MARIN COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

FINANCIAL STATEMENTS WITH INDEPENDENT AUDITOR'S REPORT

FOR THE FISCAL YEARS ENDED JUNE 30, 2011 AND 2010

MARIN COUNTY EMPLOYEES'
RETIREMENT ASSOCIATION
JUNE 30, 2011 AND 2010

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BROWN ARMSTRONG
Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT

Board of Retirement
Marin County Employees' Retirement Association
San Rafael, California

We have audited the accompanying statements of plan net assets of the Marin County Employees' Retirement Association (MCERA) as of June 30, 2011 and 2010, and the related statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of management of MCERA. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of the MCERA as of June 30, 2011 and 2010, and its changes in plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and the schedules of funding progress and employer contributions be presented to supplement the basic financial statements. Such information, although not a part of the 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 30, 2011, on our consideration of MCERA'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 to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

Bakersfield, California
September 30, 2011

MARIN COUNTY EMPLOYEES' RETIREMENT ASSOCIATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011

This Management's Discussion and Analysis (MD&A) of the financial activities of Marin County Employees' Retirement Association (MCERA) is an overview of its fiscal operations for the year ended June 30, 2011. Readers are encouraged to consider the information presented in conjunction with the Basic Financial Statements and Notes to the Basic Financial Statements.

We are pleased to provide this overview and analysis of the financial activities of MCERA for the year ended June 30, 2011. MCERA is the public employee retirement system established by the County of Marin on July 1, 1950, and is administered by the Board of Retirement to provide retirement, disability, and death and survivor benefits for its employees under the County Employees Retirement Act of 1937.

Financial Highlights

MCERA's plan net assets as of June 30, 2011, were $1,486,058,325. The plan net assets are held in trust for payment of pension benefits to participants and their beneficiaries and all of the net assets are available to meet MCERA's ongoing obligations.

- Net assets increased by $274,828,106, primarily as a result of earnings from investments.
- Total additions as reflected in the Statement of Changes in Plan Net Assets were an increase of $368,759,452, primarily as a result of earnings from investments.
- Deductions in plan net assets increased from $88,453,569 to $93,931,346 versus the prior year. The increase was due to an increase in retiree pension benefits.
- MCERA's funding objective is to meet long-term benefit obligations through contributions and investment income. As of June 30, 2010, the date of the last actuarial evaluation, the funded ratio for all MCERA agencies was 70.93%. In general, this indicates that for every dollar of benefits due we had approximately $0.709 of assets available for payment as of that date. The funding ratios of the employer entities included in MCERA were: 72.6% for the County of Marin and agencies, 62.9% for the City of San Rafael, and 77.1% for Novato Fire Protection District.

Overview of the Financial Statements

This MD&A serves as an introduction to the basic financial statements. MCERA has two basic financial reports, the notes to the basic financial statements, and two required supplementary schedules of historical trend information. The basic financial statements and the required disclosures are in compliance with the accounting principles and reporting guidelines as set forth by the Governmental Accounting Standards Board, utilizing the accrual basis of accounting.

Please note, however, that this report also contains other supplementary information in addition to the basic financial statements themselves.

The Statement of Plan Net Assets is the first basic financial report. This is a snapshot of account balances at fiscal year-end. This statement reflects assets available for future payments to retirees and their beneficiaries and any current liabilities that are owed as of fiscal year-end. The Net Assets Held in Trust for Pension Benefits, which are the assets less the liabilities, reflect the funds available for future use.

The Statement of Changes in Plan Net Assets is the second basic financial report. This report reflects all the activities that occurred during the fiscal year, and shows the impact of those activities as Additions or Deductions to the plan. The trend of Additions versus Deductions to the plan will indicate the condition of MCERA's financial position over time.

Both statements are in compliance with Governmental Accounting Standard Board (GASB) Pronouncements 25, 26, 28, 33, 34, 40, 44, 50, 51, 53, 55, and 56. These pronouncements require certain disclosures and also require the state and local governments to report using the full accrual method of accounting. MCERA complies with all material requirements of these pronouncements.

The Statement of Plan Net Assets and the Statement of Changes in Plan Net Assets report information about MCERA's activities. These statements include all assets and liabilities using the full accrual basis of accounting as practiced by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid. Investment gains and losses are reported on a trade-date basis and both realized and unrealized gains and losses on investments are shown.

These two statements report MCERA's net assets held in trust for pension benefits (net assets) – the difference between assets and liabilities – as one way to measure MCERA's financial position. Over time, increases and decreases in MCERA's net assets is one indicator of whether its financial health is improving or deteriorating. Other factors, such as market conditions, should also be considered in measuring MCERA's overall health.

The Notes to the Basic Financial Statements (Notes) are an integral part of the financial reports. The Notes provide detailed discussion of key policies, programs, and activities that occurred during the year.

The *Schedule of Funding Progress* required supplementary schedule includes historical trend information about the actuarially funded status of MCERA, and the progress made in accumulating sufficient assets to pay benefits when due. The other required supplementary schedule, the *Schedule of Employer Contributions*, presents historical trend information about the annual required contributions of the employer and the actual contributions made. These schedules provide information to help promote understanding of the changes in the funded status of MCERA over time.

