days	-
Fund of Funds <sup>(6)</sup>	5	Semi-annually	91 Days	-
Multi-Strategy <sup>(7)</sup>	116,500	Quarterly, Annually	60-90 Days	-
Relative Value <sup>(8)</sup>	98,239	Monthly, Quarterly, Semi-annually	45-120 Days	-
Real Estate Funds <sup>(9)</sup>	224,933	Quarterly, None	30-45 Days	30,843
Private Asset Funds <sup>(9)</sup>	165,580	N/A	N/A	44,687
<b>Total</b>	<b>\$ 2,591,857</b>			<b>\$ 75,530</b>

<sup>(1)</sup> *Commingled Bond Funds, Commodity Funds and Equity Funds*: Five bond funds, three commodity funds and five equity funds are considered to be commingled in nature. Each is valued at the net asset value (NAV) of units held at the end of the period based upon the fair value of the underlying investments.

<sup>(2)</sup> *CTA*: The objective of this fund is to provide consistent long-term appreciation of assets through implementation of a systematic trading model or portfolio of systematic trading models that trade in a number of debt, equity, foreign exchange and commodity instruments and derivative contracts. The fund is valued at NAV.

<sup>(3)</sup> *Directional*: The three global macro funds utilizing this strategy seek to generate consistent long-term appreciation through active, direct and indirect, leveraged trading and investment on a global basis in multiple investment strategies. All three funds are valued at NAV.

<sup>(4)</sup> *Equity Long/Short Hedge Fund*: Consisting of one fund utilizing both long and short strategies seeking risk-adjusted returns principally through investment in the Asian-Pacific region. The fund is valued at NAV.

<sup>(5)</sup> *Event-Driven Hedge Funds*: Consisting of two funds, this strategy seeks to gain an advantage from pricing inefficiencies that may occur in the onset or aftermath of a corporate action or related event. These investments are valued at NAV per share.

<sup>(6)</sup> *Fund of Funds*: Side pocket of illiquid investments from the constituent underlying funds for a fund-of-funds terminated on 2013.

<sup>(7)</sup> *Multi-Strategy Hedge Funds*: The three funds that make up this group aim to pursue varying strategies in order to diversify risks and reduce volatility. These investments are valued at NAV per share.

<sup>(8)</sup> *Relative Value Hedge Funds*: Consisting of five funds, this strategy's main focus is to benefit from valuation discrepancies that may be present in related financial instruments by simultaneously purchasing or selling these instruments. All five funds are valued at NAV.

<sup>(9)</sup> *Private Asset and Real Estate Funds*: KCERA's Private Asset portfolio consists of 9 funds investing primarily in buyouts with some exposure to distressed funds, venture capital and special situations. The Real Estate portfolio, comprised of 5 funds, invests mainly in U.S. commercial real estate and utilizes a combination of Core open-end commingled funds and closed-end Value-Added funds. The open-end funds are eligible for redemption on a quarterly basis. Distributions are received from the closed-end funds as underlying investments within the funds are liquidated. Individual holdings contained in the funds are valued at NAV using a combination of the income, cost and sales comparison approaches.

**NOTE 5 – SECURITIES LENDING**

Under provisions of state statutes, the Board of Retirement permits KCERA to participate in a securities lending program, whereby securities are transferred to independent broker-dealers and other entities for collateral with a simultaneous agreement to return the collateral for the same securities plus a fee in the future. Deutsche Bank is KCERA's agent for securities lending.

Deutsche Bank is authorized to lend U.S. government obligations, U.S. bonds and equities, and international bonds and equities that are being held in custody to various borrowers, such as banks and brokers. Securities are lent for collateral. All securities loans can be terminated on demand by either KCERA or the borrower.

U.S. securities are loaned versus collateral valued at 102% of the fair value of the securities plus any accrued interest. Non-U.S. securities are loaned versus collateral valued at 110% of the fair value

of the securities plus any accrued interest. Marking to market is performed every business day subject to de minimis rules of change in value; the borrower is required to deliver additional collateral when necessary so that the total collateral held by the agent will at least equal the fair value of the borrowed securities. Deutsche Bank invests cash collateral in repurchase agreements on an overnight and term basis collateralized by readily liquid and marketable securities at 102% or greater.

At June 30, 2018 and 2017, KCERA had no credit risk exposure to borrowers due to the nature of the program's collateralization of loans at 102% or 110% plus accrued interest.

The tables below show the balances relating to securities lending transactions as of June 30, 2018 and 2017.

*As of June 30, 2018*

(in thousands)

Security Type	Fair Value of Loaned Securities		Fair Value of Loaned Securities	
	Securitized by Cash	Cash Collateral	Securitized by Non-Cash	Non-Cash Collateral
Domestic Equities	\$ 74,487	\$ 76,202	\$ 16,648	
International Equities	2,208	3,319	2,049	-
Corporate Bonds	54,890	55,538	83	-
Government Bonds	1,406	1,435	-	-
Treasuries	3,543	3,587	-	\$ 19,497
<b>Total</b>	<b>\$ 136,534</b>	<b>\$ 140,081</b>	<b>\$ 18,780</b>	<b>\$ 19,497</b>

*As of June 30, 2017*

(in thousands)

Security Type	Fair Value of Loaned Securities		Fair Value of Loaned Securities	
	Securitized by Cash	Cash Collateral	Securitized by Non-Cash	Non-Cash Collateral
Equities	\$ 53,179	\$ 54,520	\$ 15,603	\$ 15,728
Corporate Bonds	57,171	58,533	-	-
Government Bonds	9,877	10,101	-	-
<b>Total</b>	<b>\$ 120,227</b>	<b>\$ 123,154</b>	<b>\$ 15,603</b>	<b>\$ 15,728</b>

## NOTE 6 – DERIVATIVES

### Description of and Authority for Derivative Investments

KCERA invests in derivative financial investments (i.e., instruments) as authorized by the Board of Retirement. Investment managers may use derivatives where guidelines permit. A derivative instrument is defined as a contract that derives its value, usefulness and marketability from an underlying instrument that represents a direct ownership of an asset or a direct obligation of an issuer. Derivative instruments include, but are not limited to, futures, options, forward contracts, and interest rate or commodity swap transactions. All derivatives are considered investments by KCERA.

Substitution and risk control are the two derivative strategies permitted. *Substitution strategy* is when the characteristics of the derivative sufficiently parallel that of the cash market instruments; the derivatives may be substituted on a short-term basis for the cash market instrument. *Risk control strategy* is when the characteristics of the derivative sufficiently parallel that of the cash instrument; an opposite position from the cash instrument could be taken in the derivative instrument to alter the exposure to or the risk of the cash instrument.

Portfolios may not sell securities short nor create leverage through the use of financial futures and options. Uncovered futures or options positions are prohibited.

Financial futures and options may only be used to hedge currency risk or to manage portfolio duration. Investment in structured notes is prohibited. KCERA may invest in the following:

### *Futures*

Futures contracts are used to hedge against a possible increase in the price of currency. Futures contracts are classified by category of underlying instrument, such as equity, fixed income, commodity or cash equivalent. Derivative positions are tied to the performance of underlying securities. Futures contracts are priced “mark-to-market,” and daily settlements are recorded as investment gains or losses. Accounting for the daily mark-to-markets in this manner, the fair value of the futures contract at the end of the reporting period is the pending mark-to-market. For investment performance, risk and exposure purposes, KCERA’s custodian reports the notional fair values of futures contracts with corresponding offsets. When a futures contract is closed, futures are removed from the record with the final gain/loss equal to the fluctuation in value from the last mark-to-market to the closing value.

### *Options*

Options are used to manage risk exposures in certain accounts as a result of asset allocation requirements or unusual flows of cash to or from such accounts. Purchased put/call options are reported as assets with cost equal to the premium amount paid at inception, and written put/call options are reported as liabilities with cost equal to the premium received at inception. During the term of the options contracts, options are revalued at the end of each reporting period. Unrealized gains and losses are reported as the difference between the premium (cost) and the current fair value. At expiration, sale, or exercise, options are removed from record, and realized gains and losses are generally recognized. Because of the nature of options transactions, notional values are not included in the Investment Derivatives Summary table on page 44.

**NOTE 6 – DERIVATIVES****Description of and Authority for Derivative Investments (cont.)***Swaps*

Swap transactions are used to preserve a return or spread on investments to protect against currency fluctuations as a duration management technique or to protect against any increase in the price of securities. Because the fair values of swaps can fluctuate, swaps are represented as assets (if fair value is greater than zero) and liabilities (if fair value is less than zero). If a premium is paid or received at inception of the swap, the premium amount is generally recorded as the cost of the swap. During the term of the swap agreement, the periodic cash flows as either income or expense associated with the swap agreement. At each reporting period, swaps are revalued and unrealized gains or losses are reported. KCERA's custodian generally obtains swap valuations from a pricing vendor, the investment manager or the counterparty. At closing, KCERA's custodian removes the swap assets and liabilities from the record. The difference between any closing premium exchanged and the cost basis is recognized as realized gain or loss.

*Forward Exchange Contracts*

Forward exchange contracts are used for the purpose of hedging against adverse movement in currency exchange rates and to facilitate settlement of transactions in foreign securities. KCERA's reporting methodology for foreign exchange (FX) contracts reflects payables and receivables for the currencies to be exchanged while the forward FX contracts are pending; the two pending cash flows are valued separately. The overall cost basis

for a pending FX deal is zero (the net of the cost basis for the payable and receivable). Pending forward FX contracts are valued using the closing forward FX rate as of the report date. The difference between the forward rate (base fair value) at the reporting date and the contracted rate on trade date (base cost) of the forward FX contract is unrealized gain/loss. The difference between the spot rate applied at settlement date and the contracted rate on trade date is realized gain/loss at the settlement of the forward FX contract. KCERA does not discount the valuation of the anticipated cash flows associated with pending forward FX contracts.

**Summary of Investment Derivatives**

Investment derivative instruments are reported as investments (if fair value is greater than zero) or liabilities (if fair value is less than zero) as of fiscal year end on the Statement of Fiduciary Net Position. Listed market prices are used to report the fair values for derivative instruments, if available. If listed market prices are not available for derivative instruments, the price used may be from a vendor, an investment manager or a counterparty. All changes in fair value are reported in the Statement of Changes in Fiduciary Net Position as a component of investment revenue.

As of June 30, 2018 and 2017, KCERA has the following instruments outstanding (see Summary table below) with an objective to earn a rate of return consistent with KCERA's investment policies. Notional values listed on the Summary table that are positive (assets) or negative (liabilities) are aggregated for similar derivative types.

**NOTE 6 – DERIVATIVES**
**Investment Derivative Credit Risk**

The credit risk of using derivative instruments may include the risk that counterparties to contracts will not perform and/or the public exchange will not meet its obligation to assume this counterparty risk. KCERA is exposed to credit risk on investment derivatives traded over the counter and are reported in asset positions.

KCERA's derivative investment policy states that for non-exchange-traded derivative instruments, counterparty credit status shall be of the highest caliber with care taken to avoid credit guarantees

extended through to parties less credit-worthy than the primary counterparty to the transaction. Counterparty exposure is limited to firms with a short-term rating of A1/P1 or with a long-term credit rating of AA or better. Single counterparty exposure should be limited to 10% of the value of the fund.

A summary of counterparty credit ratings relating to non-exchange-traded derivatives in asset positions as of June 30, 2018 and 2017, in addition to a summary of KCERA's derivatives as of June 30, 2018 and 2017, are as follows:

**Investment Derivatives Summary and Summary of Credit Ratings**
*As of June 30, 2018*

(In thousands)

Investment Derivative Type	Changes in			S&P Credit Rating				
	Fair Value Gain (Loss)	Fair Value	Notional Value	AA	A	BBB	Exchange Traded	Not Available
Futures	\$ (1,532)	\$ -	\$ 3,912	\$ -	\$ -	\$ -	\$ -	\$ -
Options	46	(457)	(20)	-	(352)	(89)	(16)	-
Swaps	2,778	3,328	-	-	(241)	9	3,526	34
Foreign Exchange Contracts	(1,527)	346	-	-	-	-	-	346
Rights/Warrants Equity Contracts	6	-	-	-	-	-	-	-
<b>Total Value</b>	<b>\$ (229)</b>	<b>\$ 3,217</b>	<b>\$ 3,892</b>					
<b>Total Subject to Credit Risk</b>				<b>\$ -</b>	<b>\$ (593)</b>	<b>\$ (80)</b>	<b>\$ 3,510</b>	<b>\$ 380</b>

*As of June 30, 2017*

(In thousands)

Investment Derivative Type	Changes in			S&P Credit Rating				
	Fair Value Gain (Loss)	Fair Value	Notional Value	AA	A	BBB	Exchange Traded	Not Available
Futures	\$ (77)	\$ -	\$ (19,188)	-	-	-	-	-
Options	109	(31)	(3)	\$ -	\$ (114)	\$ -	\$ 96	\$ (13)
Swaps	(3,075)	1,987	-	-	49	-	1,847	91
Foreign Exchange Contracts	1,128	(646)	-	-	-	-	-	(646)
Rights/Warrants Equity Contracts	79	-	-	-	-	-	-	-
<b>Total Value</b>	<b>\$ (1,836)</b>	<b>\$ 1,310</b>	<b>\$ (19,191)</b>					
<b>Total Subject to Credit Risk</b>				<b>\$ -</b>	<b>\$ (65)</b>	<b>\$ -</b>	<b>\$ 1,943</b>	<b>\$ (568)</b>

**NOTE 6 – DERIVATIVES**
**Investment Derivative Interest Rate Risk**

Interest rate risk is the risk that changes in interest will adversely affect the fair value of an investment. KCERA measures derivative interest

rate risk using duration. At June 30, 2018 and 2017, KCERA had the following investment derivative interest rate risks:

*As of June 30, 2018*

(In thousands)

Derivative Investment Type	Notional Value	Fair Value	< 3 Months	3 to 6 Months	6 to 12 Months	1 to 5 Years	5 to 10 Years	10+ Years
Futures	\$ 3,912	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Options	(20)	(457)	(21)	2	(3)	(435)	-	-
Swaps	-	3,328	-	-	6	208	2,629	485
Forward Exchange Contracts	-	346	296	50	-	-	-	-
<b>Total</b>	<b>\$ 3,892</b>	<b>\$ 3,217</b>	<b>\$ 275</b>	<b>\$ 52</b>	<b>\$ 3</b>	<b>\$ (227)</b>	<b>\$ 2,629</b>	<b>\$ 485</b>

*As of June 30, 2017*

(In thousands)

Derivative Investment Type	Notional Value	Fair Value	< 3 Months	3 to 6 Months	6 to 12 Months	1 to 5 Years	5 to 10 Years	10+ Years
Futures	\$ (19,188)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Options	(3)	(31)	57	-	12	(100)	-	-
Swaps	-	1,987	33	-	-	201	1,510	243
Forward Exchange Contracts	-	(646)	(339)	-	(307)	-	-	-
<b>Total</b>	<b>\$ (19,191)</b>	<b>\$ 1,310</b>	<b>\$ (249)</b>	<b>\$ -</b>	<b>\$ (295)</b>	<b>\$ 101</b>	<b>\$ 1,510</b>	<b>\$ 243</b>



**NOTE 6 – DERIVATIVES**

**Investment Derivative Foreign Currency Risk**  
 Foreign currency risk is the risk that changes in currency exchange rates will adversely affect the  
*As of June 30, 2018*

fair value of an investment. At June 30, 2018 and 2017, KCERA had the derivative foreign currency exposures listed in the table below.  
 (In thousands)

	Foreign Currency	Fair Value (USD)
Cash Collateral/Variation Margin	Canadian Dollar	\$ 15
	Euro	619
	British Pound Sterling	80
	Japanese Yen	94
	Mexican Peso	295
Foreign Exchange Contracts	Canadian Dollar	(8,605)
	Swiss Franc	162
	Chinese Yuan Renminbi	(190)
	Danish Krone	(7,248)
	Euro	(2,131)
	British Pound Sterling	(1,734)
	Japanese Yen	2,557
	Mexican Peso	(211)
	Russian Ruble	(33)
	Canadian Dollar	29
Swaps	Euro	9
	British Pound Sterling	(50)
	Japanese Yen Mexican	(98)
	Peso	(288)
<b>Total Foreign Derivatives</b>		<b>\$ (16,728)</b>

*As of June 30, 2017* (In thousands)

	Foreign Currency	Fair Value (USD)
Cash Collateral/Variation Margin	Canadian Dollar	\$ (184)
	Euro	942
	British Pound Sterling	140
	Japanese Yen	78
	Australian Dollar	1,567
Foreign Exchange Contracts	Canadian Dollar	(6,973)
	Swiss Franc	(782)
	Chinese Yuan Renminbi	(185)
	Danish Krone	(8,002)
	Euro	(700)
	British Pound Sterling	(520)
	Japanese Yen	2,833
	South Korean Won	(2,217)
	Mexican Peso	(13)
	New Zealand Dollar	(1,568)
Options	Euro	17
	Canadian Dollar	217
Swaps	Euro	142
	British Pound Sterling	(84)
<b>Total Foreign Derivatives</b>		<b>\$ (15,292)</b>

**NOTE 7 – CONTRIBUTIONS**

Following the establishment of KCERA on January 1, 1945, eligible employees and their beneficiaries became entitled to pension, disability and survivor benefits under the provisions of the CERL. As a condition of participation under the provisions of the CERL, members are required to pay a percentage of their salaries, depending on their entry age in the Plan, membership type and benefit tier.

