

**SAN FRANCISCO CITY AND COUNTY
EMPLOYEES' RETIREMENT SYSTEM**

Financial Statements and
Required Supplementary Information
(With Independent Auditor's Report Thereon)

Years Ended June 30, 2016 and 2015



Certified
Public
Accountants

**SAN FRANCISCO CITY AND COUNTY
EMPLOYEES' RETIREMENT SYSTEM
Years Ended June 30, 2016 and 2015**

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Independent Auditor's Report

Retirement Board of San Francisco
City and County Employees' Retirement System
San Francisco, California

Report on the Financial Statements

We have audited the accompanying financial statements of the San Francisco City and County Employees' Retirement System ("Retirement System"), a pension trust fund of the City and County of San Francisco, California, as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net position of the Retirement System as of June 30, 2016 and 2015, and the changes in its plan net position for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As described in Note 1, the financial statements present only the Retirement System and do not purport to, and do not, present fairly the financial position of the City and County of San Francisco as of June 30, 2016 and 2015, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 2 to the financial statements, effective July 1, 2015, the Retirement System adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 72, *Fair Value Measurement and Application*.

As discussed in Note 10 to the financial statements, the total pension liability based on the actuarial valuation as of June 30, 2015, rolled forward to June 30, 2016, exceeded the pension plan net position by \$5.8 billion. The actuarial valuation is very sensitive to the underlying assumptions, including the discount rate of 7.50%, which represents the long-term expected rate of return.

Our opinion is not modified with respect to these matters.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that management's discussion and analysis, the schedule of changes in the net pension liability and related ratios, the schedule of employer contributions, and the schedule of money-weighted rate of return, as listed in the table of contents, be presented to supplement the 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 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 financial statements, and other knowledge we obtained during our audits of the 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 Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated January 11, 2017 on our consideration of the Retirement System'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 for the year ended June 30, 2016. 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 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 the Retirement System's internal control over financial reporting and compliance.



San Francisco, California
January 11, 2017

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Management's Discussion and Analysis – Unaudited

Years Ended June 30, 2016 and 2015

(Dollar amounts in thousands)

The management of the City and County of San Francisco Employees' Retirement System (Retirement System) is pleased to provide this overview and analysis of the financial activities of its cost-sharing multiple-employer defined benefit pension plan (Plan) for the years ended June 30, 2016 and 2015. We encourage readers to consider the information presented here in conjunction with the *Financial Statements and Required Supplementary Information*, which follow this discussion. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

Financial Highlights

Fiscal Year 2016

- The assets of the Retirement System exceeded its liabilities at the close of the year ended June 30, 2016. The Plan held \$20,154,503 of net position restricted for pension benefits. All of the net position is available to meet the Retirement System's ongoing obligations to plan participants and their beneficiaries.
- The Retirement System's funding objective is to meet long-term benefit obligations through contributions and investment income. The Retirement System's plan net position as a percentage of the total pension liability should be considered when evaluating the Retirement System's financial health. Based on the June 30, 2016 measurement date, the plan net position was 77.6% of the total pension liability.
- For the year ended June 30, 2016, the Retirement System's net investment income of \$150,190 represents 0.7% of plan net position as of the beginning of the fiscal year. Specifically, net appreciation in fair value of investments declined by \$595,371 as a result of lower returns in all asset classes relative to the prior fiscal year.
- Total net position held in trust for pension benefits decreased by \$273,566, or 1.3%, primarily as a result of market conditions and the net difference between contributions received by the Plan and increased benefit payments made from the Plan.
- Members' contributions to the Plan totaled \$322,764, an increase of \$21,082 or 7.0% from the prior year. This increase is primarily a result of increases in the number of active employees contributing to the Plan. Employee contribution rates in fiscal year 2015-16 were unchanged from fiscal year 2014-15, ranging from 7.5% - 13.0%.
- In order to maintain the fiscal soundness of the Plan, required employer contributions to the Plan totaled \$526,805, a decrease of \$65,838 or 11.1% from the prior year.
- Total deductions from the Plan were \$1,273,325, an increase of 10.7% from the prior year due to the increase in benefits paid during the current fiscal year.

Fiscal Year 2015

- The assets of the Retirement System exceeded its liabilities at the close of the year ended June 30, 2015. The Plan held \$20,428,069 of net position restricted for pension benefits. All of the net position is available to meet the Retirement System's ongoing obligations to plan participants and their beneficiaries.
- The Retirement System's funding objective is to meet long-term benefit obligations through contributions and investment income. The Retirement System's plan net position as a percentage of the total pension liability should be considered when evaluating the Retirement System's financial health. Based on the June 30, 2015 measurement date, the plan net position was 89.9% of the total pension liability.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM
Management's Discussion and Analysis – Unaudited
Years Ended June 30, 2016 and 2015
(Dollar amounts in thousands)

- For the year ended June 30, 2015, the Retirement System's net investment income of \$763,429 represents a 3.8% increase in plan net position. (This return is based on plan net position as of the beginning of the fiscal year.) Net appreciation in fair value of investments declined by \$2,465,760 as a result of lower returns in all asset classes relative to the prior fiscal year.
- Total net position held in trust for pension benefits increased by \$507,462, or 2.5%, primarily as a result of investment returns which were slightly reduced by the net difference between contributions received by the Plan and increased benefit payments made from the Plan.
- Members' contributions to the Plan totaled \$301,682, an increase of \$12,662 or 4.4% from the prior year. This increase is primarily a result of increases in the number of active employees contributing to the Plan and increases in employee contribution rates, which ranged from 7.5% - 13.0% in fiscal year 2014-15.
- In order to maintain the fiscal soundness of the Plan, required employer contributions to the Plan totaled \$592,643, an increase of \$59,761 or 11.2% from the prior year.
- Total deductions from the Plan were \$1,150,292, an increase of 5.7% from the prior year due to the increase in benefits paid during the current fiscal year.

Overview of Financial Statements

The following discussion and analysis are intended to serve as an introduction to the Retirement System's financial statements, which are comprised of the following components:

1. **Statements of Plan Net Position** are snapshots of account balances as of the close of the years – June 30, 2016 and 2015. They indicate the total assets, total liabilities and the net position restricted for future payment of retirement benefits and operating expenses as of June 30, 2016 and 2015.
2. **Statements of Changes in Plan Net Position** provide a view of additions to and deductions from the Plan during the years ended June 30, 2016 and 2015.
3. **Notes to Financial Statements** provide additional information that is essential to a full understanding of the data provided in the financial statements.