Financial Analysis

The reserves needed to finance retirement benefits are accumulated through the collection of employer and employee contributions and through earnings on investment income (net of investment expense). Net assets held in trust for pension benefits as of June 30, 2011, totaled $1,486,058,325, an increase of $274,828,106 over the prior year. MCERA's assets exceeded its liabilities at the end of the year. The Total Plan Net Assets represent funds available for future payments. However, of importance, is the fact that unlike private pension funds, public pension funds are not required to report the future liability of obligations owed to retirees. Only current liabilities are reported in the Statement of Plan Net Assets. Below is a comparison of current and prior year balances:

	2011	2010	2009	Increase (Decrease) 2011/2010	Increase (Decrease) 2010/2009
Investments at fair value	$ 1,388,331,770	$ 1,068,714,633	$ 1,005,525,154	$ 319,617,137	$ 63,189,479
Cash and cash equivalents	116,800,206	135,783,006	118,021,449	(18,982,800)	17,761,557
Capital assets (net of accumulated depreciation)	7,475,819	7,189,149	6,104,088	286,670	1,085,061
Collateral held for securities loaned	98,631,898	85,912,381	48,596,264	12,719,517	37,316,117
Receivables and other assets	10,568,885	8,726,306	8,515,264	1,842,579	211,042
Total assets	1,621,808,578	1,306,325,475	1,186,762,219	315,483,103	119,563,256
Total liabilities	135,750,253	95,095,256	56,740,934	40,654,997	38,354,322
Net assets	$ 1,486,058,325	$ 1,211,230,219	$ 1,130,021,285	$ 274,828,106	$ 81,208,934

In order to determine whether Plan Net Assets will be sufficient to meet future obligations, the actuarial funded status needs to be calculated. An actuarial valuation is similar to an inventory process. On the valuation date, the assets available for the payment of retirement benefits are appraised. These assets are compared with the actuarial liabilities, which are the actuarial present value of all future benefits expected to be paid for each member. The purpose of the valuation is to determine what future contributions by the members and the County of Marin are needed to pay all expected future benefits.

MCERA's independent actuary, EFI Actuaries, performed an actuarial valuation as of June 30, 2010, and determined that the funded ratio of the actuarial assets to the actuarial accrued liability is 70.93%. The actuarial valuation as of June 30, 2009 determined the funded ratio to be 72.12%.

Additions to Plan Net Assets

There are three primary sources of funding for MCERA retirement benefits: earnings (losses) on investments of assets and employer and employee contributions. Income sources for the fiscal years June 30, 2011 and 2010, totaled $368,759,452 and $169,662,503, respectively.

	2011	2010	2009	Increase (Decrease) 2011/2010	Increase (Decrease) 2010/2009
Employer contributions	$ 66,256,762	$ 56,270,346	$ 54,555,518	$ 9,986,416	$ 1,714,828
Plan members contributions	16,800,303	17,419,684	17,397,816	(619,381)	21,868
Total net investment income (loss)	285,702,387	95,972,473	(275,832,228)	189,729,914	371,804,701
Total	$ 368,759,452	$ 169,662,503	$ (203,878,894)	$ 199,096,949	$ 373,541,397

Deductions from Plan Net Assets

MCERA was created to provide lifetime retirement annuities, survivor benefits, and permanent disability benefits to qualified members and their beneficiaries. The cost of such programs includes recurring benefit payments, as designated by the plan, refund of contributions to terminated employees, and the cost of administering the system. Below is a comparison of selected current and prior year balances:

	2011	2010	2009	Increase (Decrease) 2011/2010	Increase (Decrease) 2010/2009
Retirement benefits	$ 89,703,494	$ 83,704,078	$ 77,417,556	$ 5,999,416	$ 6,286,522
Refund of contributions	616,579	993,559	1,065,627	(376,980)	(72,068)
Administrative expenses	2,804,186	2,961,121	2,701,167	(156,935)	259,954
Legal expenses	660,807	595,410	762,963	65,397	(167,553)
Litigation settlement	4,500	-	13,000	4,500	(13,000)
Computer expenses	7,350	-	-	7,350	-
Actuarial expenses	134,430	199,401	103,113	(64,971)	96,288
Total deductions	$ 93,931,346	$ 88,453,569	$ 82,063,426	$ 5,477,777	$ 6,390,143

The Retirement Fund as a Whole

Despite variations in the stock market, MCERA's management believes that MCERA is in reasonably sound financial position to meet its obligations to the retired and current employees. The current financial position results from a diversified investment program that prudently manages risk to minimize loss, an effective system of cost control and strategic planning. Management believes there will continue to be sufficient assets to meet all benefit obligations.

Requests for Information

This financial report is designed to provide the Retirement Board, our membership, taxpayers, and investment managers with a general overview of MCERA finances and to demonstrate MCERA's accountability for the funds under its stewardship.