The funding objective of the KCERA Board of Retirement is to provide sufficient assets to permit the payment of all regular benefits promised under KCERA while minimizing the volatility of contribution rates for participating employers from year to year as a percentage of covered payroll. There are three sources of funding for KCERA retirement benefits: employer contributions, member contributions and investment earnings.

Total contributions made during fiscal years 2018 and 2017, respectively, amounted to approximately \$295.0 million and \$275.8 million, of which \$242.5 million and \$224.4 million were contributed by employers, and \$52.5 million and \$51.4 million were contributed by members.

**Pension Obligation Bonds**

In 1995 and 2003, the County of Kern issued pension obligation bonds and contributed \$224.5 million and \$285.1 million to the Plan, respectively. Special districts did not participate in the funding provided by pension obligation bonds. Therefore, different employer contribution rates are required to fund the unfunded liabilities for each class of participation.

**Cost-of-Living Adjustment**

On April 1, 1973, an annual cost-of-living adjustment (COLA) of up to 2% for all retirees and continuance beneficiaries was adopted. The 2% COLA was funded entirely from the unreserved fund balance until February 5, 1983. After this date and prior to fiscal year 2003, funding of the 2% COLA was included in the employers' contributions. In fiscal year 2002, the County of Kern activated Government Code Section 31617, which provides that COLAs shall be funded first from excess earnings, to the extent of such excess, and thereafter from employer contributions. In fiscal year 2018, the Plan had no excess earnings; \$0 was reserved to fund the employer COLA contributions in fiscal year 2018.

**Employer Contributions**

Each year, an actuarial valuation is performed for the purpose of determining the funded position of the retirement plan and the employer contributions necessary to pay benefits accruing to KCERA members not otherwise funded by member contributions or investment earnings. The employer contribution rates are actuarially determined by using the Entry Age Actuarial Cost Method. The Plan's employer rates provide for both "Normal Cost" and a contribution to amortize any unfunded or overfunded actuarial accrued liabilities. Contribution rates determined in each actuarial valuation (as of June 30) apply to the fiscal year beginning 12 months after the valuation date. Employer rates for fiscal year 2018 ranged from 28.72% to 63.48% of covered payroll, with a combined average of 44.78% for all employers.

## NOTE 7 – CONTRIBUTIONS

### Member Contributions

Member contributions are made through payroll deductions on a pre-tax basis, per IRS Code Section 414(h)(2). Member contribution rates for fiscal year 2018 ranged from 4.45% to 18.48% and were applied to the member's base pay plus "pensionable" special pay; they were calculated based on the member's KCERA entry age and actuarially calculated benefits. Members are required to contribute depending on the member's tier, employer and bargaining unit. For certain safety bargaining units, a flat member contribution rate is applied. "New members," as defined in PEPR, hired on or after January 1, 2013 pay a flat member contribution rate: 50% of the total Normal Cost rate.

For members covered by Social Security, the member contribution rates above apply to monthly salaries over \$350. (A one-third reduction in the rates applies to the first \$350 of monthly salary.)

As a result of the 1997 Memorandum of Understanding (MOU), some members received an employer "pick up" of their contributions. General members hired after MOU-specified dates in 2004 or 2005 and safety members hired after MOU-specified dates in 2007 were required to pay 100% of the employees' retirement contributions with the employer paying no part of the employees' contributions. Effective in 2014, non-contributing County general and safety members were required to pay one-third of their employee contributions. Buttonwillow Recreation and Park District and San Joaquin Valley Air Pollution Control District did not elect the 1997 MOU. Buttonwillow employees continue to pay 50% of their full rates. San Joaquin's Tier I members pay 50% of the Normal Cost rate as of June 30, 2018. Employees of the Kern County Superior Court are required to pay an additional 8% of base salary.

Interest is credited to member contributions semiannually on June 30 and December 31, in accordance with Article 5.5 of the CERL. Member contributions and credited interest are refundable upon termination of membership.

## NOTE 8 – RESERVE ACCOUNTS AND DESIGNATIONS OF NET POSITION

Member and employer contributions are allocated to various legally required reserve accounts based on actuarial determinations. Member, employer and retired members' reserves are fully funded. KCERA maintains the following reserve and designation accounts:

*Members' Deposit Reserve* – member contributions and interest allocation to fund member retirement benefits.

*Employers' Advance Reserve* – employer contributions and interest allocation to fund member retirement benefits.

*Cost-of-Living Reserve* – employer contributions and interest allocation to fund annual cost-of-living increases for retirees and their continuance beneficiaries.

*Retired Members' Reserve* – transfers from members' deposit reserve and employers' advance reserve, and interest allocation for funding of retirees' and their beneficiaries' monthly annuity payments.

*Supplemental Retiree Benefit Reserve* – monies reserved for enhanced, non-vested benefits to current and future retired members and their beneficiaries.

*COLA Contribution Reserve* – monies reserved to credit future employer COLA contributions.

*Contingency Reserve* – excess income to supplement deficient earnings. The contingency reserve satisfies the Government Code Section 31616 requirement for KCERA to reserve at least 1% of assets, up to a maximum of 3% of assets. At fiscal year ended June 30, 2018, -0.39% of the Plan's net position were in contingencies, according to the Board of Retirement's Interest Credit Policy.

**NOTE 8 – RESERVE ACCOUNTS AND DESIGNATION OF NET POSITION**

Balances in these reserve accounts and designations of net position available for pension and other benefits at June 30, 2018 and 2017

(under the five-year smoothed market asset valuation method for actuarial valuation purposes) are as follows:

(In thousands)

Reserve Account	2018	2017
Members' Deposit Reserve – General	\$ 244,678	\$ 225,695
Members' Deposit Reserve – Safety	117,439	103,224
Members' Deposit Reserve – Special District	25,259	22,673
Employers' Advance Reserve – General	401,996	359,449
Employers' Advance Reserve – Safety	442,448	388,434
Employers' Advance Reserve – Special District	43,598	38,473
Cost-of-Living Reserve – General	715,878	661,092
Cost-of-Living Reserve – Safety	509,151	469,813
Cost-of-Living Reserve – Special District	53,059	48,047
Retired Members' Reserve – General	1,122,463	1,089,422
Retired Members' Reserve – Safety	454,492	469,442
Supplemental Retiree Benefit Reserve (SRBR)	127,719	124,229
SRBR allocated for 0.5% COLA	49,370	53,850
Contingency Reserve	(16,355)	(16,355)
<b>Total reserves at five-year smoothed market actuarial valuation</b>	<b>4,291,195</b>	<b>4,037,302</b>
Market Stabilization Reserve*	(92,333)	(74,407)
<b>Total Fiduciary Net Position – Restricted for Pension Benefits</b>	<b>\$ 4,198,862</b>	<b>\$ 3,962,895</b>

\* The Market Stabilization Reserve represents the difference between the five-year smoothed fair value of the fund and the fair value as of the fiscal year end.

**NOTE 9 – COMMITMENTS AND CONTINGENCIES**
**Capital Commitments**

In fiscal year 2013, KCERA's Board approved funding new direct hedge fund managers. As of June 30, 2018, KCERA had funded \$387.2 million between 15 hedge funds managers to reach a target hedge fund allocation of 10% of the total portfolio.

As of June 30, 2018, KCERA's Board also had committed \$662.5 million to the private assets and real estate funds listed in the table below, with fair value totaling \$235.7 million. The general partner draws down invested capital from all limited partners when necessary, to fund investments.

**NOTE 10 – RELATED PARTY TRANSACTIONS**
**Office Lease**

KCERA, as the sole shareholder, formed a title holding corporation, KCERA Property, Inc. (KPI) for the purpose of accommodating the administrative offices of the Plan. In October 2010, KCERA entered into a build-to-suit lease agreement with KPI to occupy 14,348 square feet. KCERA is required to pay a monthly rate of \$1.75 per square foot as well as taxes, insurance and operating costs as defined in the agreement. The base rent was subject to an automatic 10.4% increase beginning on the fifth anniversary of the commencement date, November 2015, and on each fifth year anniversary date thereafter during the lease term. The sum of payments due for fiscal year ended June 30, 2018 is \$332,644 for base rent and \$12,815 for HVAC, insurance and assessment fees. KCERA's base rent and other costs are abated from KPI's rental income.

As of June 30, 2018

(In thousands)

Fund	Amounts			Fair Value
	Commitments	Funded	Distributions	
Abbott Capital Private Equity Fund IV	\$ 50,000	\$ 49,650	\$ 79,500	\$ 8,086
Abbott Capital Private Equity Fund V	65,000	62,725	73,745	17,608
Abbott Capital Private Equity Fund VI	50,000	48,750	36,500	39,896
Brookfield Real Estate Finance Fund V, L.P.	50,000	8,457	789	11,383
Colony Distressed Credit and Special Situations Fund IV	60,000	43,046	9,599	39,281
Invesco Real Estate Fund III	60,000	55,520	56,549	22,888
Invesco U.S. Value-Add Fund IV	50,000	36,248	10,826	32,199
Landmark Real Estate Partners VIII, L.P.	60,000	6,728	2,821	6,452
Pantheon USA Fund III	7,500	7,335	8,198	70
Pantheon USA Fund V	25,000	24,175	36,950	1,390
Pantheon USA Fund VI	35,000	33,075	42,630	9,701
Pantheon USA Fund VII	50,000	46,200	54,075	26,755
Pantheon Global Secondary Fund III "B"	50,000	47,300	45,950	7,161
TSSP Adjacent Opportunities Partners and Affiliated Partnerships	50,000	8,993	3,136	12,876
<b>Total</b>	<b>\$ 662,500</b>	<b>\$ 478,202</b>	<b>\$ 461,268</b>	<b>\$ 235,746</b>

**NOTE 11 – NET PENSION LIABILITY**

The components of the net pension liability are as follows:

	June 30, 2018	June 30, 2017
Total Pension Liability	\$ 6,529,662,330	\$ 6,326,870,318
Plan Fiduciary Net Position	(4,198,862,285)	(3,962,895,176)
<b>Net Pension Liability</b>	<b>\$ 2,330,800,045</b>	<b>\$ 2,363,975,142</b>
Plan Fiduciary Net Position as Percentage of Total Pension Liability	64.30%	62.64%

The Plan’s Fiduciary Net Position includes assets held for the Supplemental Retiree Benefit Reserve (SRBR). A split of the Total Pension Liability (TPL), Plan’s Fiduciary Net Position (FNP) and Net Pen-

sion Liability (NPL) by the regular benefits (non-SRBR) and the SRBR benefits as of June 30, 2017 and June 30, 2016 are shown in the tables below.

June 30, 2018	Regular Benefits (Non-SRBR)	SRBR Benefits	Total KCERA
Total Pension Liability	\$ 6,444,352,894	\$ 85,309,436	\$ 6,529,662,330
Plan Fiduciary Net Position	\$ 4,071,143,271	\$ 127,719,014	\$ 4,198,862,285
Net Pension Liability (Asset)	\$ 2,373,209,623	\$ (42,409,578)	\$ 2,330,800,045

June 30, 2017	Regular Benefits (Non-SRBR)	SRBR Benefits	Total KCERA
Total Pension Liability	\$ 6,270,652,272	\$ 56,218,046	\$ 6,326,870,318
Plan Fiduciary Net Position	\$ 3,838,665,847	\$ 124,229,329	\$ 3,962,895,176
Net Pension Liability (Asset)	\$ 2,431,986,425	\$ (68,011,283)	\$ 2,363,975,142

The Net Pension Liability (NPL) for the plan was measured as of June 30, 2018 and June 30, 2017. The Plan’s Fiduciary Net Position was valued as of the measurement dates while the Total Pension Liability (TPL) was determined based upon rolling forward the TPL from actuarial valuations as of June 30, 2017, and June 30, 2016, respectively.

*Plan provisions.* The plan provisions used in the measurement of the net pension liability are the same as those used in the KCERA actuarial valuation as of June 30, 2018 and June 30, 2017, respectively. The TPL and the Plan’s Fiduciary Net Position include liabilities and assets held for the Supplemental Retiree Benefit Reserve (SRBR).

*Actuarial assumptions and methods.* The TPLs as of June 30, 2018 and June 30, 2017 that were measured by actuarial valuations as of June 30, 2017 and June 30, 2016, respectively, used the same actuarial assumptions and actuarial cost method as the June 30, 2018 and June 30, 2017 funding valuations. The actuarial assumptions used in both valuations were based on the results of an experience study for the period from July 1, 2013 through June 30, 2016. In particular, the following actuarial assumptions were applied to all periods included in the measurement.

**NOTE 11 – NET PENSION LIABILITY**

As of June 30, 2018

<i>Inflation:</i>	3.00%
<i>Salary Increases:</i>	General: 4.00% to 9.00%. Safety: 4.00% to 12.50%. Varies by service, including inflation.
<i>Investment Rate of Return:</i>	7.25%, net of plan investment expenses, including inflation.
<i>Administrative Expenses:</i>	0.90% of payroll allocated to both employers and members based on the components of the total average contribution rate (before expenses) for employers and members.
<i>Other Assumptions:</i>	Same as those used in the June 30, 2018 funding valuation. These assumptions were developed in the analysis of actuarial experience for the period July 1, 2013 through June 30, 2016.

As of June 30, 2017

<i>Inflation:</i>	3.00%
<i>Salary Increases:</i>	General: 4.00% to 9.00%. Safety: 4.00% to 12.50%. Varies by service, including inflation.
<i>Investment Rate of Return:</i>	7.25%, net of plan investment expenses, including inflation.
<i>Administrative Expenses:</i>	0.90% of payroll allocated to both employers and members based on the components of the total average contribution rate (before expenses) for employers and members.
<i>Other Assumptions:</i>	Same as those used in the June 30, 2017 funding valuation. These assumptions were developed in the analysis of actuarial experience for the period July 1, 2013 through June 30, 2016.