The statements of plan net position and the statements of changes in plan net position report information about the Retirement System's financial activities, prepared using the accrual basis of accounting. Contributions to the Plan are recognized when due pursuant to legal requirements and benefits and refunds are recognized when currently due and payable in accordance with the terms of the Plan.

Investments are reported at fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Securities that do not have an established market are reported at estimated fair value derived from third party pricing services. Purchases and sales of investments are recorded on a trade date basis. Private equity investments represent the Retirement System's interest in limited partnerships. The fair values of the Retirement System's partnership interests and real estate investments are based on net asset values provided by the general partners and investment managers.

Investments in forward currency contract investments are commitments to purchase and sell stated amounts of foreign currency. Changes in fair value of open contracts are immediately recognized as gains or losses. The fair value of forward currency contracts are determined by quoted currency prices from national exchanges.

Additional information on the Retirement System's investments can be found in Notes 4 and 5 of this report.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM
Management's Discussion and Analysis – Unaudited
Years Ended June 30, 2016 and 2015
(Dollar amounts in thousands)

Financial Analysis

The Plan's net position may serve over time as a useful indication of the Plan's financial position. The assets of the Plan exceeded its liabilities at June 30, 2016 and 2015. All of the Plan's net position is restricted to meet the Retirement System's ongoing obligation to Plan participants and their beneficiaries.

The Plan's net position as of June 30, 2016, 2015, and 2014 are represented in the table below:

Net Position Summary – June 30, 2016, 2015, and 2014

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Other assets	\$ 164,233	\$ 305,801	\$ 477,213
Investments at fair value	20,980,136	21,540,021	20,735,639
Total assets	<u>21,144,369</u>	<u>21,845,822</u>	<u>21,212,852</u>
Total liabilities	<u>989,866</u>	<u>1,417,753</u>	<u>1,292,245</u>
Net position	<u>\$ 20,154,503</u>	<u>\$ 20,428,069</u>	<u>\$ 19,920,607</u>

As of June 30, 2016, the Plan's total net position held in trust for pension benefits decreased by \$273,566 or 1.3% for the year, primarily due to investment returns that did not offset the net difference between contributions received by the Plan and benefit payments made from the Plan. Payables to brokers decreased by \$266,557 and payables to borrowers of securities decreased by \$138,010 due to the timing of investment trades and lending activities.

As of June 30, 2015, the Plan's total net position held in trust for pension benefits increased by \$507,462 or 2.5% for the year, primarily due to positive investment returns. Payables to brokers increased by \$17,011 and payables to borrowers of securities increased by \$88,660 due to the timing of investment trades and lending activities.

The Retirement Board believes that the Plan remains in a strong financial position to meet its obligations to the Plan members and beneficiaries. FY 2015-2016 saw the arrival of a slowdown in the near record climb of U.S. Equities. The S&P advanced 4.0%, its lowest return since falling 26.2% in FY 2008-2009. On a positive front, U.S. unemployment continued to fall, reaching 4.9% by fiscal year end – down from 10% in late 2009. At the same time, the U.S. labor force participation rate climbed – an optimistic sign that previously inactive workers are returning to the workforce. The U.S. also continued to see growth in hourly earnings, which climbed 2.6% during the 2015-2016 fiscal year. U.S. consumer confidence remained near recent highs and spending levels continue to increase – even when adjusted for inflation. As a result of these and other factors, the Federal Reserve began to signal that the accommodative fiscal policy is changing as the Open Market Committee increased the Federal Funds rate by 25 basis points in December 2015 – the first rate change since December 2008. Outside the United States, economic growth remained muted. In Western Europe, unemployment was over 10% while gross domestic product (“GDP”) growth was flat. The economic bright spots were Germany and the United Kingdom – with unemployment rates more in-line with the U.S. The European Central Bank continued to provide a supportive fiscal policy (via quantitative easing). Also roiling the European market was the U.K. vote to exit (“BREXIT”) the European Union in June 2016. Both policy and economic analysts continue to debate the long-run impact that BREXIT will have on U.K. and EU GDP. Emerging economies continued to struggle with low commodity prices (crude oil fell by more than 20%). China, the largest emerging economy, saw exports fall 4.1% on weak demand from developed markets (U.S. and EU). GDP growth rates in many emerging markets remain near recent lows.

As fiduciaries to the Plan members and beneficiaries, the Retirement Board, Retirement System staff, and our investment consultants continuously monitor the Plan's investment strategies, which comply with a “prudent expert” standard, to secure and maintain the sustainability of the Plan.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM
Management's Discussion and Analysis – Unaudited
Years Ended June 30, 2016 and 2015
(Dollar amounts in thousands)

Highlights of Changes in Net Position – Years ended June 30, 2016, 2015, and 2014
(Dollars in thousands)

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Additions:			
Member contributions	\$ 322,764	\$ 301,682	\$ 289,020
Employer contributions	526,805	592,643	532,882
Interest	188,292	209,520	177,425
Dividends	219,529	214,636	195,503
Net appreciation in fair value of investments	(216,852)	378,519	2,844,279
Securities lending income	7,562	4,869	4,871
Investment expenses	(47,026)	(44,911)	(47,599)
Securities lending borrower rebates and expenses	(1,315)	796	952
Total additions	<u>999,759</u>	<u>1,657,754</u>	<u>3,997,333</u>
Deductions:			
Benefits	1,243,260	1,118,691	1,062,229
Refunds of contributions	12,886	12,339	10,297
Administrative expenses	16,079	18,108	14,550
Other administrative expenses - OPEB	1,100	1,154	1,195
Total deductions	<u>1,273,325</u>	<u>1,150,292</u>	<u>1,088,271</u>
Change in net position	(273,566)	507,462	2,909,062
Net position - beginning of the year	20,428,069	19,920,607	17,011,545
Net position - end of the year	<u>\$ 20,154,503</u>	<u>\$ 20,428,069</u>	<u>\$ 19,920,607</u>

Fiscal Year 2016

- Member contributions for the year ended June 30, 2016 increased by \$21,082 or 7.0% from the prior year. This increase is primarily a result of increases in the number of active employees contributing to the Plan and in employee contribution rates, which ranged from 7.5% - 13.0% in fiscal year 2015-16.
- In order to maintain the fiscal soundness of the Plan, \$526,805 in required employer contributions were made during the year ended June 30, 2016. The decrease of \$65,838 in required employer contributions reflect a decrease in the employer contribution rates, which ranged from 18.30% to 22.80% in fiscal year 2015-16 and 22.26% to 26.76% in fiscal year 2014-15.
- Net investment income decreased by \$613,239 from the prior year. The majority of the decrease is attributed to the \$595,371 decline in net appreciation in fair value of investments primarily due to lower investment returns in all of the asset classes that the Retirement System invests in. Interest income decreased by \$21,228, due mainly to the domestic fixed income market.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Management's Discussion and Analysis – Unaudited