Please address any questions about this report or requests for additional financial information to:

Marin County Employees' Retirement Association
One McInnis Parkway, Suite 100
San Rafael, CA 94903

Respectively submitted,

/s/ Lisa Jackson
Lisa Jackson
Senior Accountant

BASIC FINANCIAL STATEMENTS

MARIN COUNTY EMPLOYEES' RETIREMENT ASSOCIATION
STATEMENTS OF PLAN NET ASSETS
AS OF JUNE 30, 2011 AND 2010

	June 30, 2011	June 30, 2010
Assets		
Cash and short-term investments		
Cash and cash equivalents	$ 116,800,206	$ 135,783,006
Collateral held for securities loaned	98,631,898	85,912,381
Total Cash and Short-Term Investments	215,432,104	221,695,387
Receivables		
Contributions	4,012,115	3,199,854
Interest and dividends	2,248,386	1,929,369
Due from brokers for securities sold	2,740,582	1,894,835
Other receivables	776,299	1,083,897
Total Receivables	9,777,382	8,107,955
Investments at fair value		
Domestic fixed income	186,320,702	161,598,315
International fixed income	18,421,144	16,348,909
Domestic equities	692,039,072	523,754,964
International equities	342,607,324	237,228,105
Private equity	21,426,764	8,442,491
Real estate	127,516,764	121,341,849
Total Investments at Fair Value	1,388,331,770	1,068,714,633
Capital assets (net of accumulated depreciation)	7,475,819	7,189,149
Prepaid insurance	791,503	618,351
Total Assets	1,621,808,578	1,306,325,475
Liabilities		
Accounts payable and accrued expenses	1,290,369	1,517,441
Due to brokers for securities purchased	34,109,730	5,987,937
Rental security deposits	652,791	669,091
Retiree payroll payable	-	8,406
Prepaid contributions	65,465	-
Health insurance payable	1,000,000	1,000,000
Collateral held for securities loaned	98,631,898	85,912,381
Total Liabilities	135,750,253	95,095,256
Net Assets Held in Trust for Pension Benefits	$ 1,486,058,325	$ 1,211,230,219

A schedule of funding progress is presented in the Required Supplementary Information following this Financial Section.

The accompanying notes are an integral part of these financial statements.

MARIN COUNTY EMPLOYEES' RETIREMENT ASSOCIATION
STATEMENTS OF CHANGES IN PLAN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2011 AND 2010

	June 30, 2011	June 30, 2010
Additions		
Contributions		
Employer	$ 66,256,762	$ 56,270,346
Plan member	16,800,303	17,419,684
Total Contributions	83,057,065	73,690,030
Investment income		
Net appreciation in fair value of investments	273,208,148	80,864,466
Interest and dividends	16,330,478	15,662,211
Real estate operating income, net	4,429,705	7,191,292
Other investment income	593,864	483,780
Total investment income	294,562,195	104,201,749
Less investment expenses	9,124,321	8,462,445
Net Investment Income	285,437,874	95,739,304
Securities lending activities		
Securities lending income	510,696	437,969
Less expenses from securities lending activities	246,183	204,800
Net Securities Lending Income	264,513	233,169
Total Net Investment Income	285,702,387	95,972,473
Total Additions	368,759,452	169,662,503
Deductions		
Benefits	89,703,494	83,704,078
Refunds	616,579	993,559
Administrative expenses - Note 8	2,804,186	2,961,121
Legal expense	660,807	595,410
Litigation settlement	4,500	-
Computer expenses	7,350	-
Actuarial expenses	134,430	199,401
Total Deductions	93,931,346	88,453,569
Net Increase	274,828,106	81,208,934
Net Assets Held in Trust for Pension Benefits, Beginning of Year	1,211,230,219	1,130,021,285
Net Assets Held in Trust for Pension Benefits, End of Year	$ 1,486,058,325	$ 1,211,230,219

The accompanying notes are an integral part of these financial statements.

NOTE 1 – PLAN DESCRIPTION

The Marin County Employees' Retirement Association (MCERA) was formed July 1, 1950, by the adoption of the County Employees' Retirement Law of 1937 (State of California Government Code Section 31502) by the Marin County Board of Supervisors pursuant to a vote of the people of Marin County. MCERA is a cost-sharing, multiple-employer defined benefit plan (the Plan) covering the employees of Marin County and various special districts. MCERA, with its own governing boards, is an independent governmental entity separate and distinct from the County of Marin (County). MCERA's Annual Financial Statements are included in the County's Annual Financial Report as a pension trust fund. Maintaining appropriate controls and preparing the financial statements are the responsibility of MCERA management. On July 1, 1977, the City of San Rafael, San Rafael Redevelopment Agency, and the Novato Fire Protection District also became participants in the program.

MCERA is an agent multiple-employer public employee retirement system (PERS). Such plans cover employees of more than one employer and pool administrative and investment functions as a common investment and administrative agent for each employer. Administrative costs of MCERA are financed through investment earnings and paid by MCERA. As required under California Government Code Section 31520.1, MCERA is governed by the following Board of Retirement:

	Term Expires
Maya Gladstern	10/31/13
Howard McFarland	10/31/11
Karen Wofford	10/31/13
Allen Haim	10/31/12
Sean Webb, Alternate	10/31/12
Greg Brenk	10/31/13
Gerald Richardson	10/31/11
James Phillips	10/31/13
Bernadette Bolger	10/31/12
Gary Burroughs	Ex-Officio
Roy Given	Ex-Officio Alternate

MCERA is operated under Section 31450 of the California Government Code related to employees. At June 30, 2011, the number of participating local government employers was:

County	1
City	1
California Superior Courts, Marin	1
Special Districts	7
Total	10

NOTE 1 – PLAN DESCRIPTION (Continued)

MCERA's membership consisted of the following as reported in the most recent actuarial valuation dated June 30, 2010:

	June 30, 2011	June 30, 2010
Active Members (vested and non-vested)	2,682	2,763
Retired Members and Beneficiaries	2,431	2,335
Terminated Vested (deferred)	596	717
Total Membership	5,709	5,815

As required by State statutes and MCERA by-laws, all regular-hire employees considered at least three-quarter time must participate in the County's pension plans. Under the provisions of the County's pension plan, pension benefits vest after five years of credited service. Employees are eligible to receive benefits upon reaching the age of 50 and 10 years of credited service or after 30 years of service (Safety, 20 years of service). Pension benefit amounts vary based on the individual's age and number of years in the retirement system. The maximum pension benefit is 100% of final compensation. Also, the pension plan provides for death benefits and disability benefits. All pension, death, and disability benefits are determined in accordance with State statutes.