The Entry Age Actuarial Cost Method used in KCERA’s annual actuarial valuation has also been applied in measuring the Service Cost and TPL with one exception. For purposes of measuring the Service Cost and TPL, KCERA has reflected the same plan provisions used in determining the member’s Actuarial Present Value of Projected Benefits. This is different from the version of this method applied in KCERA’s annual funding valuation, where the Normal Cost and Actuarial Accrued Liability are determined as if the current benefit accrual rate had always been in effect.

The long-term expected rate of return on pension plan investments was determined using a build-

ing-block method in which expected future real rates of return (i.e., expected returns, net of pension plan investment expenses and inflation) are developed for each major asset class. This data is combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation.

The target allocation and projected arithmetic real rates of return for each major asset class, after deducting inflation but before investment expenses, used in the derivation of the long-term expected investment rate of return assumption are summarized on the next page.

**NOTE 11 – NET PENSION LIABILITY**

	Target Allocation	Long-Term Expected Real Rate of Return	Weighted Average
Large Cap U.S. Equity	15%	5.61%	0.84%
Small Cap U.S. Equity	4%	6.37%	0.25%
Global Equity	6%	6.50%	0.39%
Developed International Equity	8%	6.96%	0.56%
Emerging Market Equity	4%	9.28%	0.37%
U.S. Core Fixed Income	19%	1.06%	0.20%
High Yield / Specialty	6%	3.65%	0.22%
Emerging Market Debt	4%	3.85%	0.15%
Core Real Estate	5%	4.37%	0.22%
Value-Added Real Estate	5%	6.00%	0.30%
Commodities	4%	3.76%	0.15%
Hedge Funds	10%	4.70%	0.47%
Private Equity	5%	8.70%	0.44%
Private Credit	5%	5.10%	0.26%
<b>Total</b>	<b>100%</b>		<b>7.82%*</b>

\*includes inflation at 3.00%

*Discount rate:* The discount rate used to measure the TPL was 7.25% as of June 30, 2018 and June 30, 2017. The projection of cash flows used to determine the discount rates assumed plan member contributions will be made at the current contribution rate and that employer contributions will be made at rates equal to the actuarially determined contribution rates.

For this purpose, only employee and employer contributions intended to fund benefits for current plan members and their beneficiaries are included. Projected employer contributions intended to fund the service costs for future plan members and their beneficiaries, as well as projected contributions from future plan members, are not included. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments for current plan members.

Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the TPL as of both June 30, 2018 and June 30, 2017.

The discount rate assumptions have been developed without taking into consideration any impact of the 50/50 allocation of future excess earnings between the retirement and Supplement Retiree Benefit Reserve (SRBR) asset pools.

*Sensitivity of the net pension liability to changes in the discount rate:* The following presents the NPL of KCERA as of June 30, 2018, calculated using the discount rate of 7.25%, as well as what KCERA's NPL would be if it were calculated using a discount rate that is 1 percentage point lower (6.25%) or 1 percentage point higher (8.25%) than the current rate:

	1% Decrease (6.25%)	Current (7.25%)	1% Increase (8.25%)
Net Pension Liability as of June 30, 2018	\$ 3,198,828,485	\$ 2,330,800,045	\$ 1,617,558,748
	1% Decrease (6.25%)	Current (7.25%)	1% Increase (8.25%)
Net Pension Liability as of June 30, 2017	\$ 3,214,150,584	\$ 2,363,975,142	\$ 1,665,995,113



**SCHEDULE OF CHANGES IN NET PENSION LIABILITY AND RELATED RATIOS  
FOR FISCAL YEARS ENDED JUNE 30**

(In thousands)

	2018	2017	2016	2015	2014	2013
<i>Total Pension Liability:</i>						
Service Cost	\$ 123,407	\$ 122,184	\$ 123,181	\$ 125,161	\$ 125,118	\$ 125,644
Interest	450,172	438,385	427,646	415,820	400,559	384,837
Change of Benefit Terms	31,034	-	-	5,036	-	-
Differences between Expected and Actual Experience	(80,208)	(109,368)	(105,053)	(89,306)	(57,034)	(49,064)
Changes of Assumptions	-	196,259	-	-	205,039	-
Benefit Payments, including Refunds Net	(321,613)	(305,817)	(288,738)	(273,865)	(257,495)	(242,630)
Change in Total Pension Liability	202,792	341,643	157,036	182,846	416,187	218,787
<i>Total Pension Liability: Beginning of Year</i>	<u>6,326,870</u>	<u>5,985,227</u>	<u>5,828,191</u>	<u>5,645,345</u>	<u>5,229,159</u>	<u>5,010,372</u>
<i>Total Pension Liability: End of Year (a)</i>	<b>6,529,662</b>	<b>6,326,870</b>	<b>5,985,227</b>	<b>5,828,191</b>	<b>5,645,346</b>	<b>5,229,159</b>
<i>Plan Fiduciary Net Position:</i>						
Contributions – Employer	242,534	224,351	234,713	215,477	220,393	211,677
Contributions – Employee	52,504	51,410	33,279	30,325	25,810	20,283
Net Investment Income	267,659	426,606	(27,535)	81,931	487,591	319,432
Benefit Payments, including Refunds	(321,613)	(305,817)	(288,738)	(273,864)	(257,495)	(242,630)
Administrative Expense	(5,117)	(5,243)	(5,224)	(4,887)	(4,958)	(4,016)
Net Change in Plan Fiduciary Net Position	235,967	391,307	(53,505)	48,982	471,341	304,746
<i>Plan Fiduciary Net Position:</i>						
<i>Beginning of Year</i>	<u>3,962,895</u>	<u>3,571,587</u>	<u>3,625,093</u>	<u>3,576,112</u>	<u>3,104,770</u>	<u>2,800,024</u>
<i>Plan Fiduciary Net Position: End of Year (b)</i>	<b>4,198,862</b>	<b>3,962,895</b>	<b>3,571,587</b>	<b>3,625,093</b>	<b>3,576,112</b>	<b>3,104,770</b>
<i>Net Pension Liability: (a) - (b)</i>	<b>\$ 2,330,800</b>	<b>\$ 2,363,975</b>	<b>\$ 2,413,639</b>	<b>\$ 2,203,098</b>	<b>\$ 2,069,234</b>	<b>\$ 2,124,389</b>
Plan Fiduciary Net Position as a Percentage of Total Pension Liability	64.30%	62.64%	59.67%	62.20%	63.35%	59.37%
Covered Payroll*	\$ 576,729	\$ 546,671	\$ 537,540	\$ 531,598	\$ 533,851	\$ 543,558
Plan Net Pension Liability as a Percentage Of Covered Payroll	404.14%	432.43%	449.02%	414.43%	387.61%	390.83%

The pension schedules in the required supplementary information are intended to show information for ten years. Data is provided only for those years for which information is available. Additional years' information will be displayed when it becomes available.

\* "Covered payroll" represents compensation earnable and pensionable compensation. Only compensation earnable and pensionable compensation that would possibly go into the determination of retirement benefits are included.

**SCHEDULE OF EMPLOYER CONTRIBUTIONS**

Year Ended June 30	Actuarially Determined Contributions	Contributions in Relation to Actuarially Determined Contributions	Contribution Deficiency (Excess)	Covered Payroll	Contributions as % of Covered Payroll
2009	\$ 138,815,000	\$ 138,815,000	0	\$ 482,879,000	28.74%
2010	\$ 151,127,000	\$ 151,127,000	0	\$ 559,872,000	26.99%
2011	\$ 177,444,000	\$ 177,444,000	0	\$ 559,380,000	31.72%
2012	\$ 189,837,000	\$ 189,837,000	0	\$ 526,079,162	36.09%
2013	\$ 211,677,000	\$ 211,677,000	0	\$ 516,465,189	40.99%
2014	\$ 220,393,000	\$ 220,393,000	0	\$ 533,850,811	41.28%
2015	\$ 215,477,000	\$ 215,477,000	0	\$ 531,598,183	40.53%
2016	\$ 216,229,000	\$ 216,229,000	0	\$ 537,539,991	40.23%
2017	\$ 224,351,000	\$ 224,351,000	0	\$ 546,671,003	41.04%
2018	\$ 242,534,000	\$ 242,534,000	0	\$ 576,728,789	42.05%

**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION**

**Methods and assumptions used to establish actuarially determined contribution rates:**

- Valuation date:** Actuarially determined contribution rates are calculated as of June 30, two years prior to the end of the fiscal year in which contributions are reported.
- Actuarial cost method:** Entry Age Actuarial Cost Method.
- Amortization method:** Level percent of payroll for total unfunded liability (assuming 3.625% increase).
- Remaining amortization period:** 17.5 years as of June 30, 2018 for all UAAL as of June 30, 2011. Effective June 30, 2012, any changes in UAAL due to actuarial gains or losses or due to changes in actuarial assumptions or methods will be amortized over an 18-year closed period, effective with each valuation. Any change in unfunded actuarial accrued liability that arises due to plan amendments is amortized over its own declining 15-year period (except for a change due to retirement incentives, which is amortized over a declining period of up to 5 years).
- Asset valuation method:** Fair value of assets less unrecognized returns in each of the last five years. Unrecognized returns are equal to the difference between the actual market return and the expected return on a fair value basis and are recognized semiannually over a five-year period. The Actuarial Value of Assets is reduced by the value of the non-valuation reserves.

**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION (cont.)**

	June 30, 2018	June 30, 2017
<b>Actuarial Assumptions:</b>		
<i>Investment rate of return</i>	7.25%, net of investment expenses, including inflation	7.25%, net of investment expenses, including inflation
<i>Inflation rate</i>	3.00%	3.0%
<i>Real across-the-board salary increase</i>	0.50%	0.50%
<i>Projected salary increases*</i>	General: 4.00% to 9.00% Safety: 4.00% to 12.50%	General: 4.00% to 9.00% Safety: 4.00% to 12.50%
<i>Administrative expenses</i>	0.90% of payroll allocated to both the employer and member based on the components of the total average contribution rate (before expenses) for the employer and member	0.90% of payroll allocated to both the employer and member based on the components of the total average contribution rate (before expenses) for the employer and member
<i>Cost-of-living adjustments</i>	2.5% (actual increases based on CPI increases with a 2.5% maximum)	2.5% (actual increases based on CPI increases with a 2.5% maximum)
<i>Other assumptions</i>	Same as those used in the June 30, 2018 funding actuarial valuation	Same as those used in the June 30, 2017 funding actuarial valuation

\* For 2018 and 2017, includes inflation at 3.00% plus real across-the-board salary increase of 0.50% plus merit and promotional increases.

**SCHEDULE OF MONEY-WEIGHTED RATES OF RETURNS FOR LAST 10 FISCAL YEARS ENDED JUNE 30**

	2018	2017	2016	2015	2014	2013
Annual Money-Weighted Rate of Return*	6.8%	12.0%	0.3%	3.0%	15.5%	10.8%

\* Net of investment expenses.

Data is provided only for those years for which information is available.

**SCHEDULE OF ADMINISTRATIVE EXPENSES  
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

	2018	2017
<i>Staffing:</i>		
Salaries	\$ 1,827,083	\$ 1,804,212
Benefits	1,246,085	1,339,368
Temporary staff	<u>33,846</u>	<u>16,380</u>
Staffing Total	3,107,014	3,159,960
<i>Staff Development</i>	58,079	44,427
<i>Professional Fees:</i>		
Actuarial fees	33,526	51,964
Audit fees	39,750	51,000
Consultant fees	61,991	28,873
Legal fees	<u>65,187</u>	<u>82,396</u>
Professional Fees Total	200,454	214,233
<i>Office Expenses:</i>		
Building expenses	62,328	53,361
Communications	16,597	16,339
Equipment lease	10,780	13,011
Equipment maintenance	20,155	7,447
Memberships	8,750	8,012
Office supplies & misc. admin.	46,480	25,586
Payroll & accounts payable fees	6,147	6,010
Postage	25,513	38,798
Subscriptions	13,016	6,655
Utilities	<u>43,359</u>	<u>41,422</u>
Office Expenses Total	253,125	216,641
<i>Insurance</i>	127,538	128,124
<i>Member Services:</i>		
Benefit payment fees	34,977	43,791
Disability - legal fees	57,262	50,465
Disability - medical advisors	61,206	120,445
Disability - professional services	39,098	34,054
Member communications	<u>27,144</u>	<u>37,050</u>
Members Services Total	\$ 219,687	\$ 285,805

See accompanying independent auditors' report. Schedule continued on next page.

**SCHEDULE OF ADMINISTRATIVE EXPENSES  
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017 (cont.)**

	2018	2017
<i>Systems:</i>		
Audit - security & vulnerability scan	\$ 7,650	\$ 9,800
Business continuity expenses	8,073	10,437
Hardware	83,611	97,192
Licensing & support	273,166	247,290
Software	40,224	72,014
Website design	<u>885</u>	<u>1,560</u>
Systems Total	413,609	438,293
<i>Board of Retirement:</i>		
Board compensation	11,175	9,203
Board conferences & training	47,776	24,827
Board elections	-	46,299
Board meetings	<u>5,759</u>	<u>1,621</u>
Board of Retirement Total	64,710	81,950
<i>Depreciation / Amortization</i>	672,256	673,792
<b>Total Administrative Expenses</b>	<b>\$ 5,116,472</b>	<b>\$ 5,243,225</b>

**SCHEDULE OF INVESTMENT EXPENSES  
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

	2018	2017
<i>Investment Manager Fees:</i>		
Equity	\$ 8,010,189	\$ 5,587,224
Fixed income	3,358,730	2,972,414
Commodities	1,631,711	1,241,604
Real estate	4,047,290	2,225,336
Private equity / Credit funds	2,228,395	2,187,500
Hedge funds	<u>10,254,369</u>	<u>9,064,841</u>
Total Investment Manager Fees	29,530,684	23,278,919
<i>Other Investment Expenses:</i>		
Custodian	344,565	327,627
Actuarial valuation	307,393	140,894
Investment consultants	970,878	761,855
Legal fees	127,398	28,675
Due diligence	1,561	36,001
Real estate	<u>39,445</u>	<u>34,579</u>
Total Other Investment Expenses	1,791,240	1,329,631
<b>Total Fees and Other Investment Expenses</b>	<b>31,321,924</b>	<b>24,608,550</b>
<i>Securities Lending Rebates and Bank Fees</i>	84,256	55,521
<b>Total Investment Expenses</b>	<b>\$ 31,406,180</b>	<b>\$ 24,664,071</b>

See accompanying independent auditors' report.

**SCHEDULE OF PAYMENTS TO CONSULTANTS  
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

Individual or Firm	Nature of Service	Commission / Fee	
		2018	2017
Cortex Applied Research, Inc.	Policy consultants	\$ 48,750	\$ 20,641
Segal Consulting	Actuarial services	33,526	51,964
Kern County Counsel	Legal counsel	59,308	56,747
Hanson Bridgett	Legal counsel	-	3,236
Nossaman LLP	Legal counsel	41,685	56,322
Ice Miller	Legal counsel	5,843	4,611
Reed Smith LLP	Legal counsel	15,614	11,945
Upside Strategies	HR consultants	-	8,216
CliftonLarsonAllen	External auditors	39,750	51,000
Agility Recovery Solutions	Disaster recovery	8,073	8,073
Aurora Systems Consulting	System audit	-	9,800
TraceSecurity LLC	System audit	7,650	-
<b>Total Payments to Consultants</b>		<b>\$ 260,199</b>	<b>\$ 282,555</b>

*These payments were made to outside consultants other than investment professionals. A Schedule of Investment Fees is presented on pages 76-78 in the Investment Section.*

*See accompanying independent auditors' report.*

# **INVESTMENT**

## **Section**



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October 3, 2018

Mr. Dominic Brown  
Executive Director  
Kern County Employees' Retirement Association  
11125 River Run Boulevard  
Bakersfield, CA 93311

**Dear Mr. Brown,**

Verus is pleased to have had the opportunity to serve the Kern County Employees' Retirement Association since July 2011 and to provide this investment review for the fiscal year ending June 30, 2018.