Years Ended June 30, 2016 and 2015

(Dollar amounts in thousands)

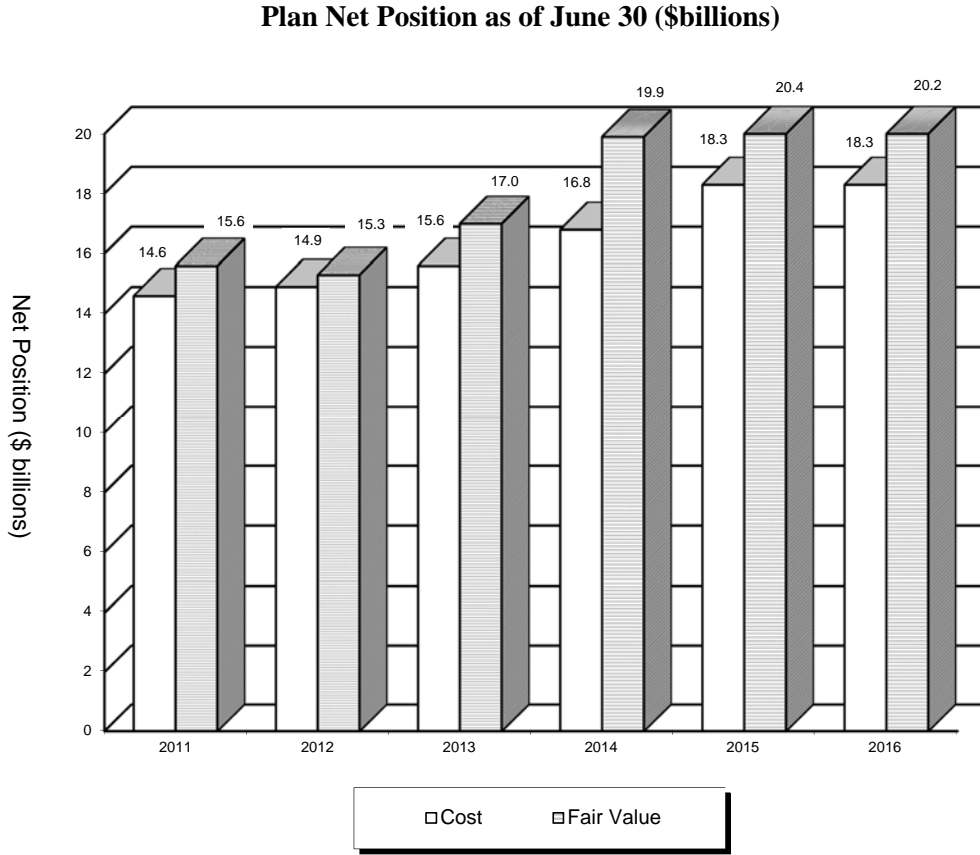
- Benefit payments to Plan participants increased by \$124,569 or 11.1%, primarily due to retroactive Supplemental COLAs paid as of a result of the Court decision that removed the “fully funded” requirement for SFERS members who retired after November 6, 1996 and were hired before January 7, 2012.
- Accrued DROP retirement benefits decreased by \$878 reflecting the wind down of the program as a result of the program being closed to new participants as of July 1, 2011.

Fiscal Year 2015

- Member contributions for the year ended June 30, 2015 increased by \$12,662 or 4.4% from the prior year. This increase is primarily a result of increases in the number of active employees contributing to the Plan and in employee contribution rates, which ranged from 7.5% - 13.0% in fiscal year 2014-15.
- In order to maintain the fiscal soundness of the Plan, \$592,643 in required employer contributions were made during the year ended June 30, 2015. The increase of \$59,761 in required employer contributions reflect an increase in the employer contribution rates, which ranged from 22.26% to 26.76% in fiscal year 2014-15 and 20.32% to 24.32% in fiscal year 2013-14.
- Net investment income decreased by \$2,412,002 from the prior year. The majority of the decrease is attributed to the \$2,465,760 decline in net appreciation in fair value of investments primarily due to lower investment returns in all of the asset classes that the Retirement System invests in. Interest income increased by \$32,095, due mainly to the domestic fixed income market.
- Benefit payments to Plan participants increased by \$56,462 or 5.3%, which is primarily due to an increase in service retirement benefits as a result of increased average benefit payments.
- Accrued DROP retirement benefits decreased by \$1,605 reflecting the wind down of the program as a result of the program being closed to new participants as of July 1, 2011.

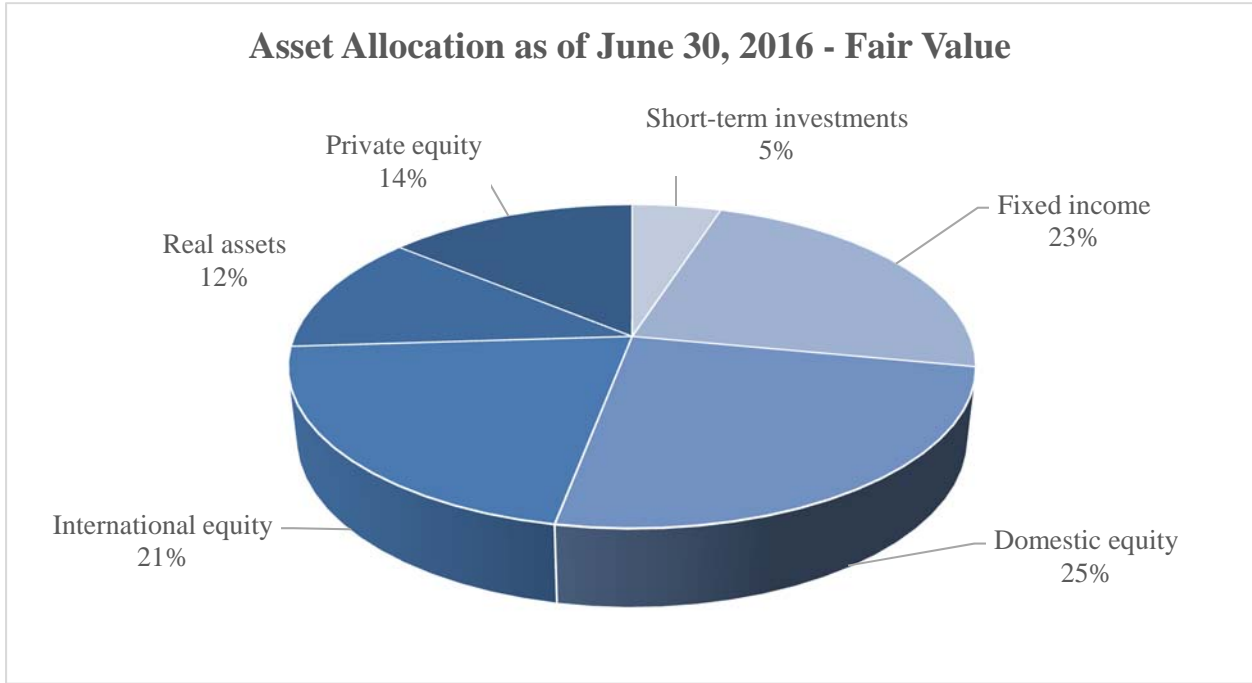
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Management's Discussion and Analysis – Unaudited
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(Dollar amounts in thousands)