Contributions are determined based on a percentage of compensation for each entry age so as to provide a lifetime annuity commencing at age 50. For the County members hired on or after July 1, 2008, and for Marin County Superior Courts members hired on or after January 1, 2008, the lifetime annuity commences at age 55.

MCERA also facilitates for the County a healthcare premium benefit provided to retirees with five or more years of qualifying service credit (substantially all retirees). MCERA does not hold any funds in a 401h account related to these benefits. As a result, the actuarial information presented on pages 20 through 21 excludes obligations for future health benefits. Separate asset reserves are maintained for health benefits for retirees of the City of San Rafael. All health benefits are funded on a pay-as-you-go basis.

Employer and employee contributions are based on actuarial valuations that cover the mortality, service, and compensation experience of the members and beneficiaries, and the evaluation of the assets and liabilities of the retirement fund. The Board of Supervisors makes the necessary changes in County contribution rates and interest rates based upon the valuations and recommendations of the actuary. According to the June 30, 2010, actuarial valuation, depending on the age and classification at hire date, employees' weighted contributions are 9.66% of covered payroll for the County; City of San Rafael employees' weighted contributions are 10.92%; and Novato Fire Protection District employees' weighted contributions are 13.36%.

Retiree and survivor benefits are adjusted annually for cost of living by the annual increase or decrease in the Consumer Price Index (CPI). In years when the CPI changes by more than specified limits, the excess is accumulated and applied to future years when the change in the CPI is less than those limits. The following limits are currently in effect: (a) 3% for City of San Rafael, (b) 2% for County retirees hired after June 30, 1980, and (c) 4% for all other retirees.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

MCERA follows the accounting principles and reporting guidelines as set forth by the Governmental Accounting Standards Board (GASB).

The financial statements are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the Plan.

NOTE 2 – <u>SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES</u> (Continued)

Investments are reported at fair value, except that short-term investments are reported at cost, which approximates fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates or by various outside pricing sources. The fair value of real estate investments is based on independent appraisals.

<u>Cash</u>

Cash includes deposits with various financial institutions, the County trust fund, and international currency holdings, which have original maturities of less than 90 days, translated to U.S. dollars using the exchange rates in effect at June 30, 2011 and 2010.

<u>Capital Assets</u>

Capital assets are valued at historical cost less accumulated depreciation. Capital assets with an initial cost of more than $5,000 and an estimated useful life in excess of one year are depreciated. Depreciation is calculated using the straight-line method over the estimated useful lives of the depreciable assets. Equipment has a useful life of ten years, leasehold improvements and office space forty years, and twelve years for the CPAS pension system.

MCERA signed an agreement on July 2, 2007, for the purchase of a building located on One McInnis Parkway, San Rafael, CA 94903. The final purchase price for the building was $17,300,000 and was finalized in October 2007. MCERA occupied the building on November 14, 2008. MCERA occupies 33% of the building and leases the other 67%. Therefore, the portion of the building occupied by MCERA was capitalized and is being depreciated over its useful life. The remaining 67% will be treated as an investment and, accordingly, marked to market value in addition to recognizing any earned income and expenses incurred. As of June 30, 2011, the capitalized portion of the building was $3,663,124 and computers and equipment were $3,812,696, net of accumulated depreciation.

<u>Use of Estimates</u>

The preparation of MCERA's financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the basic financial statements and accompanying notes. Actual results could differ from these estimates.

<u>Reclassifications</u>

Comparative data for the prior year has been presented in the selected sections of the accompanying Statements of Plan Net Assets and Changes in Plan Net Assets. Also, certain accounts presented in the prior year's data may have been reclassified in order to be consistent with the current year's presentation.

<u>Reserves</u>

The reserves represent the components of MCERA's net assets. Reserves are established from employee and employer contributions and the accumulation of investment income after satisfying investment and administrative expenses. The reserves do not represent the present value of assets needed, as determined by actuarial valuation, to satisfy requirements and other benefits as they become due.

The Contingency Reserve is established as required by the County Employees Retirement Law of 1937 to absorb possible future losses on investments. The reserve balance, per the County Employees Retirement Law of 1937, is one percent (1%) of the total market value of assets if excess earnings exist. MCERA's policy sets the targeted rate at one percent (1%). The Contingency Reserve is 1% and 1% of the market value of total assets at June 30, 2011 and 2010, respectively.