Verus independently calculated the Fund's fiscal year performance results utilizing a time-weighted annualized rate of return methodology (modified Dietz method) with data on market valuations and transactions provided by the Fund's custodian bank, the Northern Trust Company. For the fiscal year ended June 30, 2018, KCERA's retirement fund had an investment gain of 6.8% (gross of fees) and 6.5% (net of fees) and ended the fiscal year with total assets of approximately \$4.15 billion.

All KCERA's investments are managed according to guidelines codified in KCERA's Statement of Investment Goals, Objectives and Policies. This Statement is reviewed periodically to ensure best practices are employed in all aspects of our work and was last updated in July 2016.

Capital Markets Review

Here in the U.S., the economy has displayed relative strength in several ways. First, real GDP grew at an annualized quarterly rate of 4.1% in the second quarter of 2018, marking the strongest quarterly annualized growth rate since 2014. Also, the rate of inflation picked up, reaching 2.3% year-over-year, which is just above the Fed's objective target. In addition, the Fed raised rates for the second time this year, to a target range of 1.8% to 2.0%. Further, the labor market has shown continuous improvement, as headline unemployment pushed lower to 4.0%. Despite such a low unemployment figure that many observers would interpret as full employment, there may still be some room to run, since the entire labor force is not captured in traditional unemployment measures. For example, looking at the number of Americans employed illustrates a different picture, since a larger portion of the population remains unemployed relative to the period just before the financial crisis 10 years ago.

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“Synchronized global growth” has been a key narrative for much of the past fiscal year, leading to a favorable environment for investments traditionally viewed as higher risk. More recently, however, that story is being tested as economies worldwide have displayed disparate performance. While the narrative remains broadly intact, global growth has moderated with some regions outpacing others. In the Eurozone for example, many economies in the region missed expectations in several areas including GDP growth, retail sales, and industrial production. This is casting some doubt over the vitality of European recovery story. Labor markets tightened broadly, in-line with an environment of positive economic expansion. However, joblessness in some Eurozone countries such as Italy, Spain, and Greece, remains stubbornly high. Within emerging market economies, several of the larger economies reported favorable key indicators. However, stocks and other investments in these regions have posted disappointing returns, impacted by U.S. dollar strength and contagion concerns arising from smaller countries such as Argentina and Turkey, which face political as well as economic pressure.

Worldwide, interest rates remain near historic lows, but the era of monetary stimulus appears to be waning. In a Bloomberg report, there are three times the number of central banks raising rates compared to those that are cutting. In June, Mario Draghi officially announced the end of Europe’s bond buying program with asset purchases scheduled to end in December.

Equity markets performed favorably over the past fiscal year with the S&P 500 appreciating 14.4%. Growth stocks outperformed value as the Russell 1000 Growth outpaced the Russell 1000 Value 22.5% to 6.8% over the same period. International equities from developed nations, represented by the MSCI EAFE cooled in the latter half of the year but still finished the fiscal year up 6.8% despite the currency headwinds posed by a strengthening U.S. Dollar. Emerging markets followed a similar path and struggled in the latter portion of the fiscal year as the MSCI EM index returned -8.0% over the second quarter of 2018 but still managed a positive 8.2% return over the trailing one-year period. Real Estate’s solid performance continued with the NCREIF-ODCE index advancing 8.4% for the fiscal year while U.S. Bonds were down slightly, as the Bloomberg Barclays Aggregate Index fell 0.4% over the same period.



Asset Allocation

At fiscal year-end, KCERA’s asset allocation was broadly in line with Investment Policy targets, as shown in the table below:

Asset Class	Target	Year-End Allocation*
Domestic Equity	19%	20.5%
International Equity	18%	21.1%
Fixed Income	29%	35.1%
Real Estate	10%	5.6%
Hedge Funds	10%	9.4%
Private Equity	5%	2.5%
Private Credit	5%	1.5%
Commodities	4%	4.2%
Cash	0%	0.1%

*\*May not sum to 100% due to rounding*

The overweight to fixed income at the end of the fiscal year is due to the use of the asset class as a holding place for scheduled investments in private credit and real estate.

Investment Performance

Plan performance fell short of the actuarial assumed rate of return and the policy benchmark, as the total fund returned 6.8% for the fiscal year, versus the policy benchmark return of 7.0%. The primary cause of the shortfall was Plan’s overweight to fixed income in a strong equity market environment. This allocation effect was partially offset by favorable attribution highlighted below:

- KCERA’s Domestic Equity composite return 16.1% and outperformed the benchmark Russell 3000 Index return of 14.8%.
- The International Equity allocation returned 9.4% for the fiscal year, beating the benchmark return of 7.8% over the same period.
- KCERA’s Fixed Income composite, which includes a broad selection of domestic and international bonds, returned 0.2% and outperformed the Barclays Aggregate Bond Index by 60 basis points.



As always, Verus greatly appreciates the opportunity to assist the KCERA Board in meeting the Plan's long-term investment objectives. We look forward to continuing in our role of investment advisor and providing guidance to help navigate ever-changing capital markets.

Sincerely,

A handwritten signature in blue ink, appearing to read "Scott J. Whalen".

Scott J. Whalen, CFA  
Executive Managing Director

**POLICIES ADOPTED BY THE BOARD OF RETIREMENT ON MARCH 9, 2016**

**General Information**

The Board of Retirement (the Board) has exclusive control of the investments of the retirement fund and, therefore, establishes investment policies and implements investment decisions. The overall objective of KCERA’s investment program is to prudently invest assets such as to offset some of the costs of the Plan in providing the retirement benefits required by the County Employees’ retirement Law of 1937.

The Board is governed by Government Code Sections 31594 and 31595, which provide a standard of care commonly known as the “prudent expert rule,” a rule that recognizes that special skill and knowledge may be necessary in order to invest the fund prudently. Accordingly, the Board retains a number of professional investment advisers and investment consultants. The Board is required to diversify the investments of the Plan so as to minimize the risk of loss and to maximize the rate of return, unless it is clearly prudent not to do so.

The Board consists of nine members and two alternate members. Four members of the Board are appointed by the Kern County Board of Supervisors; four members are elected by active and retired members of KCERA; and the County Treasurer-Tax Collector is a statutory member of the Board.

**Summary of Investment Guidelines**

The Board of Retirement has adopted an Investment Policy Statement to serve as the

framework for investment policy making and investment objective setting within the context of applicable California laws. The Statement establishes investment guidelines, objectives and policies, and defines the responsibilities of the Board members in regard to KCERA’s investments. The investment philosophy articulated in the Statement is outlined below:

- Protecting the corpus of the Fund;
- Managing the fund in a prudent manner, recognizing risk and return trade-offs;
- Earning adequate investment returns in order to protect and pay the benefits promised to the participants with a minimum amount of associated risk;
- Maintaining sufficient liquidity to fund expenses and benefit payments as they come due; and
- Complying with applicable law.

**Summary of Proxy Voting Guidelines**

The Board has established the KCERA Proxy Voting Policy for dealing with proxies. This policy considers shareholder voting on corporate issues to represent assets of the Plan to be voted in the best interests of the beneficiaries of the Plan. The voting of proxies is delegated to a third party to vote on behalf of the Board according to the guidelines established in the policy. The Board is responsible to monitor proxy voting to see that its policies are implemented effectively.

## ASSET ALLOCATION

The Board of Retirement periodically establishes an asset allocation policy aimed at achieving a long-term rate of return on the fund’s investments such as to prudently add income to the fund to help provide the benefits promised. The asset allocation statement provides a target allocation or weighting to each of the broad investment classes of assets along with allowable ranges of weightings around each target weight. The target weights are viewed as longer-term objectives to be funded in a manner consistent with efficiency and cost savings. The asset allocation policy provides the target level of diversification among asset classes anticipated for the future. Asset allocation is reviewed on an annual basis to ensure that the expectations and assumptions incorporated in the policy remain valid and appropriate. Investment performance is monitored on quarterly, annual and multi-year basis. The asset allocation of the fund is rebalanced, as needed, but also in view of the costs of such transactions.

The Board engages external professional investment advisers to invest various portions of the fund. The advisers are, however, constrained to invest as provided in KCERA’s investment policies and allocation guidelines. Investment advisers formally notice their compliance with such policies, and their portfolios are scrutinized for compliance at regular intervals. KCERA’s investment consultant and investment staff participate in policy formulation and new manager searches, as well as in the termination of existing managers failing to perform or maintain compliance with their investment mandates.

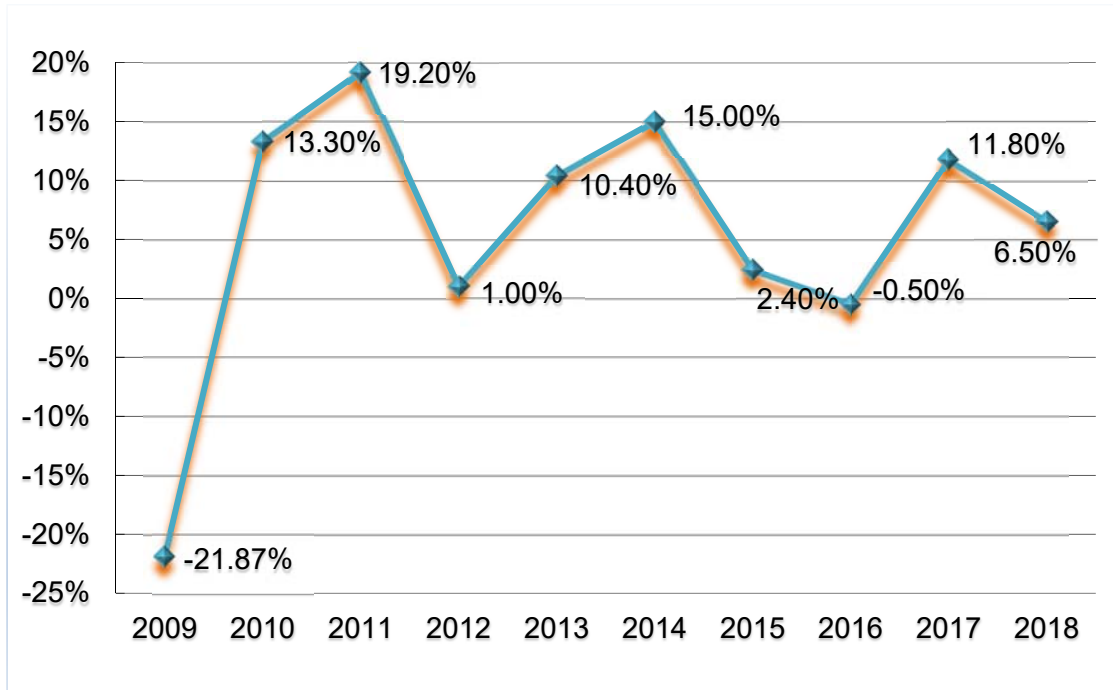
The Board of Retirement adopted the current asset allocation policy in July 2016. KCERA’s strategic target asset allocation and actual asset allocation as of June 30, 2018 are as follows:

Asset Class	Actual	Target	Target Ranges	
			Minimum	Maximum
Domestic Equity	20.5%	19.0%	10.0%	30.0%
International / Global Equity	21.1%	18.0%	10.0%	30.0%
Global Fixed Income	35.1%	29.0%	19.0%	39.0%
Real Estate	5.6%	10.0%	3.0%	15.0%
Private Equity	2.5%	5.0%	0.0%	10.0%
Hedge Funds	9.4%	10.0%	0.0%	15.0%
Commodities	4.2%	4.0%	0.0%	8.0%
Private Credit	1.5%	5.0%	0.0%	8.0%
Cash and Equivalents	0.1%	0.0%	0.0%	5.0%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>		

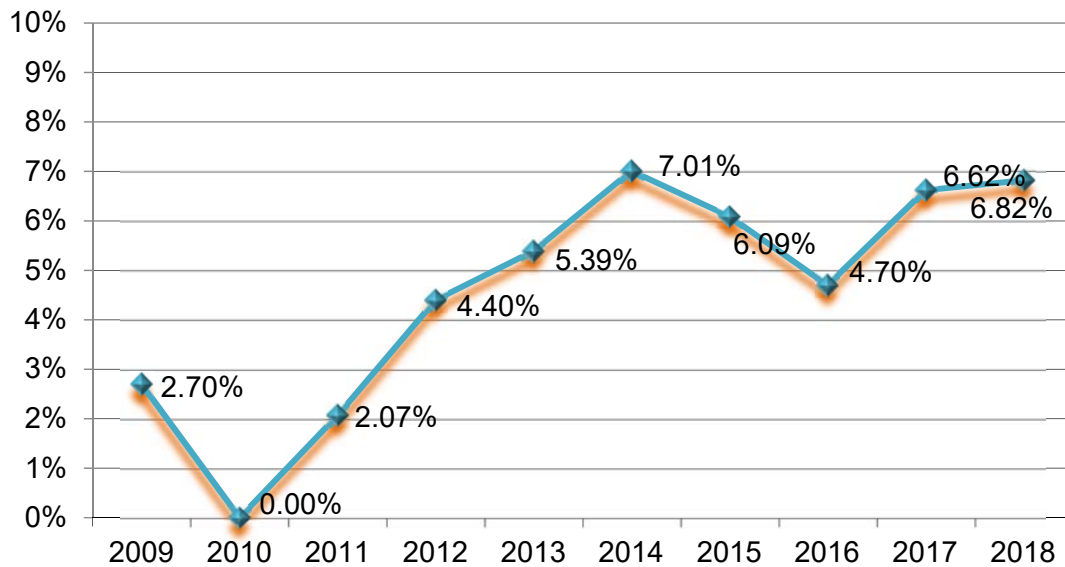
Type of Investment	Fair Value (In thousands)	% of Total Fair Value
<i>Domestic Equities:</i>		
All Cap Passive	\$ 215,157	5.18
Large Cap Enhanced	431,610	10.40
Small Cap Growth	97,368	2.35
Small Cap Value	<u>106,999</u>	<u>2.58</u>
Total Domestic Equities	851,134	20.51
<i>International / Global Equities:</i>		
Large Cap	306,686	7.39
Global	229,985	5.54
Small Cap	160,888	3.87
Emerging Markets	<u>176,686</u>	<u>4.26</u>
Total International Equities	874,245	21.06
<i>Fixed Income:</i>		
Core	502,542	12.11
Core Plus	490,966	11.83
Structured Debt	94,631	2.28
High Yield	204,108	4.92
Emerging Markets	<u>164,053</u>	<u>3.95</u>
Total Fixed Income	1,456,300	35.09
<i>Real Estate:</i>		
Core	176,427	4.25
Value Added	54,041	1.30
Opportunistic	3,907	0.09
Property	<u>4,360</u>	<u>0.11</u>
Total Real Estate	238,735	5.75
<i>Alternative Investments:</i>		
Private Credit	61,694	1.49
Private Equities	104,465	2.52
Hedge Funds	388,122	9.35
Commodities	<u>175,300</u>	<u>4.22</u>
Total Alternative Investments	729,581	17.58
<i>Cash &amp; Cash Equivalents</i>	304	0.01
<i>Assets in Liquidation</i>	0	0.00
<b>Total Investments</b>	<b>\$ 4,150,299</b>	<b>100.00</b>
KCERA Capital Assets	3,205	
KCERA Receivables / Payables	45,358	
<b>Fiduciary Net Position</b>	<b>\$ 4,198,862</b>	



**ANNUAL RETURNS (NET OF FEES)  
FOR PERIODS ENDED JUNE 30**



**FIVE-YEAR SMOOTHED ASSET VALUATION  
FOR PERIODS ENDED JUNE 30**



KCERA uses the five-year smoothed spread gain valuation method to allocate investment earnings greater than (or less than) the assumed investment return (i.e., actuarial assumption rate minus actual rate). The reserve account balances reflect the five-year smoothed asset valuation

method for actuarial purposes. In accordance with KCERA’s Interest Crediting Policy, when investment returns would result in a negative five-year smoothed rate, KCERA sets the smoothed rate at 0.00% and credits the Contingency Reserve with the negative balance.