Plan net position as of June 30, 2011 through 2016 expressed at cost and fair value are represented in the chart below:

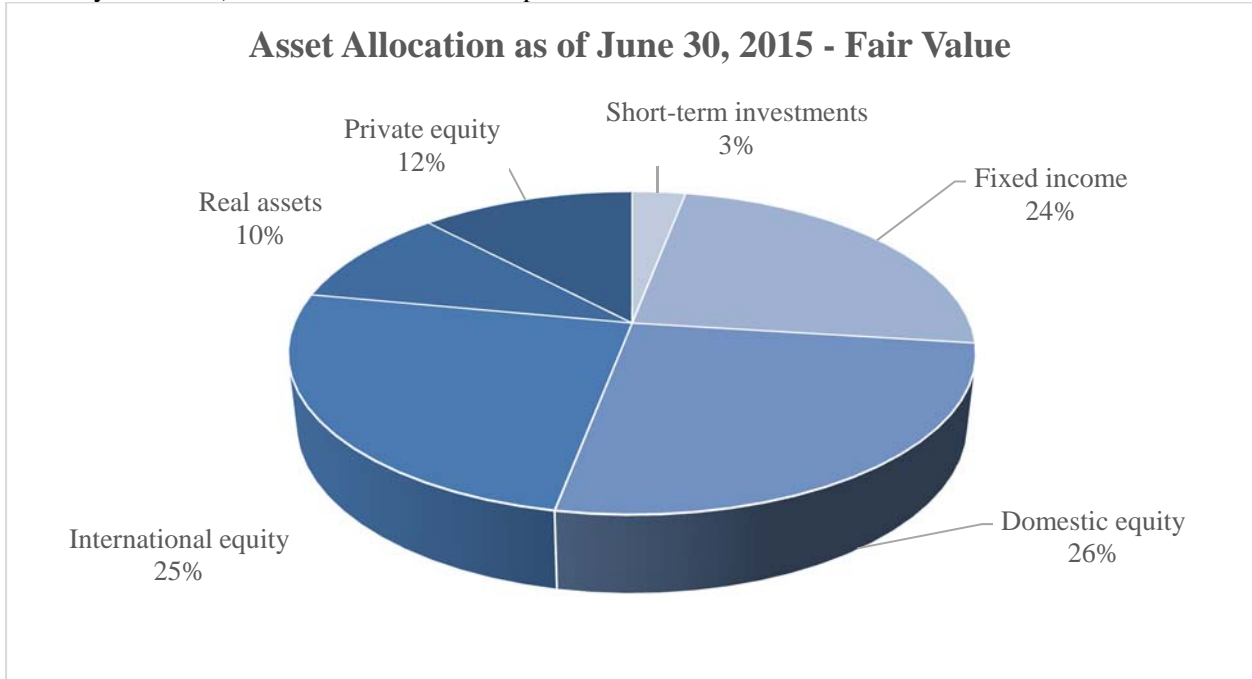


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Management's Discussion and Analysis – Unaudited
Years Ended June 30, 2016 and 2015
(Dollar amounts in thousands)

The asset allocation at fair value based on holdings (excluding securities lending collateral and foreign currency contracts) as of June 30, 2016 is represented in the chart below:



The asset allocation at fair value based on holdings (excluding securities lending collateral and foreign currency contracts) as of June 30, 2015 is represented in the chart below:



SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM
Management's Discussion and Analysis – Unaudited
Years Ended June 30, 2016 and 2015
(Dollar amounts in thousands)

Currently Known Facts and Events Affecting Next Year

The Retirement System's funding objective is to meet long-term benefit obligations through contributions and investment income. The Retirement Board believes that the Retirement System remains in a strong financial position to meet its obligations to Plan participants and beneficiaries.

Requests for information

This financial report is designed to provide a general overview of the Retirement System's finances for the years ended June 30, 2016 and 2015. Questions regarding any of the information provided in this report or requests for additional financial information should be addressed to:

Jay Huish, Executive Director
San Francisco City and County Employees' Retirement System
1145 Market Street – 5th floor
San Francisco, CA 94103

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM
Statements of Plan Net Position
June 30, 2016 and 2015
(In thousands)

	<u>2016</u>	<u>2015</u>
Assets:		
Deposits	\$ 43,521	\$ 31,969
Contributions receivable - members	10,908	8,078
Investment income receivable:		
Interest	21,831	25,582
Dividends	20,643	13,358
Securities lending	641	613
Receivable from brokers, general partners, and others	66,689	226,201
Investments at fair value:		
Short-term investments	1,009,676	656,185
City investment pool	6,656	-
Debt securities:		
U.S. government and agency securities	1,648,271	1,074,204
Other debt securities	3,068,745	3,892,924
Equity securities:		
Domestic	4,970,838	5,320,353
International	4,304,025	5,134,177
Real assets	2,341,500	1,975,926
Private equity	2,750,619	2,484,299
Foreign currency contracts, net	14,125	722
Invested securities lending collateral	865,681	1,001,231
Total investments	<u>20,980,136</u>	<u>21,540,021</u>
Total assets	<u>21,144,369</u>	<u>21,845,822</u>
Liabilities:		
Payable to brokers	107,444	374,001
Deferred retirement option program	613	1,491
Other	18,273	40,715
Payable to borrowers of securities	863,536	1,001,546
Total liabilities	<u>989,866</u>	<u>1,417,753</u>
Plan net position – restricted for pension benefits	<u>\$ 20,154,503</u>	<u>\$ 20,428,069</u>