NOTE 3 – DEPOSIT AND INVESTMENT RISK DISCLOSURE

The County Employees Retirement Law of 1937 (Retirement Law) vests the Board of Retirement (Board) with exclusive control over MCERA's investment portfolio. The Board established an Investment Policy Statement in accordance with applicable local, State, and Federal laws. The Board members exercise authority and control over the management of MCERA's assets (the Plan) by setting policy which the Investment Staff executes either internally, or through the use of external prudent experts. The Board oversees and guides the Plan subject to the following basic fiduciary responsibilities:

- Solely in the interest of, and for the exclusive purpose of, providing economic benefits to participants and their beneficiaries, minimizing contributions thereto, and defraying reasonable expenses of administering the Plan.
- Invest and manage Plan assets as a prudent investor would, by considering the purposes, terms, distribution requirements, and other circumstances of the Plan. In satisfying this standard of care, the trustees shall exercise reasonable care, skill, and caution.
- Diversify the investments of the Plan so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances, it is clearly prudent not to do so. Diversification is applicable to the deployment of the assets as a whole.

The Investment Policy Statement encompasses the following:

- Criteria for Selecting and Terminating Investment Managers
- Investment Objective and Guidelines by Asset Class
- Duties and Responsibilities of the MCERA Board
- Duties and Responsibilities of Staff, Investment Managers, Custodian and Investment Consultant
- Proxy Voting
- Statement of Objectives, Guidelines and Procedures for each Investment Manager

Credit Risk

Credit Risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. MCERA seeks to maintain a diversified portfolio of fixed income instruments in order to obtain the highest total return for the fund at an acceptable level of risk within this asset class. To control Credit Risk, credit quality guidelines have been established.

The Domestic Fixed Income Core Portfolio must meet the following credit qualities:

- The portfolio will be invested only in investment grade securities as defined by one of the major rating agencies. The Core Fixed Income manager will maintain an overall portfolio quality rating of "AA-Aa3" or equivalent or better.
- The Core Fixed Income manager may invest up to 10% of the portfolio in 144A securities.

The Domestic Fixed Income Core Plus Portfolio must meet the same credit qualities listed above, except for the following:

- The Core Plus Fixed Income manager may invest up to 20% of the portfolio in securities rated below investment grade by at least one of the major rating agencies.
- The Core Plus Fixed Income manager may invest up to 20% of the portfolio in 144A securities.

As of June 30, 2011 and 2010, the total MCERA fixed income portfolio maintained an Aa2 rating (as represented by moody's). The Core Fixed Income manager maintained an Aa2 rating, while the Core Plus Fixed Income manager maintained an Aa1 rating.

NOTE 3 – DEPOSIT AND INVESTMENT RISK DISCLOSURE (Continued)

Custodial Credit Risk

Custodial Credit Risk for deposits is the risk that in the event of a financial institution's failure, MCERA would not be able to recover its deposits. Deposits are exposed to custodial credit risk if they are not insured or not collateralized. MCERA's deposits are not exposed to custodial credit risk as its deposits are eligible for and covered by "pass-through insurance" in accordance with applicable law and FDIC rules and regulations. Additional insurance against loss and theft is provided through a Financial Institution Bond.

Custodial Credit Risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, MCERA would not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in MCERA's name, and held by the counterparty. MCERA's investment securities are not exposed to custodial credit risk because all securities are held by MCERA's custodial bank in MCERA's name. MCERA has investments in commingled funds that are not held by MCERA's custodial bank. However, investments in open-end mutual funds are not exposed to custodial credit risk because their existence is not evidenced by securities that exist in physical or book entry form. MCERA has no general policy on custodial credit risk for investments.

Concentration of Credit Risk

As of June 30, 2011 and 2010, MCERA did not hold any investments in any one issuer that would represent five percent (5%) or more of total investments. Investments issued or explicitly guaranteed by the U.S. government and pooled investments are excluded from this requirement.

Interest Rate Risk

Interest Rate Risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Duration is a measure of the price sensitivity of a fixed income portfolio to changes in interest rates. It is calculated as the weighted average time to receive a bond's coupon and principal payments. The longer the duration of a portfolio, the greater its price sensitivity to changes in interest rates.

MCERA does not have a general policy to manage interest rate risk. To manage interest rate risk, the modified adjusted duration of the Domestic Fixed Income Core and Core Plus Portfolios are restricted to +/- 25% of the Lehman Brothers Aggregate Bond Index's modified adjusted duration. Deviations from any of the stated guidelines require prior written authorization from MCERA.

As of June 30, 2011 and 2010, MCERA's Core Fixed Income manager had a duration of 4.62 years and 3.93 years, respectively, while MCERA's Core Plus Fixed Income manager had a duration of 4.86 years and 4.37 years, respectively.

Foreign Currency Risk

Foreign Currency Risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or deposit. Forward currency contracts and currency futures (maturity ranging from at least 30 days and not to exceed one year for either instrument) are permitted for currency hedging.

MCERA's exposure to Foreign Currency Risk in U.S. dollars as of June 30, 2011 and 2010, was $0 and $0, respectively.

MCERA invests indirectly, through its portfolio managers, in foreign currency forward transactions to limit its exposure to fluctuations in foreign currency exchange rates. Aside from net currency gains or losses reported as a component of investment income, no other amounts are recorded on the financial statements.

NOTE 3 – DEPOSIT AND INVESTMENT RISK DISCLOSURE (Continued)

Foreign Currency Risk (Continued)

These forward transactions typically range from one to six months. When used in a hedging strategy, a loss in value of the underlying security, due to a weakening of a foreign currency relative to the U.S. dollar will result in an opposite gain in value of the gift foreign currency transaction. The reverse is true for a foreign currency, which strengthens relative to the U.S. dollar.