RETURNS FOR PERIODS ENDED JUNE 30

	Current Year	Annualized		
		3-Year	5-Year	10-Year
Total Fund:	6.5	5.8	6.9	5.1
Benchmark: Policy Index*	7.0	5.7	6.5	5.8
Domestic Equity:	15.5	12.5	13.6	10.3
Benchmark: Russell 3000	14.8	11.6	13.3	10.2
International Equity:	8.7	5.9	7.7	3.7
Benchmark: MSCI ACWI ex-US	7.8	5.6	6.5	3.0
Global Fixed Income:	-0.1	2.7	2.7	4.8
Benchmark: Barclays US Aggregate	-0.4	1.7	2.3	3.7
Real Estate:	7.1	8.4	10.9	N/A
Benchmark: NCREIF-ODCE	8.4	9.4	11.0	N/A
Hedge Funds:	6.8	2.7	4.0	3.0
Benchmark: Policy Index**	7.0	5.8	5.9	5.1
Private Equity:	7.8	7.7	10.1	6.9
Benchmark: Russell 3000 + 300 bps	17.2	13.5	16.5	12.9
Private Credit:	9.3	N/A	N/A	N/A
BoA ML High Yield Master II + 2%	4.6	N/A	N/A	N/A
Commodities:	12.5	-0.5	-4.8	N/A
Benchmark: Bloomberg Comm. Index	7.3	-4.5	-6.4	N/A

\* Total Fund: 19% Russell 3000  
 18% MSCI ACWI ex-U.S.  
 29% Barclays US Aggregate  
 10% NCREIF Property  
 4% Bloomberg Commodities  
 7.5% 91-Day T-Bills + 400 bps  
 2.5% MSCI ACWI  
 5% Russell 3000 + 300 bps  
 5% ICE BofA ML High Yield  
 Master II + 200 bps

\*\* Hedge Fund: 75% 90-Day T-Bills + 400 bps  
 25% MSCI ACWI

Note: Return calculations were prepared, net of fees, using a time-weighted rate of return based on fair values.

CONSULTANTS
Verus Investments Albourne America LLC
CUSTODIAN
The Northern Trust Company
THIRD-PARTY SECURITIES LENDING
Deutsche Bank
INVESTMENT MANAGERS
<p><b><u>Domestic Equity</u></b>                      Alliance Bernstein Trust Company                      Henderson Geneva Capital Management                      Mellon Capital Management Corporation                      Pacific Investment Management Company</p> <p><b><u>International / Global Equity</u></b>                      Alliance Bernstein Trust Company                      BlackRock Institutional Trust Company                      Dimensional Fund Advisors, L.P.                      Dodge &amp; Cox Funds                      Fidelity Institutional Asset Management                      Sustainable Growth Advisors</p> <p><b><u>Global Fixed Income</u></b>                      Gramercy Funds Management LLC                      Mellon Capital Management Corporation                      Pacific Investment Management Company                      Stone Harbor Investment Partners                      TCW                      Western Asset Management Company</p> <p><b><u>Private Equity</u></b>                      Abbott Capital Management, LLC                      Pantheon Ventures, Inc.</p>

INVESTMENT MANAGERS (CONT.)
<p><b><u>Real Estate</u></b>                      ASB Real Estate Investors                      Invesco Real Estate Funds                      J. P. Morgan Chase Bank                      Landmark Real Estate Partners</p> <p><b><u>Commodities</u></b>                      Gresham Investment Management LLC                      Pacific Investment Management Co., LLC                      Wellington Trust Company</p> <p><b><u>Hedge Funds</u></b>                      Aristeia International Ltd                      Black Diamond / Carlson Capital GP                      Brevan Howard Asset Management LLP                      Cevian Capital L.P.                      D. E. Shaw &amp; Co.                      HBK Capital Management                      Indus Capital Partners, LLC                      Magnetar Capital LLC                      MentaGlobal Offshore Ltd                      MKP Capital Management, LLC                      Myriad Asset Management Ltd                      Och-Ziff Capital Management Group LLC                      River Birch International, Ltd.                      Systematica BlueTrend Fund Ltd                      York Capital Management</p> <p><b><u>Private Credit</u></b>                      Brookfield Real Estate Finance Fund                      Colony Capital                      TSSP Adjacent Opportunities Partners</p>

**LARGEST STOCK DIRECT HOLDINGS (FAIR VALUE)**

Shares	Stocks	Fair Value (\$)
39,456	Visa Inc.	5,225,947
44,911	SAP SE	5,194,406
71,975	Schlumberger Ltd.	4,824,484
542,539	AIA Group Ltd.	4,743,919
46,763	TJX Cos Inc.	4,450,902
220,302	Infosys Ltd.	4,280,468
9,586	Equinix Inc.	4,120,926
8,924	Fast Retailing Ltd.	4,101,664
51,208	Nike Inc.	4,080,253
31,099	Autodesk Inc.	4,076,768

**LARGEST BOND DIRECT HOLDINGS (FAIR VALUE)**

Par	Bonds	Fair Value (\$)
35,000,000	FNMA Single Family 3.5% 30 Yrs	34,791,610
34,880,000	U.S. Treasury 2.25% due 08-15-2027	33,197,319
32,500,000	U.S. Treasury 1.25% due 07-31-2023	30,200,885
27,800,000	FNMA Single Family 4% 30 Yrs	28,301,957
16,040,000	U.S. Treasury 3.75% due 11-15-2043	18,234,849
18,000,000	FNMA Single Family 3.5% 30 Yrs	17,915,328
11,000,000	FNMA Single Family 4.5% 30 Yrs	11,433,224
11,010,000	U.S. Treasury 2.75% due 08-15-2047	10,506,381
7,340,000	GNMA II Jumbos 4.5% 30 Yrs	7,629,079
45,200,000	Nykredit Realkredi 1% 01/10/2018	7,109,245

*A complete list of portfolio holdings is available upon request.*

(In thousands)

Asset Classes	2018	2017
Domestic Equity	\$ 909,836	\$ 788,828
International / Global Equity	806,215	737,122
Fixed Income	1,542,469	1,575,718
Real Estate	241,836	229,250
Hedge Funds	387,203	348,133
Private Credit	63,769	32,206
Private Equity	110,667	133,374
Commodities	175,300	155,853
<b>Investments at Fair Value</b>	<b>4,237,295</b>	<b>4,000,484</b>
Cash & Short-Term Investments	103,722	84,238
Investments Sold / Purchased	(165,708)	(132,693)
Investment Income & Other Liabilities	(25,010)	7,167
<b>Total Assets Under Management</b>	<b>4,150,299</b>	<b>3,959,196</b>
KCERA Capital Assets	3,180	3,805
KCERA Prepaid Expenses	25	68
KCERA Accruals	45,358	(174)
<b>Fiduciary Net Position</b>	<b>\$ 4,198,862</b>	<b>\$ 3,962,895</b>

Years Ended June 30, 2018 and 2017

Investment Manager Fees	2018	2017
<u>Domestic Equity</u>		
AllianceBernstein Trust Company	\$ 867,320	\$ 753,848
Henderson Geneva Capital Management	662,409	535,708
Mellon Capital Management (Dynamic US Equity)	889,697	905,348
Mellon Capital Management (US Equity)	34,983	51,189
Pacific Investment Management Company	274,745	463,869
PanAgora Asset Management	-	121,010
Sustainable Growth Advisors	632,114	80,017
T. Rowe Price Associates	-	281,006
Total Domestic Equity Managers	3,361,268	3,191,995
<u>International / Global Equity</u>		
BlackRock Institutional Trust Company	2,032,259	251,742
Dodge & Cox Funds	680,687	106,334
JP Morgan Investment Management	-	123,342
Pyramis Global Advisors (Large Cap)	-	463,770
Pyramis Global Advisors (Small Cap)	800,591	752,467
Total International Equity Managers	3,513,537	1,697,655
<u>Emerging Markets Managers</u>		
AllianceBernstein Trust Company	759,039	426,732
Dimensional Fund Advisors	376,345	270,842
Total Emerging Markets Managers	1,135,384	697,574
<u>High Yield Managers:</u>		
Western Asset Management Company	406,585	362,282
Total High Yield Managers	406,585	362,282
<u>Global Fixed Income</u>		
Gramercy Funds Management	582,967	553,667
Mellon Capital Management (Fixed Income)	117,984	80,059
Pacific Investment Management Company	556,533	361,621
Stone Harbor Investment Partners	468,396	435,369
TCW Securitized Opportunities	714,308	668,464
Western Asset Management Company	511,957	510,952
Total Global Fixed Income Managers	2,952,145	2,610,132
<u>Commodities</u>		
Gresham Investment Management	253,289	237,746
Pacific Investment Management Company	961,620	860,590
Wellington Trust Company	416,802	143,268
Total Commodity Managers	1,631,711	1,241,604

(Schedule of Investment Fees continued on next page)

Investment Manager Fees	2018	2017
<u>Real Estate</u>		
ASB Real Estate Investors	714,645	533,201
Long Wharf Real Estate Partners (FREG Fund III)	-	192,719
Invesco Real Estate (Fund III)	329,683	412,172
Invesco Real Estate (US Value-Add Fund IV)	1,250,204	323,741
J.P. Morgan Chase Banke (Strategic Property Fund)	825,041	763,503
Landmark Real Estate Partners VIII	927,717 *	-
Total Real Estate Managers	4,047,290	2,225,336
<u>Private Equity</u>		
Abbott Capital Management (Fund V)	289,636	321,816
Abbott Capital Management (Fund VI)	346,276	384,752
Pantheon Ventures, Inc. (Fund V)	61,625	80,742
Pantheon Ventures, Inc. (Fund VI)	157,624	174,380
Pantheon Ventures, Inc. (Fund VII)	320,762	354,863
Pantheon Ventures, Inc. (Secondary Fund III)	308,414	344,933
Total Private Equity Managers	1,484,337	1,661,486
<u>Hedge Funds</u>		
Aristeia International Ltd	479,319	178,071
Black Diamond Relative Value Partners	358,444	327,048
BlueTrend Fund	334,369	346,522
Brevan Howard Multi-Strategy Fund	664,962	856,786
Cevian Capital II SP	300,499	520,415
D.E. Shaw Composite Fund	1,924,243	845,780
HBK Multi-Strategy Fund	836,844	402,760
Indus Pacific Opportunities Fund	1,042,171	1,054,648
Magnetar Structured Credit Fund	690,601	633,332
MentaGlobal Offshore Ltd	345,632	357,164
MKP Opportunity Offshore Ltd	408,173	420,359
Myriad Opportunities Offshore Fund	1,115,002	1,165,066
OZ Domestic Partners II	1,033,599	1,316,827
River Birch International Ltd	335,229	318,243
York Capital Management	385,282	321,820
Total Hedge Fund Managers	10,254,369	9,064,841
<u>Private Credit</u>		
Brookfield Real Estate Finance Fund V	96,330	-
Colony Capital Credit IV, LLC	330,778	-
TSSP Adjacent Opportunities Partners	316,950	526,014
Total Private Credit Managers	744,058	526,014
<b>Total Investment Managers' Fees</b>	<b>\$29,530,684</b>	<b>\$23,278,919</b>

\*In fiscal year 2018, KCERA paid management fees from fund's initial closing date 12/15/2016; \$327,717 fees attributed to prior fiscal years.  
(Schedule of Investment Fees continued on next page)



Other Investment Expenses	2018	2017
<i>Custodial Fees</i>		
The Northern Trust Company	\$344,565	\$327,627
<i>Actuarial Fees</i>		
Segal Company	307,393	140,894
<i>Investment Consultant Fees</i>		
Albourne America LLC	590,000	416,855
Glass, Lewis & Co.	14,588	15,000
Verus	366,290	330,000
<i>Legal Fees</i>		
Foley & Lardner LLP	28,906	1,830
Hanson Bridgett LLP	0	15,900
Nossaman LLP	98,492	10,945
<i>Due Diligence Travel Expenses</i>		
Trustees / KCERA Management	1,561	36,001
<i>Security Lending Bank Fees</i>		
Deutsche Bank	84,256	55,521
<i>Real Estate Expenses</i>		
KCERA Property Inc.	39,445	34,579
<b>Total Other Investment Expenses</b>	<b>1,875,496</b>	<b>1,385,151</b>
<b>Total Investment Fees and Services</b>	<b>\$31,406,180</b>	<b>\$24,664,071</b>

# **ACTUARIAL**

## **Section**

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October 5, 2018

Board of Retirement  
Kern County Employees' Retirement Association  
11125 River Run Boulevard  
Bakersfield, CA 93311

**Re: Kern County Employees' Retirement Association  
June 30, 2017 Actuarial Valuation for Funding Purposes**

Dear Members of the Board:

Segal Consulting (Segal) prepared the June 30, 2017 annual actuarial valuation of the Kern County Employees' Retirement Association (KCERA). We certify that the valuation was performed in accordance with generally accepted actuarial principles and practices and KCERA's funding policy that was last reviewed with the Board in 2012. In particular, it is our understanding that the assumptions and methods used for funding purposes meet the parameters set by Actuarial Standards of Practice (ASOPs).

As part of the June 30, 2017 actuarial valuation, Segal conducted an examination of all participant data for reasonableness. However, the scope of this examination does not qualify as an audit. Summaries of the employee data used in performing the actuarial valuations over the past several years are provided in our valuation report. We did not audit the Association's financial statements. For actuarial valuation purposes, retirement plan assets are valued at Actuarial Value. Under this method, the assets used to determine employer contribution rates take into account market value by recognizing the differences between the total return at market value and the expected investment return over 10 six-month periods. The deferred return is further adjusted, if necessary, so that the actuarial value of assets will stay within 50% of the market value of assets.

One of the general goals of an actuarial valuation is to establish contribution rates, which, over time, will remain level as a percentage of payroll for each generation of active members. Actuarial funding is based on the Entry Age Cost Method. Under this method, the employer contribution rate provides for current cost (normal cost) plus a level percentage of payroll to amortize any unfunded actuarial accrued liability (UAAL).

The UAAL as of June 30, 2011 is amortized as a level percentage of payroll over a 18.5-year period as of June 30, 2017. Effective June 30, 2012, any changes in UAAL due to actuarial gains or losses or due to changes in actuarial assumptions or methods will be amortized over a 18-year closed period effective with each valuation. Any change in unfunded actuarial accrued liability

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Board of Retirement  
 Kern County Employees' Retirement Association  
 October 5, 2018  
 Page 2

that arises due to plan amendments is amortized over its own declining 15-year period (with exception of a change due to retirement incentives, which is amortized over a declining period of up to 5 years). The progress being made towards meeting the funding objective through June 30, 2017 is illustrated in the Schedule of Funding Progress.

A listing of supporting schedules Segal prepared for inclusion in the actuarial, statistical, and financial sections of the Association's CAFR is provided below. Unless otherwise stated, the schedules were prepared based on the results of the actuarial valuation as of June 30, 2017 for funding purposes. The notes to the financial section and Required Supplementary Information were prepared by the Association based on the results of the Governmental Accounting Standards (GAS) 67 actuarial valuation as of June 30, 2018 prepared by Segal.

- Exhibit I      Schedule of Active Member Valuation Data;
- Exhibit II     Retirees and Beneficiaries Added To and Removed From Retiree Payroll;
- Exhibit III    Solvency Test;
- Exhibit IV     Actuarial Analysis of Financial Experience; and
- Exhibit V      Schedule of Funding Progress.