See accompanying notes to financial statements.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM
Statements of Changes in Plan Net Position
Years Ended June 30, 2016 and 2015
(In thousands)

	<u>2016</u>	<u>2015</u>
Additions:		
Member contributions		
Miscellaneous	\$ 266,929	\$ 248,084
Police	32,345	30,977
Fire	23,490	22,621
Total member contributions	<u>322,764</u>	<u>301,682</u>
Employer contributions		
Miscellaneous	442,184	494,353
Police	49,164	57,950
Fire	35,457	40,340
Total employer contributions	<u>526,805</u>	<u>592,643</u>
Investment income (expenses)		
Interest	188,292	209,520
Dividends	219,529	214,636
Net appreciation (depreciation) in fair value of investments	(216,852)	378,519
Securities lending income	7,562	4,869
Investment expenses	(47,026)	(44,911)
Securities lending borrower rebates and expenses	(1,315)	796
Net investment income	<u>150,190</u>	<u>763,429</u>
Total additions	<u>999,759</u>	<u>1,657,754</u>
Deductions:		
Benefits	1,243,260	1,118,691
Refunds of contributions	12,886	12,339
Administrative expenses	16,079	18,108
Other administrative expenses - other postemployment benefits	1,100	1,154
Total deductions	<u>1,273,325</u>	<u>1,150,292</u>
Net increase (decrease) in net position	(273,566)	507,462
Plan net position – restricted for pension benefits		
Beginning of year	<u>20,428,069</u>	<u>19,920,607</u>
End of year	<u>\$ 20,154,503</u>	<u>\$ 20,428,069</u>

See accompanying notes to financial statements.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Notes to Financial Statements Years Ended June 30, 2016 and 2015 (Dollar amounts in thousands)

(1) Plan Description

(a) General

The San Francisco City and County Employees' Retirement System (the Retirement System) administers a cost-sharing multiple-employer defined benefit pension plan (the Plan) established to provide pension benefits for substantially all employees of the City and County of San Francisco (the City and County), certain classified and certificated employees of the Community College and Unified School Districts, and San Francisco Trial Court employees other than judges. The Retirement System provides service retirement, disability, and death benefits based on specified percentages of defined final average monthly salary and annual cost-of-living adjustments after retirement. While the Plan is not subject to the provisions of the Employee Retirement Income Security Act of 1974 (ERISA), it is a tax-qualified plan under Internal Revenue Code provisions. The City and County Charter (the Charter) and the Administrative Code are the authorities that establish and amend the benefit provisions and employer and member obligations to the Plan.

The Retirement System is considered to be a part of the City and County's financial reporting entity and is included in the City and County's basic financial statements as a pension trust fund. The financial statements of the Retirement System are intended to present only the plan net position and changes in plan net position of the Retirement System. They do not purport to, and do not, present fairly the financial position of the City and County as of June 30, 2016 and 2015, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America. The City and County's basic financial statements can be obtained from City Hall, Room 316, 1 Dr. Carlton B. Goodlett Place, San Francisco, CA 94102.

The Retirement System is administered by the Executive Director, an employee of the City and County, in accordance with the provisions of the Charter and Administrative Code, and the policies and regulations of the Retirement Board. The Retirement Board is composed of seven members: three members elected by the active and retired members of the Retirement System; three members appointed by the Mayor in accordance with Section 12.100 of the San Francisco City Charter; and one member of the Board of Supervisors appointed by the President of the Board of Supervisors.

The Retirement System pays benefits according to the category of employment and the type of benefit coverage provided by the City and County. The four main categories of Plan membership are:

- **Miscellaneous Non-Safety Members** – staff, operational, supervisory, and all other eligible employees who are not in special membership categories.
- **Sheriff's Department and Miscellaneous Safety Members** – sheriffs assuming office on and after January 7, 2012, and undersheriffs, deputized personnel of the sheriff's department, and miscellaneous safety employees hired on and after January 7, 2012.
- **Firefighter Members** – firefighters and other employees whose principal duties are in fire prevention and suppression work or who occupy positions designated by law as firefighter member positions.
- **Police Members** – police officers and other employees whose principal duties are in active law enforcement or who occupy positions designated by law as police member positions.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Notes to Financial Statements
Years Ended June 30, 2016 and 2015
(Dollar amounts in thousands)

(b) Service Retirement

Miscellaneous Non-Safety Members who became members prior to July 1, 2010 qualify for a service retirement benefit if they are at least 50 years old and have at least 20 years of credited service or if they are at least 60 years old and have at least 10 years of credited service. The service retirement benefit is calculated using the member's final compensation (highest one-year average monthly compensation) multiplied by the member's years of credited service times the member's age factor up to a maximum of 75% of the member's final compensation.

Miscellaneous Non-Safety Members who became members on or after July 1, 2010 and prior to January 7, 2012 qualify for a service retirement benefit if they are at least 50 years old and have at least 20 years of credited service or if they are at least 60 years old and have at least 10 years of credited service. The service retirement benefit is calculated using the member's final compensation (highest two-year average monthly compensation) multiplied by the member's years of credited service times the member's age factor up to a maximum of 75% of the member's final compensation.

Miscellaneous Non-Safety Members who became members on or after January 7, 2012 qualify for a service retirement benefit if they are at least 53 years old and have at least 20 years of credited service or if they are at least 60 years old and have at least 10 years of credited service. The service retirement benefit is calculated using the member's final compensation (highest three-year average monthly compensation) multiplied by the member's years of credited service times the member's age factor up to a maximum of 75% of the member's final compensation.

Sheriff's Department Members and Miscellaneous Safety Members who were hired on or after January 7, 2012 qualify for a service retirement benefit if they are at least 50 years old and have at least 5 years of credited service. The service retirement benefit is calculated using the member's final compensation (highest three-year average monthly compensation) multiplied by the member's years of credited service times the member's age factor up to a maximum of 90% of the member's final compensation.

Firefighter Members and Police Members who became members of the Plan before November 2, 1976 qualify for a service retirement benefit if they are at least 50 years old and have at least 25 years of credited service. The service retirement benefit is calculated using the member's final compensation (monthly salary earnable at the rank or position the member held for at least one year immediately prior to retiring) multiplied by the member's years of credited service times the member's age factor up to a maximum of 90% of the member's final compensation.