Foreign currency forward transactions are typically transacted with highly rated (usually AA or better) financial institutions, typically major worldwide commercial or investment banks. Counterparty risk occurs when the financial institution (who engages in the forward transaction with MCERA) has a liability due to MCERA and is unable to pay. This risk is monitored on a daily basis by the investment advisors and limited to maximum levels of exposure for the entire portfolio.

Derivatives

The investment derivatives schedule below reports the fair value balances, changes in fair value, and notional amounts of derivatives outstanding as of and for the year ended June 30, 2011, classified by type. For financial reporting purposes, all MCERA derivatives are classified as investment derivatives.

The fair values of currency forward contracts are determined using a proprietary pricing service, which uses published foreign exchange rates as the primary source. The fair values of credit rate swaps, interest rate swaps, and warrants are determined using the custodian pricing vehicles. The fair value of TBA transactions are also determined by the custodian pricing vehicles.

Investment derivatives for the year ended June 30, 2011, were as follows:

	Changes in Fair Value	Fair Value	Notional Value
Fixed Income Futures Long	$ 1,762,598	$ -	$ 42,150,000
Fixed Income Futures Short	(776,327)	-	(37,500,000)
Futures Options Bought	(130,510)	12,122	127,500
Futures Options Written	186,676	(49,372)	(377,500)
Index Futures Long	39,650,881	-	12,350
TBA Transactions Long	34,566	-	-
Total	$ 40,727,884	$ (37,250)	

Investment derivatives for the year ended June 30, 2010, were as follows:

	Changes in Fair Value	Fair Value	Notional Value
Fixed Income Futures Long	$ 5,939,986	$ 542,522	$ 34,800,000
Fixed Income Futures Short	(956,221)	(258,232)	(15,900,000)
Futures Options Bought	(5,588)	76,481	283,500
Futures Options Written	72,913	(124,369)	(760,500)
Index Futures Long	22,607,935	(7,637,601)	144,600
TBA Transactions Long	160,669	(1,284)	2,000,000
Total	$ 27,819,694	$ (7,402,483)	

NOTE 3 – DEPOSIT AND INVESTMENT RISK DISCLOSURE (Continued)

Custodial Credit Risk – Derivatives – As of June 30, 2011 and 2010, MCERA's investments did not include collateral associated with derivatives activity.

Credit Risk – Derivatives – MCERA is exposed to credit risk on investment derivatives that are traded over the counter and are reported in asset positions. Derivatives exposed to credit risk include credit default and interest rate swaps, currency forward contracts, rights, warrants, and TBA transactions. To minimize credit risk exposure, MCERA investment managers continuously monitor credit ratings of counterparties. Should there be a counterparty failure, MCERA would be exposed to the loss of fair value of derivatives that are in asset positions and any collateral provided to the counterparty, net of the effect of applicable netting arrangements. MCERA has no general investment policy with respect to netting arrangements or collateral requirements. Netting arrangements legally provide MCERA with a right of offset in the event of bankruptcy or default by the counterparty. As of June 30, 2011 and 2010, MCERA had no exposure to loss in case of default of a counterparty. In addition, MCERA had no collateral reducing exposure or liabilities subject to netting arrangements.

NOTE 4 – REAL ESTATE

The following is a listing of California real estate held by MCERA (dollars in thousands):

	Appraised Value	
Location	2011	2010
Separate Properties:		
Sacramento	$ -	$ 3,370
Sunnyvale*	4,775	4,250
South San Francisco	8,000	8,000
Foster City	24,500	22,000
San Bruno*	17,000	17,900
Pleasanton*	26,680	23,540
Richmond*	12,390	12,370
One McInnis*	6,670	7,860
Total	100,015	99,290
AEW Capital Management	1,721	1,780
ING Clarion	20,555	17,073
RREEF America REIT III	5,226	3,199
Total	27,502	22,052
Grand Total	$ 127,517	$ 121,342

* Properties are appraised on a quarterly rotational basis at the discretion of management. On average two properties are appraised each quarter.

NOTE 5 – SECURITIES LENDING TRANSACTIONS

State statutes and the investment policies of MCERA allow the Plan to enter into securities lending transactions (loans of securities to broker-dealers and other entities for collateral with a simultaneous agreement to return the collateral for the same securities in the future). Securities loaned are secured by cash collateral of 103% of the fair value of the loaned securities plus accrued interest. MCERA is not exposed to credit risk on security lending transactions because its custodian is required to indemnify MCERA against any related losses.

Securities loaned include U.S. government and agencies securities, corporate bonds, and domestic corporate stock. MCERA is not restricted as to the amount of loans that can be made. MCERA cannot pledge or sell collateral securities received unless the borrower defaults. As of June 30, 2011 and 2010, the value of securities loaned by MCERA totaled $96,927,702 and $83,522,419, respectively. As of June 30, 2011 and 2010, the value of collateral held for securities loaned was $98,631,898 and $85,912,381, respectively.

NOTE 6 – CONCENTRATIONS

MCERA has entered into a custodial agreement with State Street. State Street custodies securities and collects income for MCERA. The value of MCERA's investments under State Street's custodianship at June 30, 2011 and 2010, was approximately $670,472,238 and $641,785,584, respectively.