The valuation assumptions included in the Actuarial Section were adopted by the Retirement Board based on our recommendations following the June 30, 2016 Actuarial Experience Study.

As we disclosed in our June 30, 2017 funding valuation report, the 7.25% investment return assumption that the Board approved for determining the liabilities for funding purposes and used for establishing the employer and employee contribution rates was developed without considering the impact of any future 50/50 excess earnings allocation. This is based on our understanding that Article 5.5 of the Statute, which authorizes the allocation of 50% of excess earnings to the SRBR, does not allow for the use of a different investment return for funding than is used for interest crediting. This would appear in effect to preclude the prefunding of the SRBR through the use of an assumption lower than the market earnings assumption of 7.25%.

As indicated by the guidance found in Actuarial Standard of Practice (ASOP) No. 4 ("Measuring Pension Obligations and Determining Pension Plan Costs or Contributions"), we performed stochastic modeling in 2015 to estimate the impact of the 50% allocation of future excess earnings to the SRBR. The results of our model indicated that the 50/50 allocation of future excess earnings would have about the same impact as an "outflow" (i.e., assets not available to fund the benefits included in the funding valuation) that would average approximately 0.3% of assets over time. **For informational purposes only**, when we applied the results of our stochastic model to this valuation, we estimated that such an annual outflow would increase the AAL measured in this valuation using a 7.25% investment return assumption from \$6.19 billion to \$6.42 billion (for a difference of \$232 million) and would increase the employer's contribution rate by about 4.2% of payroll.

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Board of Retirement  
Kern County Employees' Retirement Association  
October 5, 2018  
Page 3

It is our opinion that the assumptions used in the June 30, 2017 valuation produce results, which, in aggregate, reflect the future experience of the retirement plan. Actuarial valuations are performed on an annual basis. An experience analysis is performed every three years and was last performed as of June 30, 2016 with those assumptions first being implemented in the June 30, 2017 actuarial valuation.

In the June 30, 2017 valuation, the ratio of the valuation assets to actuarial accrued liabilities (funded percentage) decreased from 63.4% to 63.2%. The aggregate employer contribution rate has increased from 44.78% of payroll to 47.69% of payroll, while the aggregate employee rate has increased from 6.22% of payroll to 6.46% of payroll.

Under the asset smoothing method, the total unrecognized investment losses are \$74 million as of June 30, 2017. These investment losses will be recognized in the determination of the actuarial value of assets for funding purposes in the next few years.

The deferred losses of \$74 million represent about 2% of the market value of assets as of June 30, 2017. Unless offset by future investment gains or other favorable experience, the recognition of the \$74 million market losses is expected to have an impact on the Association's future funded percentage and contribution rate requirements. This potential impact may be illustrated as follows:

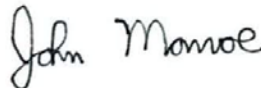
- If the deferred losses were recognized immediately in the valuation value of assets, the funded percentage would decrease from 63.2% to 62.0%.
- If the deferred losses were recognized immediately in the valuation value of assets, the aggregate employer rate would increase from 47.69% to 48.76% of payroll.

We are members of the American Academy of Actuaries and we meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion contained herein.

Sincerely,



Paul Angelo, FSA, MAAA, FCA, EA  
Senior Vice President and Actuary



John Monroe, ASA, MAAA, EA  
Vice President and Actuary

MYM/bbf  
Enclosures

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The methods and assumptions below were selected by the actuary as being appropriate for the Plan and were used in the latest actuarial valuation dated June 30, 2017. The most recently updated Summary of Actuarial Assumptions and Methods was adopted by the Board of Retirement on December 10, 2014.

**Economic Assumptions**

<i>Interest Rate of Return:</i>	7.25% per year, net of investment expenses
<i>Salary Increases:</i>	General: 4.00% to 9.00%. Safety: 4.00% to 12.50% (see Table 1 on page 86).
<i>Inflation Assumption:</i>	3.00% per year
<i>Cost-of-Living Adjustments:</i>	2.50% (actual increases depend on CPI increases; 2.50% maximum)

**Actuarial Methods**

<i>Funding Method:</i>	Entry Age Funding Method. Costs are allocated as a level percent of salary.
<i>Actuarial Cost Method:</i>	Entry Age Actuarial Cost Method. The actuarial present value of the projected benefits of each member are allocated as a level percentage of the member's projected compensation between entry age and assumed exit (until maximum retirement age).
<i>Amortization Period:</i>	<p>The actuarial present value of benefits expected to be paid in the future is the Normal Cost. The difference between the Normal Cost and the actuarial present value of all future benefits for contributing members, former contributing members and their survivors is the Actuarial Accrued Liability (AAL). The difference between the AAL and the actuarial value of the assets is the Unfunded Actuarial Accrued Liability (UAAL).</p> <p>As of June 30, 2017, the remaining amortization period for all UAAL as of June 30, 2011 was 18.5 years. Effective June 30, 2012, any changes in UAAL due to actuarial gains or losses or due to changes in actuarial assumptions or methods will be amortized over an 18-year closed period, effective with each valuation. Any change in UAAL that arises due to plan amendments is amortized over its own declining 15-year period (with the exception of a change due to retirement incentives, which are amortized over a declining period of up to 5 years).</p>

**Actuarial Methods (cont.)**

*Amortization Period (cont.):* Beginning July 1, 2009, any liability attributable to golden handshakes is paid by one of two methods, as elected by the employer:

1. Payment in full in the first month of the fiscal year following the fiscal year in which the golden handshake(s) was granted; or
2. According to a 5-year amortization to be invoiced to the employer in the first month of the fiscal year following the fiscal year in which the golden handshake(s) was granted. The amortization schedule will be based upon the valuation interest rate used in the most recently completed valuation at the time that the amortization schedule is created. The employer may complete payment of the golden handshake(s) at any time during the 5-year amortization period.

**Demographic Assumptions**

*Post-Retirement Mortality:*

- A) General Members and Safety Members: Combined RP-2014 Healthy Annuitant Mortality Table set forward one year for male and two years for female General Members and set back one year for male and female Safety members projected generationally with the two-dimensional MP-2016 projection scale.
- B) Beneficiaries: Rates are the same as a General service retiree of the opposite sex.
- C) Disability Retirement: Combined RP-2014 Healthy Annuitant Mortality Table set forward seven years for male and eight years for female General Members and set forward three years for male and female Safety Members projected generationally with the two-dimensional MP-2016 projection scale.

*Proportion of Members with Spouse/Partner at Retirement:* 75% of male active members and 55% of female active employees are assumed to have a spouse or registered domestic partner eligible for the 60% continuance at retirement. Females are assumed to be three years younger than their spouses.

*Rate of Termination of Employment:* Rates vary by years of service, as shown in Table 2 on page 87.

*Reciprocal Agency:* For current active members, the probability of joining a reciprocal agency immediately after terminating is 55% for General members and 60% for Safety members.

*Deferred Retirement Age for Vested Termination:* Age 57 for General members. Age 53 for Safety members.



Years of Service	General Members	Safety Members
0	5.50%	8.00%
1	4.00%	6.50%
2	3.50%	5.50%
3	3.00%	4.00%
4	2.25%	3.50%
5	2.00%	3.25%
6	1.75%	3.00%
7	1.50%	2.50%
8	1.25%	1.75%
9	1.00%	1.50%
10	0.90%	1.25%
11	0.80%	1.00%
12	0.70%	0.90%
13	0.60%	0.85%
14	0.50%	0.80%
15	0.50%	0.75%
16	0.50%	0.70%
17	0.50%	0.65%
18	0.50%	0.60%
19	0.50%	0.55%
20 & Over	0.50%	0.50%

*The chart above depicts annual increases in salary before wage inflation. Inflation is 3.00% per year, plus “across-the-board” salary increases of 0.50% per year, plus the promotional and merit increases listed above.*

(Rates in percentages)

Age Nearest	Ordinary Death	Disability*	Service Retirement		
<b>General Members - Male</b>			<i>Tier I</i>	<i>Tier II</i>	<i>Tier III</i>
25	0.04	0.03	0.00	0.00	0.00
30	0.05	0.05	0.00	0.00	0.00
40	0.11	0.14	0.00	0.00	0.00
50	0.23	0.28	6.00	3.00	0.00
60	0.64	0.38	23.00	13.50	13.50

**General Members - Female**      *Tier I*   *Tier II*   *Tier III*

25	0.02	0.03	0.00	0.00	0.00
30	0.03	0.05	0.00	0.00	0.00
40	0.07	0.14	0.00	0.00	0.00
50	0.17	0.28	6.00	3.00	0.00
60	0.45	0.38	23.00	13.50	13.50

**Safety Members - Male**      *Tier I*   *Tier II*

25	0.04	0.08	0.00	0.00
30	0.04	0.16	0.00	0.00
40	0.10	0.50	0.00	0.00
50	0.19	1.35	20.00	6.00
60	0.52	3.60	20.00	20.00

**Safety Members - Female**      *Tier I*   *Tier II*

25	0.02	0.08	0.00	0.00
30	0.02	0.16	0.00	0.00
40	0.06	0.50	0.00	0.00
50	0.14	1.35	20.00	6.00
60	0.36	3.60	20.00	20.00

(Rates in percentages)

Years of Service	Withdrawal	
	General	Safety
0	18.00	8.00
5	6.00	2.60
10	3.25	2.00
15	2.30	1.10
20	1.50	0.00
25	1.00	0.00
30 & Over	0.00	0.00

\* 55% of General member disabilities are assumed to be service-connected, and the other 45% are assumed to be nonservice-connected. Furthermore, 100% of Safety member disabilities are assumed to be service-connected.

Valuation Date	Plan Type	Members	Annual Payroll	Annual Average Pay	Increase in Average Pay
06/30/08	General	7,216	\$ 369,093,653	\$ 51,149	5.6%
	Safety	1,841	\$ 117,947,008	\$ 64,067	3.6%
	<b>Total</b>	<b>9,057</b>	<b>\$ 487,040,661</b>	<b>\$ 53,775</b>	<b>5.1%</b>
06/30/09*	General	7,166	\$ 423,075,334	\$ 59,039	15.4%
	Safety	1,854	\$ 141,829,138	\$ 76,499	19.4%
	<b>Total</b>	<b>9,020</b>	<b>\$ 564,904,472</b>	<b>\$ 62,628</b>	<b>16.5%</b>
06/30/10	General	6,802	\$ 423,551,766	\$ 62,269	5.5%
	Safety	1,765	\$ 141,008,072	\$ 79,891	4.4%
	<b>Total</b>	<b>8,567</b>	<b>\$ 564,559,838</b>	<b>\$ 65,899</b>	<b>5.2%</b>
06/30/11	General	6,487	\$ 404,729,012	\$ 62,391	0.2%
	Safety	1,700	\$ 135,105,643	\$ 79,474	-0.5%
	<b>Total</b>	<b>8,187</b>	<b>\$ 539,834,655</b>	<b>\$ 65,938</b>	<b>0.1%</b>
06/30/12	General	6,494	\$ 406,039,414	\$ 62,525	0.2%
	Safety	1,759	\$ 137,518,061	\$ 78,180	-1.6%
	<b>Total</b>	<b>8,253</b>	<b>\$ 543,557,475</b>	<b>\$ 65,862</b>	<b>-0.1%</b>
06/30/13	General	6,619	\$ 410,905,480	\$ 62,080	-0.7%
	Safety	1,866	\$ 144,847,330	\$ 77,625	-0.7%
	<b>Total</b>	<b>8,485</b>	<b>\$ 555,752,810</b>	<b>\$ 65,498</b>	<b>-0.6%</b>
06/30/14	General	6,629	\$ 410,350,884	\$ 61,902	-0.3%
	Safety	1,883	\$ 145,284,147	\$ 77,156	-0.6%
	<b>Total</b>	<b>8,512</b>	<b>\$ 555,635,031</b>	<b>\$ 65,277</b>	<b>-0.3%</b>
06/30/15	General	6,637	\$ 411,427,313	\$ 61,990	0.1%
	Safety	1,844	\$ 145,396,935	\$ 78,849	2.2%
	<b>Total</b>	<b>8,481</b>	<b>\$ 556,824,248</b>	<b>\$ 65,655</b>	<b>0.6%</b>
06/30/16	General	6,788	\$ 421,043,714	\$ 62,028	0.1%
	Safety	1,839	\$ 146,217,425	\$ 79,509	0.8%
	<b>Total</b>	<b>8,627</b>	<b>\$ 567,261,139</b>	<b>\$ 65,754</b>	<b>0.2%</b>
06/30/17	General	6,966	\$ 431,532,274	\$ 61,948	-0.1%
	Safety	1,762	\$ 140,549,312	\$ 79,767	0.3%
	<b>Total</b>	<b>8,728</b>	<b>\$ 572,081,586</b>	<b>\$ 65,546</b>	<b>-0.3%</b>

\* Annual payroll data as of June 30, 2009 includes supplemental pay items with pensionable salary.

Plan Year	At Beginning of Year	Added During Year	Removed During Year	At End of Year	Annual Allowance Added	Annual Allowance Removed	Retiree Payroll Ending	% Increase in Retiree Allowance	Average Annual Allowance*
2008	5,552	196	97	5,651	\$ 5,039,591	\$1,610,546	\$145,783,557	4.8%	\$25,798
2009	5,651	458	182	5,927	\$16,056,013	\$2,751,455	\$164,591,026	12.9%	\$27,770
2010	5,927	476	204	6,199	\$13,128,260	\$3,658,618	\$181,377,904	10.2%	\$29,259
2011	6,199	569	198	6,570	\$27,159,926	\$3,568,064	\$204,969,766	13.0%	\$31,198
2012	6,570	499	179	6,890	\$24,783,041	\$3,411,092	\$226,341,715	10.4%	\$32,851
2013	6,890	468	187	7,171	\$22,305,618	\$3,825,313	\$244,822,020	8.2%	\$34,141
2014	7,171	442	216	7,397	\$19,663,621	\$4,173,211	\$260,312,430	3.1%	\$35,192
2015	7,397	440	238	7,599	\$20,734,025	\$5,817,539	\$275,229,096	5.7%	\$36,219
2016	7,599	454	206	7,847	\$20,236,339	\$5,034,075	\$290,431,360	5.5%	\$37,012
2017	7,847	501	255	8,093	\$22,566,737	\$6,358,810	\$306,639,287	5.6%	\$37,889

\* Excludes SRBR amounts

(Dollars in thousands)

Valuation Date	Aggregate Accrued Liabilities				Portion of Accrued Liabilities Covered by Reported Assets			
	Active Member Contributions	Retired/Vested Members	Active Members (Employer Financed Portion)	Total	Actuarial Value of Assets	Active Member Contributions	Retired/Vested Members	Active Members (Employer Financed Portion)
06/30/08	\$ 222,418	\$ 1,913,946	\$ 1,535,096	\$ 3,671,460	\$ 2,654,316	100%	100%	34%
06/30/09	\$ 232,426	\$ 2,159,371	\$ 1,813,403	\$ 4,205,200	\$ 2,780,215	100%	100%	21%
06/30/10	\$ 229,784	\$ 2,380,826	\$ 1,846,429	\$ 4,457,038	\$ 2,794,644	100%	100%	10%
06/30/11	\$ 225,649	\$ 2,680,161	\$ 1,766,538	\$ 4,672,348	\$ 2,839,747	100%	98%	0%
06/30/12	\$ 231,626	\$ 2,933,987	\$ 1,729,377	\$ 4,894,990	\$ 2,960,507	100%	93%	0%
06/30/13	\$ 244,832	\$ 3,153,966	\$ 1,709,821	\$ 5,108,619	\$ 3,120,632	100%	91%	0%
06/30/14	\$ 268,826	\$ 3,446,962	\$ 1,776,652	\$ 5,492,440	\$ 3,342,122	100%	89%	0%
06/30/15	\$ 295,447	\$ 3,607,511	\$ 1,754,215	\$ 5,657,173	\$ 3,529,786	100%	90%	0%
06/30/16	\$ 320,400	\$ 3,766,875	\$ 1,725,817	\$ 5,813,092	\$ 3,685,447	100%	89%	0%
06/30/17	\$ 351,592	\$ 4,093,826	\$ 1,746,015	\$ 6,191,433	\$ 3,913,073	100%	87%	0%