Firefighter Members and Police Members who became members of the Plan on or after November 2, 1976 and prior to July 1, 2010 qualify for a service retirement benefit if they are at least 50 years old and have at least 5 years of credited service. The service retirement benefit is calculated using the member's final compensation (highest one-year average monthly compensation) multiplied by the member's years of credited service times the member's age factor up to a maximum of 90% of the member's final compensation.

Firefighter Members and Police Members who became members of the Plan on or after July 1, 2010 and prior to January 7, 2012 qualify for a service retirement benefit if they are at least 50 years old and have at least 5 years of credited service. The service retirement benefit is calculated using the member's final compensation (highest two-year average monthly

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Notes to Financial Statements Years Ended June 30, 2016 and 2015 (Dollar amounts in thousands)

compensation) multiplied by the member's years of credited service times the member's age factor up to a maximum of 90% of the member's final compensation.

Firefighter Members and Police Members who became members of the Plan on or after January 7, 2012 qualify for a service retirement benefit if they are at least 50 years old and have at least 5 years of credited service. The service retirement benefit is calculated using the member's final compensation (highest three-year average monthly compensation) multiplied by the member's years of credited service times the member's age factor up to a maximum of 90% of the member's final compensation.

(c) Disability Retirement

Miscellaneous Non-Safety Members are eligible to apply for a disability retirement benefit, regardless of age, when they have 10 or more years of credited service and they sustain an injury or illness that prevents them from performing their duties. The disability retirement benefit is calculated using the member's average final compensation multiplied by the member's years of credited service times the disability factor (1.8) up to a maximum of 75% of average final compensation.

Firefighter Members, Police Members, Sheriff Members, and Miscellaneous Safety Members are eligible to apply for an industrial disability retirement benefit from their first day on the job in firefighter or police service if their disability is caused by an illness or injury that they receive while performing their duties. The industrial disability retirement benefit is based on the member's average final compensation multiplied by the permanent disability rating (from 50% to 90%) or the member's service retirement benefit if the member is eligible for a service retirement.

Firefighter Members, Police Members, Sheriff Members, and Miscellaneous Safety Members are eligible to apply for an ordinary disability retirement benefit, regardless of age, when they have 10 or more years of credited service and they sustain an injury or illness that is not caused by their work, but that prevents them from performing their duties. The disability retirement benefit is calculated using 1.5% of the member's average final compensation multiplied by years of credited service subject to a minimum of 33.3% and a maximum (75% to 90%).

(d) Separation and Death Benefits

Separation from Employment

Upon separation from City employment, **Miscellaneous Non-Safety Members** may either elect to withdraw their accumulated contributions from the Plan or, if they have 5 or more years of credited service, elect to leave their accumulated contributions in the Plan and receive a vesting benefit that is first payable at or after age 50 for members hired prior to January 7, 2012 or at or after age 53 for members hired on or after January 7, 2012. Miscellaneous members hired before November 2, 1976 need 10 years of credited service to elect the vesting option.

Upon separation from City employment, **Firefighter Members, Police Members, Sheriff Members, and Miscellaneous Safety Members** may either elect to withdraw their accumulated contributions from the Plan or, if they have 5 or more years of credited service, elect to leave their accumulated contributions in the Plan and receive a deferred benefit that is first payable at or after age 50.

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Death Benefits Prior to Retirement

Generally, upon the death of an active employee who is eligible for a service retirement, the Retirement System provides continuation benefits to a qualified surviving spouse or qualified domestic partner equal to 50% to 100% of the member's retirement allowance that the member would have received had he or she retired on the date of death.

For qualified surviving spouses and qualified domestic partners of **Firefighter Members, Police Members, Sheriff Members, and Miscellaneous Safety Members** who die prior to becoming eligible for service retirement and whose death is due to an injury received in or illness caused by the performance of duty, salary continuation is provided to the qualified survivor until such time as the member would have qualified for service retirement had he or she lived at which time a continuation benefit equal to 100% of the member's service retirement allowance is provided to the qualified survivor.

A lump sum death payment equal to 6 months' earnable salary plus the member's accumulated contributions is provided upon the death of an active employee not yet eligible for a service retirement to the member's named beneficiary or estate.

Death Benefits after Retirement

Generally, upon the death of a retired member, the Retirement System provides continuation benefits to a qualified surviving spouse or qualified domestic partner equal to 50% to 100% of the member's retirement allowance as of the date of death.

(e) **Cost of Living Adjustments (COLA)**

Basic COLA

Miscellaneous Non-Safety Members receive a benefit adjustment each July 1 equal to the percentage increase or decrease in the Consumer Price Index (CPI) rounded to the nearest 1%, to a maximum of 2% of the member's previous June 30 retirement benefit. If the CPI decreases in a particular year, however, the negative adjustment cannot reduce a member's monthly retirement benefit below the initial pension amount.

Firefighter Members and Police Members who became members of the Plan before November 2, 1976 receive a benefit adjustment each July 1 equal to 50% of the actual dollar or percentage increase or decrease in the salary of the rank or position on which the member's retirement benefit is based. Although decreases are possible in a given year, a negative adjustment cannot reduce a member's monthly benefit below the initial pension amount.

Firefighter Members and Police Members who became members of the Plan on or after November 2, 1976 and Sheriff Members and Miscellaneous Safety Members receive a benefit adjustment each July 1 equal to the percentage increase or decrease in the CPI rounded to the nearest 1%, to a maximum of 2% of the member's previous June 30 retirement benefit. If the CPI decreases in a particular year; however, the negative adjustment cannot reduce a member's monthly retirement benefit below the initial pension amount.

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Supplemental COLA

The Plan provides for a Supplemental COLA in years when there are sufficient “excess” investment earnings in the Plan. Effective July 1, 2012, voters approved changes in the criteria for payment of the Supplemental COLA benefit. Certain provisions of the voter approved proposition were challenged in the Courts. A decision by the California Courts modified the interpretation of the proposition. Effective July 1, 2012, SFERS members who retired before November 6, 1996 will receive a Supplemental COLA when there are sufficient “excess” investment earnings in the Plan and the Plan is also fully funded on a market value of assets basis. The “full funding” requirement does not apply to SFERS members who retired after November 6, 1996 and were hired before January 7, 2012. For members who were hired before January 7, 2012, all Supplemental COLAs paid to them in retirement benefits will continue into the future even where an additional Supplemental COLA is not payable in any given year. For members who are hired on and after January 7, 2012, a Supplemental COLA will be paid to retirees when there are sufficient “excess” investment earnings in the Plan and the Plan is also fully funded on a market value of assets basis. For this group, Supplemental COLAs will not be permanent adjustments to retirement benefits. In years when a Supplemental COLA is not paid, all previously paid Supplemental COLAs will expire.