The following firms professionally manage MCERA's investments (dollars in thousands):

	Value of Investments 2011	Value of Investments 2010
Woodmont Real Estate Services	$ 100,015	$ 99,290
Western Asset Management	147,284	141,002
Wellington Management Company	154,572	131,933
Columbus Circle	75,661	41,605
Dodge & Cox	137,066	87,428
RCM Global Investors	136,456	104,139
Blackrock Global Investors	-	79,123
Dimensional Fund Advisors	69,194	53,702
Artisan Funds	113,064	85,572
Morgan Stanley	118,652	97,040
Numeric Investors LP	-	29,227
Fidelity Market Neutral	-	33,391
Fidelity Small Cap International	46,364	32,904
Analytic Investors - US	-	21,863
AEW Partners	1,721	1,780
ING Clarion	20,555	17,073
RREEF	5,225	3,199
Abbott	11,546	5,705
Pathway	9,881	2,738
Eaton Vance	32,527	-
S & P 500	208,549	-

NOTE 7 – OPERATING LEASES

MCERA holds real property on which it collects rental income under several operating lease arrangements. Generally, these leases provide for renewal options at the conclusion of fixed terms that vary in length. Rental income on all operating leases of MCERA amounted to $9,481,344 and $9,773,080 for the years ended June 30, 2011 and 2010, respectively.

NOTE 8 – ADMINISTRATIVE EXPENSES

California Government Code §31580.2 requires that the Board of Retirement may expend no more than .18% of the total assets of the retirement system for administrative expenses. However, per §31580.3 if during the year the expense of administration of the retirement system includes expenditures for software, hardware, and computer technology consulting services in support of that software or hardware, the expense incurred may not exceed the greater of the following: (1) the sum of eighteen hundredths of 1 percent of the total assets of the retirement system plus one million ($1,000,000) or (2) twenty-three hundredths of 1 percent of the total assets of the retirement system.

For the years ended June 30, 2011 and 2010, administrative expenses were $2,804,186, or .17%, and $2,961,121, or .23%, respectively, of the total assets of MCERA at year-end. Due to the exclusion in §31580.3 mentioned above, MCERA is in compliance due to the implementation of new CPAS software. Administrative costs of the plan are financed through investment plan assets.

NOTE 9 – RISK MANAGEMENT

MCERA is exposed to various risks of loss related to torts; theft or damage to, or destruction of, assets; injuries to employees; and errors and omissions. To address these risk items, MCERA is covered by the following policies and programs:

$10,000,000	General Liability Edgewood Partners Insurance Center $1,000,000 per occurrence
$ 1,000,000	Workers' Compensation California State Association of Counties Excess Insurance Authority Liability Program Self-insured retention of $500,000 per occurrence County of Marin
$10,000,000	Fidelity and Performance Bond National Union Fire Insurance $2,500 deductible per occurrence County of Marin

For each of the above self-insurance coverage limits, the County maintains a separate Internal Service Fund. Funding for each fund is actuarially determined.

$10,000,000	Fiduciary Liability National Union Fire Insurance Self-insured retention, $100,000 per occurrence MCERA (includes waiver of trustee liability*)

* Premium for this waiver has been paid by each trustee individually.

In addition to the above, each investment manager and the Plan's custodian carries a separate fidelity bond as well as errors and omissions insurance at levels consistent with their total funds under management.

NOTE 10 – ACTUARIAL VALUATIONS

Pursuant to provisions in the Retirement Law, MCERA engages an independent actuarial firm to perform an annual actual valuation. A system actuarial valuation is performed every three (3) years (i.e., triennial valuation). The economic and non-economic assumptions are updated at the time each triennial valuation is performed. Triennial valuations serve as the basis for changes in member contribution rates necessary to properly fund the Plan. MCERA also hires an independent actuarial firm to audit the results of each triennial valuation.

The information displayed below presents the funded status of the most recent actuarial valuation. The Schedule of Funding Progress in the Required Supplementary Information section immediately following the notes to the financial statements presents multiyear trend information regarding whether the actual value of plan assets is increasing or decreasing over time, relative to the actuarial accrued liability of benefits.

(In Thousands)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Annual Covered Payroll ((b-a)/c)
6/30/2010	$ 1,368,705	$ 1,929,666	$ 560,961	70.93%	$ 215,969	259.74%

The information presented in the supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation is as follows:

Valuation date	June 30, 2010
Actuarial cost method	Entry age normal method
Amortization method	Level percentage of payroll
Asset valuation method	Excess earnings smoothed over five years, 80%/120%corridor around market value
Annual inflation rate	3.50%
Investment rate of return	7.75%
Postretirement benefit increase	COLA, maximum of 2/3/4% based on Tier
Projected salary increases	3.50%, plus service-based rates
Remaining amortization periods	30 years for Special Amortization Base (closed)
County of Marin	For the remainder of Unfunded Liability*
City of San Rafael	For the remainder of Unfunded Liability*
California Superior Court, Marin	For the remainder of Unfunded Liability*
Novato Fire Protection District	For the remainder of Unfunded Liability*
Southern Marin Fire Protection District	For the remainder of Unfunded Liability*
LAFCO	For the remainder of Unfunded Liability*
Marin Sonoma Mosquito Abatement	For the remainder of Unfunded Liability*
Tamalpais Community Service District	For the remainder of Unfunded Liability*
San Rafael Redevelopment Agency	For the remainder of Unfunded Liability*
Marin City Community Services District	For the remainder of Unfunded Liability*

*Remaining at 17 for four years, then closed

NOTE 11 – COMMITMENTS AND CONTINGENCIES

Litigation

MCERA is defendant in various lawsuits and other claims arising in the ordinary course of its operations. MCERA's management and legal counsel estimate the ultimate outcome of such litigation will not have a material effect on MCERA's basic financial statements.