(In thousands)

	<b>Gain (or Loss) for Year – UAAL</b>		
	<b><u>June 30, 2017</u></b>	<b><u>June 30, 2016</u></b>	<b><u>June 30, 2015</u></b>
Investment Performance			
Greater (Less) than Expected	\$ (17,692)	\$ (87,833)	\$ (34,742)
Salary Increase			
(Greater) Less than Expected	50,071	50,037	55,020
Other Experience			
Including Demographic Changes	26,780	39,692	9,908
Change in Assumptions/Methodology	(213,476)	-	-
<b>Composite Gain (or Loss) During Year</b>	<b>\$ (154,317)</b>	<b>\$ 1,896</b>	<b>\$ 30,186</b>

**SCHEDULE OF FUNDING PROGRESS\***

(Dollars in thousands)

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability	Unfunded Actuarial Accrued Liability (UAAL) (3) - (2)	Funded Ratio (2) / (3)	Annual Covered Payroll	UAAL as % of Annual Payroll (4) / (6)
(1)	(2)	(3)	(4)	(5)	(6)	(7)
6/30/2008	\$ 2,654,305	\$ 3,671,460	\$ 1,017,155	72.3%	\$ 482,879	210.6%
6/30/2009	\$ 2,780,215	\$ 4,205,200	\$ 1,424,985	66.1%	\$ 559,872	254.5%
6/30/2010	\$ 2,794,644	\$ 4,457,038	\$ 1,662,394	62.7%	\$ 559,380	297.2%
6/30/2011	\$ 2,839,747	\$ 4,672,348	\$ 1,832,601	60.8%	\$ 539,836	339.5%
6/30/2012	\$ 2,960,507	\$ 4,894,990	\$ 1,934,483	60.5%	\$ 543,558	355.9%
6/30/2013	\$ 3,120,632	\$ 5,108,619	\$ 1,987,987	61.1%	\$ 555,752	357.7%
6/30/2014	\$ 3,342,122	\$ 5,492,440	\$ 2,150,318	60.8%	\$ 555,634	387.0%
6/30/2015	\$ 3,529,786	\$ 5,657,173	\$ 2,127,387	62.4%	\$ 556,824	382.1%
6/30/2016	\$ 3,685,447	\$ 5,813,092	\$ 2,127,645	63.4%	\$ 567,261	375.1%
6/30/2017	\$ 3,913,073	\$ 6,191,433	\$ 2,278,360	63.2%	\$ 572,081	398.3%

\* Net of SRBR and \$5,000 death benefits

**SCHEDULE OF EMPLOYER CONTRIBUTIONS**

(Dollars in thousands)

Fiscal Year Ended June 30,	Annual Required Contributions	Percentage Contributed
2008	\$ 137,264	100%
2009	\$ 138,815	100%
2010	\$ 151,127	100%
2011	\$ 177,444	100%
2012	\$ 189,837	100%
2013	\$ 211,677	100%
2014	\$ 220,393	100%
2015	\$ 215,477	100%
2016	\$ 234,714	100%
2017	\$ 224,351	100%

Briefly summarized below are the major provisions of the County Employees' Retirement Law of 1937, including Sections 31676.01, 31676.14, 31676.17, 31664, 31664.1 and 7522.20(a), as adopted by the County of Kern and special districts.

### **Membership**

Membership is automatic upon appointment to a permanent position of 50% or more of the regular standard hours required. Retirement entry date is the first day of the first full biweekly payroll period following the date of employment.

All safety and general members hired by the County of Kern or a special district on or after January 1, 2013 are subject to the "new member" provisions found in Code Section 7522.20(a) of the Public Employees' Pension Reform Act of 2013 (PEPRA).

### **Final Average Salary**

For non-PEPRA benefit tiers, "final average salary" is the highest 12 consecutive months of pensionable pay, including base salary and other pay elements includible as a result of the "Ventura" decision. "Pensionable compensation" for members subject to PEPRA is the highest 36 consecutive months of pensionable pay, including base salary and eligible special pay items defined in PEPRA.

### **Vesting**

Members are considered vested in the Plan after obtaining five years of retirement service credit.

### **Member Contribution Rates**

The basic contribution is computed on the member's base pay plus pensionable special pays, with the contribution rate being determined by the member's entry age into KCERA, the classification of the member, the Plan's economic assumptions and the member's life expectancy at the retirement age specified in the County Employees' Retirement Law of 1937.

The normal rates of contribution are such as to provide, for each year of service, an average annuity at age 55 of 1.0% of final compensation

for General Tier I members, an average annuity at age 60 of 0.833% of final compensation for General Tier II members, an average annuity at age 50 of 1.5% of final compensation for Safety Tier I members, and an average annuity at age 50 of 1.0% of final compensation for Safety Tier II members, according to the tables adopted by the Board of Supervisors, for each year of service rendered after entering the Plan.

General and safety members subject to PEPRA provisions will pay 100% of their contributions until retirement. Their contribution rates will be 50% of the actuarially determined Normal Cost rate for each membership group. All other KCERA members will contribute based on their entry age or a flat average rate (i.e., for certain safety bargaining units).

Per IRS Code Section 414(h)(2), member contributions made through payroll deductions are pretax. Interest is credited to contribution balances on June 30 and December 31, per the County Employees' Retirement Law of 1937, Article 5.5.

### **Withdrawal Benefits**

If a member resigns, his or her contributions plus interest can be refunded. Members with less than five years of service may elect to leave his or her contributions on deposit and receive interest. Any vested member may elect to leave his or her contributions on deposit and receive a deferred-vested benefit when eligible for retirement.

### **Compensation Limit**

For members who joined KCERA on or after July 1, 1996 but before January 1, 2013, "compensation earnable" is limited by IRC Section 401(a)(17) and indexed annually for inflation. "Pensionable compensation" for General Tier III members enrolled in Social Security is capped at the Social Security limit and indexed annually for inflation.

### **Service Retirement Benefits**

General members with at least 10 years of retirement service credit who are age 50 or older, have 30 years of service credit regardless of age, or are age 70 regardless of service credit are eligible for service retirement.



**Service Retirement Benefits (cont.)**

General Tier I provides 3.0% of final compensation for each year of service at age 60, multiplied by Government Code Section 31676.17 factors. General Tier II provides 1.62% of final compensation for each year of service at age 65, multiplied by Government Code Section 31676.01 factors.

Berrenda Mesa Water District and Inyokern Community Services District still have Government Code Section 31676.14 for service prior to January 1, 2005.

General Tier II applies to most general members hired by the County of Kern and Kern County Hospital Authority on or after October 27, 2007, or hired by the following special districts: Berrenda Mesa Water District on or after January 12, 2010; Buttonwillow Recreation and Park District and East Kern Cemetery District on or after December 17, 2012; Inyokern Community Services District on or after December 13, 2012; Kern County Water Agency on or after January 1, 2010; Kern Mosquito and Vector Control District on or after December 12, 2012; North of the River Sanitation District on or after October 29, 2007; San Joaquin Valley Air Pollution Control District on or after July 31, 2012; Shafter Recreation and Park District on or after December 19, 2012; West Side Cemetery District on or after December 18, 2012; WestSide Mosquito and Vector Control District on or after November 15, 2012; and Kern County Superior Court on or after March 12, 2011.

General members hired by the West Side Recreation and Park District on or after January 1, 2013 are General Tier III members. Their benefit formula is 2.5% at age 67. They are eligible to retire at age 52 with 5 years of retirement service credit.

Safety members with at least 10 years of retirement service credit who are age 50 or older, or with 20 years of retirement service credit regardless of age, are eligible for service retirement.

Safety Tier I provides 3.0% of final compensation for each year of service at age 50, multiplied by

Government Code Section 31664.1 factors. Safety Tier II provides 2.0% of final compensation for each year of service at age 50, multiplied by Government Code Section 31664 factors.

For members integrated with Social Security, benefits based on \$350 of monthly final average salary are reduced by one-third.

**Disability Benefit**

Members with five years of retirement service credit, regardless of age, are eligible for nonservice-connected disability. This benefit provide 20% to 40% of the member’s final average monthly compensation for life.

If the disability is service-connected, there is no minimum retirement service credit requirement. This benefit provides 50% of the member’s final average monthly compensation, tax-free, for life.

**Death Benefit (Before Retirement)**

A non-vested active member’s beneficiary is entitled to receive the Basic Death Benefit, which consists of accumulated contributions plus interest and one month of salary for each full year of service, up to six months of salary.

The beneficiary (i.e., eligible spouse or registered domestic partner) of a vested active member who does *not* die in the performance of duty is entitled to either the Basic Death Benefit or a monthly benefit equal to 60% of the benefit payable if the member had retired with a nonservice-connected disability on his or her date of death. This also applies to minor children if there is no eligible spouse or partner.

If a member dies in the performance of duty, the eligible spouse, partner or minor children receives 50% of the member’s final averagesalary.

**Death Benefit (After Retirement)**

A death benefit of \$5,000 is payable to the designated beneficiary or estate of a retiree after the member dies.

**Death Benefit (After Retirement) (cont.)**

If a member retired for service or with a non-service-connected disability and he or she chose the Unmodified Option, the eligible surviving spouse, registered domestic partner or minor children will receive a benefit equal to 60% of the member's retirement benefit. If the retirement was for a service-connected disability, the member's spouse, registered domestic partner or minor children will receive a 100% continuance of the benefit.

**Supplemental Retirement Benefits (SRBR)**

The Board of Retirement adopted California Government Code Section 31618 on April 23, 1984,

which provided for the establishment of the Supplemental Retiree Benefit Reserve (SRBR). The SRBR may be used only for the benefit of retired members and their beneficiaries. The distribution of the SRBR shall be determined by the Board of Retirement. SRBR-approved benefits include all Tier 1, Tier 2, Tier 3 and death benefits approved through the June 30, 2016 Actuarial Valuation.

**Post-Retirement Cost-of-Living Benefits**

Each April 1, retiree benefits are adjusted by the percentage change in the Consumer Price Index for the preceding calendar year (capped at 2.5%).

<b>Eligibility</b>	Tier 1:	Hired on or before July 1, 1994.
	Tier 2:	Pensioners with at least five years of credited service and who retired prior to 1981 or 1985 (and their surviving beneficiaries) whose benefits have reduced by 20% in purchasing power since retirement.
	Tier 3:	Pensioners and their surviving beneficiaries whose benefits have reduced by 20% in purchasing power since retirement.
<b>Benefits</b>	Tier 1:	\$35.50 per month, not subject to cost-of-living adjustments.
	Tier 2:	\$1.372 times years of service, per month, for members who retired prior to 1985; granted July 1, 1994. \$5.470 times years of service, per month, for members who retired prior to 1985; granted July 1, 1996. \$10.276 times years of service, per month, for members who retired prior to 1981; granted July 1, 1997.
	Tier 3:	Additional benefits to maintain 80% purchasing power protection.
	Death Benefit:	A one-time payment of \$5,000 to a retired member's beneficiary.
	0.5% COLA	\$64.7 million allocation of funds to initially pay for a 0.5% cost-of-living allowance; arisen from a litigation judgment entered on January 24, 2002.
	<b>Funding</b>	Crediting of interest and the allocation of "undistributed earnings": the amount that remains after net earnings have been used to credit interest to the Plan's reserves.

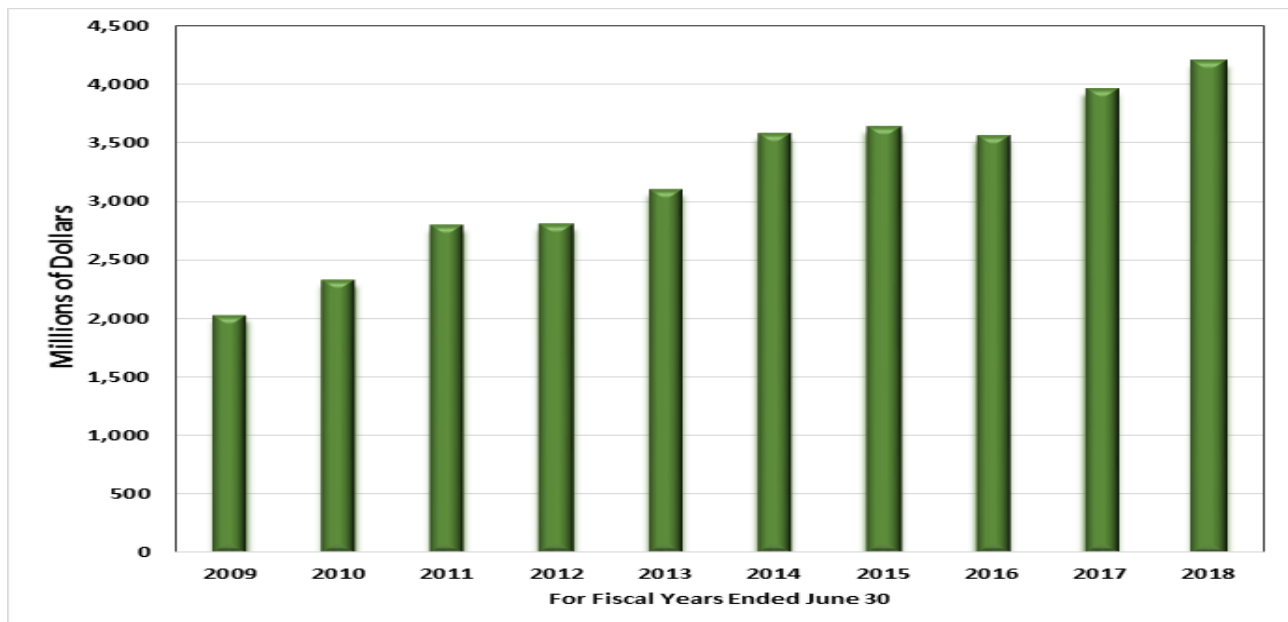
# STATISTICAL Section

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The Statistical Section offers additional historical perspective and detail to provide a fuller understanding of this year’s financial statements, note disclosures and supplementary information. This section also provides 10-year trending of financial and operating information to supply a more comprehensive perspective on how KCERA’s

financial position and performance have changed over time. Specifically, the financial and operating information provides contextual data for KCERA’s changes in net position, benefit expenses, retirement types, benefit payments and membership data. The financial and operating trend information is located on the following pages.