(f) Deferred Retirement Option Program

In February 2008, the voters of the City and County approved a Charter amendment to provide a Deferred Retirement Option Program (DROP) for certain Police members of the Plan to be effective July 1, 2008. An eligible police officer could elect to participate in DROP for a specified period of time up to a maximum of three years depending on the rank of the police officer. While participating in DROP, the police officer continues to work and receive pay as a police officer and accrues monthly DROP distributions posted to a nominal account maintained by the Retirement System. The monthly DROP distribution is equal to the participant’s monthly service retirement allowance calculated as of the participant’s entry into DROP. Interest at an annual effective rate of 4% and applicable COLAs are posted to the participant’s DROP account during participation in DROP. Upon exiting from DROP, the participant receives a lump sum distribution from his or her DROP account and begins to receive a monthly service retirement allowance calculated using age, covered compensation, and service frozen as of the date of his or her entry into DROP. DROP was closed to new applicants on June 30, 2011. The Retirement System held \$613 and \$1,491 pursuant to the DROP as of June 30, 2016 and 2015, respectively.

(g) Membership

Membership of the Retirement System consisted of the following as of June 30, 2016:

	Police	Fire	Miscellaneous and Sheriff	Total
Retirees and beneficiaries				
currently receiving benefits	2,639	2,069	23,595	28,303
Active members	2,260	1,572	29,598	33,430
Terminated members entitled to but not yet receiving benefits	131	71	6,615	6,817
Total	5,030	3,712	59,808	68,550

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Membership of the Retirement System consisted of the following as of June 30, 2015:

	Police	Fire	Miscellaneous and Sheriff	Total
Retirees and beneficiaries				
currently receiving benefits	2,587	2,067	22,823	27,477
Active members	2,120	1,486	27,233	30,839
Terminated members entitled to but not yet receiving benefits	148	74	6,897	7,119
Total	4,855	3,627	56,953	65,435

(2) Summary of Significant Accounting Policies

(a) Basis of Presentation

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

Member contributions are recognized in the period in which the contributions are due. Employer contributions and member contributions made by the employer to the Plan are recognized when due pursuant to legal requirements. Benefits and refunds are recognized when currently due and payable in accordance with the terms of the Plan.

(b) Investments

Investments are reported at fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Securities that do not have an established market are reported at estimated fair value derived from third party pricing services. Purchases and sales of investments are recorded on a trade date basis.

The fair values of the Retirement System's real estate investments are based on net asset values provided by the investment managers. Partnership financial statements are audited annually as of December 31 and net asset values are adjusted monthly or quarterly for cash flows to/from the Retirement System, investment earnings and expenses, and changes in fair value. The Retirement System has established leverage limits for each investment style based on the risk/return profile of the underlying investments. The leverage limits for core and value-added real estate investments are 40% and 65%, respectively. The leverage limits for high return real estate investments depend on each specific offering. Outstanding mortgages for the Retirement System's real estate investments were \$492,212, including \$26,665 in recourse debt, as of June 30, 2016, and \$639,620, including \$51,719 in recourse debt, as of June 30, 2015. The underlying real estate holdings are valued periodically based on appraisals performed by independent appraisers in accordance with Uniform Standards of Professional Appraisal Practice (USPAP). Such fair value estimates involve subjective judgments of unrealized gains and losses, and the actual market price of the real estate can only be determined by negotiation between independent third parties in a purchase and sale transaction.

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Notes to Financial Statements **Years Ended June 30, 2016 and 2015** (Dollar amounts in thousands)

Private equity investments represent the Retirement System's interest in limited partnerships. The fair values of private equity investments are based on net asset values provided by the general partners. Partnership financial statements are audited annually as of December 31 and net asset values are adjusted monthly or quarterly for cash flows to/from the Retirement System, investment earnings and changes in fair value. Such fair value estimates involve subjective judgments of unrealized gains and losses, and the actual market price of the investments can only be determined by negotiation between independent third parties in a purchase and sale transaction.

The Charter and Retirement Board policies permit the Retirement System to use investments of 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. The collateral may consist of cash or non-cash; non-cash collateral is generally U.S. Treasuries or other U.S. government obligations. The Retirement System's securities custodian is the agent in lending the Plan's domestic securities for collateral of 102% and international securities for collateral of 105%. Contracts with the lending agent require them to indemnify the Retirement System if the borrowers fail to return the securities (and if the collateral were inadequate to replace the securities lent) or fail to pay the Retirement System for income distributions by the securities' issuers while the securities are on loan. Non-cash collateral cannot be pledged or sold unless the borrower defaults, and therefore, is not reported in the Retirement System's financial statements.

All securities loans can be terminated on demand by either the Retirement System or the borrower, although the average term of the loans as of June 30, 2016 and 2015 was 78 days and 61 days, respectively. All cash collateral received was invested in a separately managed account by the lending agent using investment guidelines developed and approved by the Retirement System. As of June 30, 2016 and 2015, the weighted average maturity of the reinvested cash collateral account was 25 days and 24 days, respectively. The term to maturity of the loaned securities is generally not matched with the term to maturity of the investment of the said collateral. Cash collateral may also be invested separately in term loans, in which case the maturity of the loaned securities matches the term of the loan.

Cash collateral invested in the separate account managed by the lending agent is reported at fair value. Payable to borrowers of securities in the statements of plan net position represents the cash collateral received from borrowers. Additionally, the income and costs of securities lending transactions, such as borrower rebates and fees, are recorded respectively as revenues and expenses in the statements of changes in plan net position.

(c) Administrative Expenses

All costs to administer the Retirement System are borne by the Retirement System.

(d) Use of Estimates

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

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Notes to Financial Statements Years Ended June 30, 2016 and 2015 (Dollar amounts in thousands)

(e) Implementation of GASB Statement

The Retirement System adopted GASB Statement No. 72, *Fair Value Measurement and Application*. This Statement addresses accounting and financial reporting issues related to fair value measurements. GASB Statement No. 72 requires the Retirement System to use valuation techniques that are appropriate under the circumstances and for which sufficient data are available to measure fair value. The techniques should be consistent with one or more of the following approaches: the market approach, the cost approach, or the income approach. This statement establishes a three-tier hierarchy of inputs to valuation techniques used to measure fair value.