Capital Commitments

MCERA real estate and Private Equity investment managers identify and acquire investments on a discretionary basis. Each manager's investment activity is controlled by the Manager Investment Plan, which identifies the limitations on each manager's discretion. Such investment activities are further restricted by the amount of capital allocated or committed to each manager. Both the Manager Investment Plan and capital commitments are subject to approval by the MCERA Board of Retirement and may be updated as often as necessary to reflect MCERA investment preferences, as well as changes in market conditions.

During fiscal year 2011, MCERA funded $10,417,500 of its private equity capital commitments. As of June 30, 2011, outstanding commitments to the various investment managers, as approved by the Board, totaled $176,773,622. Subsequent to June 30, 2011, MCERA funded $12,808,878 of these capital commitments.

NOTE 12 – SUBSEQUENT EVENTS

Subsequent to June 30, 2011, and through September 30, 2011, the date through which management evaluated subsequent events and on which the financial statements were issued, MCERA did not identify any subsequent events that require disclosure, besides those noted in Note 11.

REQUIRED SUPPLEMENTARY INFORMATION

MARIN COUNTY EMPLOYEES' RETIREMENT ASSOCIATION
SCHEDULE OF FUNDING PROGRESS
(DOLLAR AMOUNTS IN THOUSANDS)

Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Annual Covered Payroll ((b-a)/c)
County of Marin						
6/30/2005	$ 858,183	$ 992,226	$ 134,043	86.49%	$ 141,272	94.88%
6/30/2006	908,767	1,090,344	181,577	83.35%	149,527	121.43%
6/30/2007	1,013,543	1,141,736	128,193	88.77%	159,177	80.53%
6/30/2008	1,111,115	1,280,206	169,091	86.79%	173,735	97.33%
6/30/2009	1,002,218	1,350,528	348,310	74.21%	178,027	195.65%
6/30/2010	1,018,082	1,402,358	384,276	72.60%	176,833	217.31%
City of San Rafael (including RDA)						
6/30/2005	195,698	265,205	69,507	73.79%	28,357	245.11%
6/30/2006	209,785	306,079	96,294	68.54%	28,606	336.62%
6/30/2007	235,756	325,219	89,463	72.49%	30,180	296.43%
6/30/2008	262,677	360,298	97,621	72.91%	31,854	306.46%
6/30/2009	239,841	379,801	139,960	63.15%	32,413	431.80%
6/30/2010	248,500	394,889	146,389	62.93%	30,320	482.81%
Novato Fire Protection District						
6/30/2005	86,839	98,787	11,948	87.91%	7,889	151.45%
6/30/2006	92,390	109,131	16,741	84.66%	7,990	209.52%
6/30/2007	102,658	115,974	13,316	88.52%	7,881	168.96%
6/30/2008	112,126	129,116	16,990	86.84%	8,860	191.76%
6/30/2009	101,194	132,105	30,911	76.60%	9,116	339.09%
6/30/2010	102,123	132,419	30,296	77.12%	8,816	343.65%
Total						
6/30/2005	1,140,720	1,356,218	215,498	84.11%	177,518	121.40%
6/30/2006	1,210,942	1,505,554	294,612	80.43%	186,123	158.29%
6/30/2007	1,351,957	1,582,929	230,972	85.41%	197,238	117.10%
6/30/2008	1,485,918	1,769,620	283,702	83.97%	214,449	132.29%
6/30/2009	1,343,253	1,862,434	519,181	72.12%	219,556	236.47%
6/30/2010	1,368,705	1,929,666	560,961	70.93%	215,969	259.74%

MARIN COUNTY EMPLOYEES' RETIREMENT ASSOCIATION
SCHEDULE OF EMPLOYER CONTRIBUTIONS
(DOLLAR AMOUNTS IN THOUSANDS)

Schedule of Employer Contributions

Year Ended June 30,	Annual Required Contribution	Percentage Contributed
County of Marin		
6/30/2005	$ 22,085	100%
6/30/2006	36,870	100%
6/30/2007	42,416	100%
6/30/2008	39,656	100%
6/30/2009	36,638	100%
6/30/2010	39,437	100%
City of San Rafael (including RDA)		
6/30/2005	7,653	100%
6/30/2006	4,231	100%
6/30/2007	11,187	100%
6/30/2008	14,068	100%
6/30/2009	13,702	100%
6/30/2010	12,700	100%
Novato Fire Protection District		
6/30/2005	2,343	100%
6/30/2006	2,526	100%
6/30/2007	3,612	100%
6/30/2008	4,366	100%
6/30/2009	4,215	100%
6/30/2010	4,134	100%
Total		
6/30/2005	32,081	100%
6/30/2006	43,627	100%
6/30/2007	57,215	100%
6/30/2008	58,090	100%
6/30/2009	54,555	100%
6/30/2010	56,271	100%