### KCERA NET POSITION VALUE FOR THE FISCAL YEARS ENDED JUNE 30



(In thousands)

	2009	2010	2011	2012	2013
<b>Additions</b>					
Employer Contributions	\$ 138,815	\$ 151,127	\$ 177,444	\$ 189,837	\$ 211,677
Member Contributions	18,191	17,877	18,271	18,720	20,283
Net Investment Income (Loss)	<u>(677,336)</u>	<u>291,333</u>	<u>503,553</u>	<u>21,150</u>	<u>319,264</u>
<b>Total Additions</b>	<b>(520,330)</b>	<b>460,337</b>	<b>699,268</b>	<b>229,707</b>	<b>551,224</b>
<b>Deductions</b>					
Total Benefit Expenses*	162,489	180,366	201,013	222,140	242,630
Administrative Expenses	3,072	3,207	3,763	3,469	3,848
Miscellaneous	<u>-</u>	<u>547</u>	<u>-</u>	<u>-</u>	<u>-</u>
<b>Total Deductions</b>	<b>165,561</b>	<b>184,120</b>	<b>204,776</b>	<b>225,609</b>	<b>246,478</b>
<b>Change in Fiduciary Net Position</b>	<b>\$ (685,891)</b>	<b>\$ 276,217</b>	<b>\$ 494,492</b>	<b>\$ 4,098</b>	<b>\$ 304,746</b>

(In thousands)

	2014	2015	2016	2017	2018
<b>Additions</b>					
Employer Contributions*	\$ 220,393	\$ 215,477	\$ 234,714	\$ 224,351	\$ 242,534
Member Contributions*	25,810	30,325	33,278	51,410	52,503
Net Investment Income (Loss)	<u>487,494</u>	<u>81,930</u>	<u>(27,535)</u>	<u>426,607</u>	<u>267,659</u>
<b>Total Additions</b>	<b>733,697</b>	<b>327,732</b>	<b>240,457</b>	<b>702,368</b>	<b>562,696</b>
<b>Deductions</b>					
Total Benefit Expenses**	257,495	273,865	288,738	305,817	321,613
Administrative Expenses	4,860	4,886	5,225	5,243	5,116
Miscellaneous	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
<b>Total Deductions</b>	<b>262,355</b>	<b>278,751</b>	<b>293,963</b>	<b>311,060</b>	<b>326,729</b>
<b>Change in Fiduciary Net Position</b>	<b>\$ 471,342</b>	<b>\$ 48,981</b>	<b>\$ (53,506)</b>	<b>\$ 391,308</b>	<b>\$ 235,967</b>

\* The current fiscal year's financial statements reclassified employer paid member contributions as member contributions.

\*\* See Schedule of Benefit Expenses by Type on next page.

(In thousands)

	2009	2010	2011	2012	2013
<i>Service Retirement Benefits</i>					
General	\$ 79,546	\$ 89,204	\$ 101,934	\$ 114,742	\$ 127,139
Safety	<u>43,311</u>	<u>49,949</u>	<u>55,886</u>	<u>62,207</u>	<u>68,078</u>
Total	122,857	139,153	157,820	176,949	195,217
<i>Service-Connected Disability (SCD) Benefits</i>					
General	7,720	7,906	7,924	7,947	8,064
Safety	<u>13,545</u>	<u>14,230</u>	<u>14,656</u>	<u>15,145</u>	<u>15,495</u>
Total	21,265	22,136	22,580	23,092	23,559
<i>Beneficiary Benefits</i>					
General	8,573	9,072	9,533	10,353	11,152
Safety	<u>6,525</u>	<u>7,222</u>	<u>7,580</u>	<u>8,231</u>	<u>8,602</u>
Total	15,098	16,294	17,113	18,584	19,754
<i>Lump Sum Death Benefits</i>	640	466	383	433	606
<b>Total Benefit Payments</b>	<b>\$ 159,860</b>	<b>\$ 159,860</b>	<b>\$ 197,896</b>	<b>\$ 219,058</b>	<b>\$ 239,136</b>
<i>Refunds</i>					
General	2,270	1,998	2,666	2,408	2,973
Safety	<u>359</u>	<u>319</u>	<u>451</u>	<u>674</u>	<u>521</u>
Total	2,629	2,317	3,117	3,082	3,494
<b>Total Benefit Expenses</b>	<b>\$ 162,489</b>	<b>\$ 180,366</b>	<b>\$ 201,013</b>	<b>\$ 222,140</b>	<b>\$ 242,630</b>

(In thousands)

	2014	2015	2016	2017	2018
<i>Service Retirement Benefits</i>					
General	\$ 137,993	\$ 148,697	\$ 159,101	\$ 169,370	\$ 179,977
Safety	<u>68,705</u>	<u>72,097</u>	<u>74,978</u>	<u>78,453</u>	<u>81,806</u>
Total	206,698	220,794	234,079	247,823	261,783
<i>Service-Connected Disability (SCD) Benefits</i>					
General	8,331	8,422	8,260	8,411	8,647
Safety	<u>20,565</u>	<u>21,222</u>	<u>21,676</u>	<u>22,207</u>	<u>22,842</u>
Total	28,896	29,644	29,936	30,618	31,489
<i>Beneficiary Benefits</i>					
General	10,660	11,186	12,261	13,579	14,136
Safety	<u>7,565</u>	<u>7,881</u>	<u>8,393</u>	<u>8,979</u>	<u>9,612</u>
Total	18,225	19,067	20,654	22,558	23,748
<i>Lump Sum Death Benefits</i>	564	862	787	894	903
<b>Total Benefit Payments</b>	<b>\$ 254,383</b>	<b>\$ 270,367</b>	<b>\$ 285,456</b>	<b>\$ 301,893</b>	<b>\$ 317,923</b>
<i>Refunds</i>					
General	2,762	2,876	2,563	2,718	2,966
Safety	<u>350</u>	<u>622</u>	<u>719</u>	<u>1,206</u>	<u>724</u>
Total	3,112	3,498	3,282	3,924	3,690
<b>Total Benefit Expenses</b>	<b>\$ 257,495</b>	<b>\$ 273,865</b>	<b>\$ 288,738</b>	<b>\$ 305,817</b>	<b>\$ 321,613</b>



Amount of Monthly Benefit	Number of Retirants	Type of Retirement								
		1	2	3	4	5	6	7	8	9
\$1-500	409	285	2	0	0	63	11	0	2	46
\$501-1,000	924	626	35	1	0	164	19	3	23	53
\$1,001-1,500	1,018	693	79	52	0	126	25	0	13	30
\$1,501-2,000	902	613	37	106	0	84	16	0	19	27
\$2,001-3,000	1,615	1,094	17	245	0	153	7	3	62	34
\$3,001-4,000	1,045	769	7	147	0	82	2	5	21	12
\$4,001-5,000	637	556	1	38	0	29	2	0	8	3
\$5,001-6,000	463	404	3	29	0	22	1	0	4	0
Over \$6,000	1,283	1,131	7	115	0	15	1	0	13	1
<b>Totals</b>	<b>8,296</b>	<b>6,171</b>	<b>188</b>	<b>733</b>	<b>0</b>	<b>738</b>	<b>84</b>	<b>11</b>	<b>165</b>	<b>206</b>

Amount of Monthly Benefit	Number of Retirants	Option Selected						
		Option 1	Option 2	Option 3	Option 4	Unmodified		
						A	B	C
\$1-500	409	13	30	1	0	123	0	242
\$501-1,000	924	7	61	2	0	320	1	533
\$1,001-1,500	1,018	6	52	5	1	377	20	557
\$1,501-2,000	902	7	41	3	0	325	68	458
\$2,001-3,000	1,615	12	61	9	3	592	170	768
\$3,001-4,000	1,045	6	44	3	0	438	106	448
\$4,001-5,000	637	3	32	3	3	345	28	222
\$5,001-6,000	463	1	21	2	2	280	24	131
Over \$6,000	1,283	2	50	3	2	894	105	227
<b>Totals</b>	<b>8,296</b>	<b>57</b>	<b>392</b>	<b>31</b>	<b>11</b>	<b>3,694</b>	<b>522</b>	<b>3,586</b>

**Type of Retirement**

- 1 – Normal retirement for age and service
- 2 – Nonservice-connected disability retirement
- 3 – Service-connected disability retirement
- 4 – Former member with deferred future benefit
- 5 – Beneficiary payment – normal retirement
- 6 – Beneficiary payment – active member who died and was eligible for retirement
- 7 – Beneficiary payment – death in service
- 8 – Beneficiary payment – disability retirement
- 9 – Supplemental and ex-spouses

**Option Selected**

- Option 1** – Beneficiary receives lump sum of member’s unused contributions
- Option 2** – Beneficiary receives 100% of member’s reduced monthly allowance
- Option 3** – Beneficiary receives 50% of member’s reduced monthly allowance
- Option 4** – More than one beneficiary receives 100% of member’s reduced monthly allowance
- A** – Unmodified 60% continuance
- B** – Unmodified no continuance
- C** – Unmodified 100% continuance

Fiscal Years Ended June 30, 2009 – 2013

	Years of Retirement Service Credit						
	0-5	5-10	10-15	15-20	20-25	25-30	30+
<b><i>Fiscal Year 2009</i></b>							
Average Annual Benefit (\$)	6,723	13,251	23,257	30,811	52,087	64,022	94,989
Average Monthly Benefit (\$)	560	1,104	1,939	2,568	4,341	5,335	7,916
Average Final Monthly Salary (\$)	10,183	4,254	5,022	4,655	6,200	6,079	7,329
Number of Active Retirants	11	34	52	44	37	67	91
<b><i>Fiscal Year 2010</i></b>							
Average Annual Benefit (\$)	9,845	18,365	21,268	36,183	45,074	64,316	90,915
Average Monthly Benefit (\$)	820	1,530	1,772	3,015	3,756	5,360	7,576
Average Final Monthly Salary (\$)	7,264	5,601	4,722	5,569	5,405	6,311	7,268
Number of Active Retirants	14	31	68	45	60	80	52
<b><i>Fiscal Year 2011</i></b>							
Average Annual Benefit (\$)	9,326	13,830	25,010	36,390	44,473	62,648	88,002
Average Monthly Benefit (\$)	777	1,152	2,084	3,032	3,706	5,221	7,334
Average Final Monthly Salary (\$)	5,755	5,031	5,577	5,684	5,468	6,063	7,120
Number of Active Retirants	10	50	72	51	94	96	99
<b><i>Fiscal Year 2012</i></b>							
Average Annual Benefit (\$)	8,182	15,037	20,599	34,635	46,509	68,852	86,890
Average Monthly Benefit (\$)	682	1,253	1,717	2,886	3,876	5,738	7,241
Average Final Monthly Salary (\$)	7,079	5,620	4,682	5,603	5,685	6,626	7,035
Number of Active Retirants	13	32	80	47	69	90	78
<b><i>Fiscal Year 2013</i></b>							
Average Annual Benefit (\$)	9,121	16,908	21,948	32,303	45,408	63,765	78,584
Average Monthly Benefit (\$)	760	1,409	1,829	2,692	3,784	5,314	6,549
Average Final Monthly Salary (\$)	7,851	5,485	4,951	5,420	5,659	6,332	6,543
Number of Active Retirants	17	31	80	57	67	63	75

Fiscal Years Ended June 30, 2014 – 2018

	Years of Retirement Service Credit						
	0-5	5-10	10-15	15-20	20-25	25-30	30+
<b>Fiscal Year 2014</b>							
Average Annual Benefit (\$)	9,215	13,410	21,177	32,740	44,637	70,218	86,650
Average Monthly Benefit (\$)	768	1,117	1,765	2,728	3,720	5,851	7,221
Average Final Monthly Salary (\$)	9,447	5,590	5,082	5,403	5,829	6,988	7,301
Number of Active Retirants	16	27	67	41	49	68	46
<b>Fiscal Year 2015</b>							
Average Annual Benefit (\$)	4,559	14,428	23,357	35,953	43,234	60,235	89,828
Average Monthly Benefit (\$)	380	1,202	1,946	2,996	3,603	5,020	7,486
Average Final Monthly Salary (\$)	5,732	5,444	5,236	5,805	5,395	6,350	7,493
Number of Active Retirants	6	44	74	40	42	75	54
<b>Fiscal Year 2016</b>							
Average Annual Benefit (\$)	6,508	14,308	24,278	32,909	45,685	64,833	78,159
Average Monthly Benefit (\$)	542	1,192	2,023	2,742	3,807	5,403	6,513
Average Final Monthly Salary (\$)	7,213	5,417	5,828	5,614	5,958	6,747	7,062
Number of Active Retirants	23	43	70	44	47	78	55
<b>Fiscal Year 2017</b>							
Average Annual Benefit (\$)	7,349	14,633	24,354	36,971	49,048	63,608	84,147
Average Monthly Benefit (\$)	612	1,219	2,029	3,081	4,087	5,301	7,012
Average Final Monthly Salary (\$)	8,677	5,941	5,921	6,001	6,427	6,558	7,230
Number of Active Retirants	17	46	76	65	68	60	55
<b>Fiscal Year 2018</b>							
Average Annual Benefit (\$)	6,440	12,906	20,699	33,844	54,312	60,419	84,403
Average Monthly Benefit (\$)	537	1,076	1,725	2,820	4,526	5,035	7,034
Average Final Monthly Salary (\$)	8,446	6,155	5,588	5,750	7,332	6,635	7,331
Number of Active Retirants	13	46	59	54	56	53	40

	2009	2010	2011	2012	2013
<i>County of Kern:</i>					
General Members	6,254	5,920	5,622	5,632	5,873
Safety Members	<u>1,854</u>	<u>1,765</u>	<u>1,703</u>	<u>1,762</u>	<u>1,873</u>
Total	8,108	7,685	7,325	7,394	7,746
<i>Participating Agencies (General Membership):</i>					
Berrenda Mesa Water District	12	11	10	10	10
Buttonwillow Recreation and Park District	4	5	6	6	6
East Kern Cemetery District	1	1	1	1	1
Inyokern Community Services District	2	2	1	1	1
Kern County Water Agency	76	72	73	71	65
Kern Mosquito & Vector Control District	19	19	18	19	18
North of the River Sanitation District	9	10	10	11	13
San Joaquin Valley Air Pollution Control District	291	292	287	281	281
Shafter Recreation and Park District	-	-	-	-	-
West Side Cemetery District	6	6	6	6	6
West Side Mosquito & Vector Control Dist.	8	8	8	7	7
West Side Recreation and Park District	12	12	10	10	10
Kern County Superior Court	<u>472</u>	<u>444</u>	<u>441</u>	<u>443</u>	<u>353</u>
Total	912	882	871	866	771
<b>Total Active Membership:</b>					
General Members	7,166	6,802	6,493	6,498	6,644
Safety Members	1,854	1,765	1,703	1,762	1,873
<b>Total</b>	<b>9,020</b>	<b>8,567</b>	<b>8,196</b>	<b>8,260</b>	<b>8,517</b>

Data retrieved from the Plan's database.

	2014	2015	2016	2017	2018
<i>County of Kern:</i>					
General Members	5,833	5,827	5,937	4,720	4,818
Safety Members	<u>1,886</u>	<u>1,847</u>	<u>1,840</u>	<u>1,767</u>	<u>1,771</u>
Total	7,719	7,674	7,777	6,487	6,589
<i>Participating Agencies (General Membership):</i>					
Berrenda Mesa Water District	10	9	6	6	4
Buttonwillow Recreation and Park District	4	4	4	3	2
East Kern Cemetery District	1	1	2	2	2
Inyokern Community Services District	1	1	1	-	-
Kern County Hospital Authority	-	-	-	1,374	1,446
Kern County Water Agency	68	67	62	60	59
Kern Mosquito & Vector Control District	18	18	18	18	19
North of the River Sanitation District	12	13	13	13	18
San Joaquin Valley Air Pollution Control District	276	264	269	273	275
Shafter Recreation and Park District	-	-	-	1	3
West Side Cemetery District	6	6	6	6	6
West Side Mosquito & Vector Control Dist.	10	10	9	8	8
West Side Recreation and Park District	11	11	11	9	8
Kern County Superior Court	<u>389</u>	<u>414</u>	<u>457</u>	<u>478</u>	<u>483</u>
Total	806	818	858	2,251	2,333
Total General Members	6,639	6,645	6,795	6,971	7,151
Total Safety Members	1,886	1,847	1,840	1,767	1,771
<b>Total Active Membership</b>	<b>8,525</b>	<b>8,492</b>	<b>8,635</b>	<b>8,738</b>	<b>8,922</b>

*Note: The Kern County Hospital Authority came into existence at the start of FY 2016-17 (July 1, 2016).*

*Data retrieved from the Plan's database.*



**KERN COUNTY**  
EMPLOYEES'  
RETIREMENT  
ASSOCIATION