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly.
- Level 3 inputs are all inputs that are unobservable.

The Retirement System's implementation of this statement effective July 1, 2015 has no material impact on the financial statements. The additional disclosures and related notes are presented in Note 5.

(3) Deposits

Deposits are carried at cost, which approximates fair value. Deposits in bank accounts were \$43,521 and \$31,969 as of June 30, 2016, and 2015, respectively. Deposit and investment risk disclosures for the pooled funds with the City and County Treasurer are discussed in the City and County's basic financial statements.

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government may not be able to recover its deposits or may not be able to recover collateral securities that are in the possession of an outside party. The Retirement System does not have a specific policy addressing custodial credit risk for deposits. As of June 30, 2016 and 2015, the Retirement System's deposits in bank accounts were not exposed to custodial credit risk.

(4) Investments

The Retirement System's investments are invested pursuant to investment policy guidelines as established by the Retirement Board. The objective of the policy is to maximize the expected return of the fund at an acceptable level of risk. The Retirement Board has established percentage guidelines for types of investments to ensure the portfolio is diversified.

Investment managers are required to diversify by issue, maturity, sector, coupon, and geography. Investment managers retained by the Retirement System follow specific investment guidelines and are evaluated against specific market benchmarks that represent their investment style. Any exemption from general guidelines requires approval from the Retirement Board. The Retirement System invests in securities with contractual cash flows, such as asset backed securities, commercial mortgage backed securities, and collateralized mortgage obligations. The value, liquidity, and related income of these securities are sensitive to changes in economic conditions, including real estate values, delinquencies or defaults, or both, and may be affected by shifts in the market's perception of the issuers and changes in interest rates.

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(Dollar amounts in thousands)

The investment policy permits investments in domestic and international debt and equity securities, real estate, securities lending, foreign currency contracts, derivative instruments, and private equity investments, which include investments in a variety of commingled partnership vehicles.

The Retirement Board's asset allocation policies for the years ended June 30, 2016 and 2015 are as follows:

<u>Asset Class</u>	<u>Target Allocation through January 2015</u>	<u>Target Allocation since February 2015</u>
Global Equity	47.0%	40.0%
Fixed Income	25.0%	20.0%
Private Equity	16.0%	18.0%
Real Assets	12.0%	17.0%
Hedge Funds/Absolute Return	0%	5.0%
	<u>100.0%</u>	<u>100.0%</u>

The Retirement System is not directly involved in repurchase or reverse repurchase agreements. However, external investment managers retained by the Retirement System may employ repurchase arrangements if the securities purchased or sold comply with the manager's investment guidelines. The Retirement System monitors the investment activity of its investment managers to ensure compliance with guidelines. In addition, the Retirement System's securities lending cash collateral separately managed account is authorized to use repurchase arrangements. As of June 30, 2016 and 2015, \$419,000 (or 48.4% of reinvested cash collateral) and \$503,000 (or 50.2% of reinvested cash collateral), respectively, consisted of such agreements.

The Retirement System maintains its operating fund cash in the City and County's investment pool. The City and County's pool is invested pursuant to investment policy guidelines established by the City Treasurer, subject to review by the Treasury Oversight Committee. The Treasury Oversight Committee, established under California Government Code Sections 27130 to 27137, is composed of various City and County officials and representatives of agencies with large cash balances in the pool. The policy addresses soundness of financial institutions in which the City and County will deposit funds, types of investment instruments as permitted by the California Government Code, and the percentage of the portfolio which may be invested in certain instruments with longer terms to maturity. The provisions of the City and County's investment policy also address interest rate risk, credit risk, and concentration of credit risk and provide for additional restrictions related to investments. The notes to the basic financial statements of the City and County provide more detailed information concerning deposit and investment risks associated with the City and County's pool of cash and investments at June 30, 2016 and 2015.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Notes to Financial Statements
Years Ended June 30, 2016 and 2015

(Dollar amounts in thousands)

(a) Interest Rate Risk

Interest rate risk is the risk that changes in interest rates may adversely affect the fair value of an investment. The Retirement System does not have a specific policy to manage interest rate risk.

Below are tables depicting the segmented time distribution for fixed income investments based upon the expected maturity (in years) as of June 30, 2016 and 2015.

Investments at Fair Value as of June 30, 2016

Investment Type	Fair Value	Maturities			
		Less than 1 year	1-5 years	6-10 years	10+ years
Asset Backed Securities	\$ 178,327	\$ -	\$ 57,102	\$ 11,880	\$ 109,345
Bank Loans	139,680	1,240	106,587	31,853	-
City Investment Pool	6,656	4,119	2,537	-	-
Collateralized Bonds	167	-	-	-	167
Commercial Mortgage-Backed	438,764	6,254	6,708	5,558	420,244
Commingled and Other					
Fixed Income Funds	231,780	264,114	569	51	(32,954)
Corporate Bonds	1,627,327	580,310	443,592	437,779	165,646
Corporate Convertible Bonds	293,360	3,460	197,038	35,709	57,153
Foreign Currencies and Cash Equivalents	144,456	144,456	-	-	-
Government Agencies	971,329	952,962	368	-	17,999
Government Bonds	589,416	150,467	278,583	43,497	116,869
Government Mortgage-					
Backed Securities	145,030	-	10,819	-	134,211
Index Linked Government Bonds	1,359	-	-	1,243	116
Mortgages	-	-	-	-	-
Municipal/Provincial Bonds	40,049	-	9,182	1,628	29,239
Non-Government Backed					
Collateralized Mortgage Obligations	59,543	-	2,376	2,033	55,134
Options	(64)	(64)	-	-	-
Short Term Investment Funds	865,219	865,219	-	-	-
Swaps	950	(78)	831	197	-
Total	\$ 5,733,348	\$ 2,972,459	\$ 1,116,292	\$ 571,428	\$ 1,073,169

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Notes to Financial Statements
Years Ended June 30, 2016 and 2015

(Dollar amounts in thousands)

Investments at Fair Value as of June 30, 2015

Investment Type	Fair Value	Maturities			
		Less than 1 year	1-5 years	6-10 years	10+ years
Asset Backed Securities	\$ 140,493	\$ 2,605	\$ 53,240	\$ 18,596	\$ 66,052
Bank Loans	115,885	3,192	82,628	30,065	-
Collateralized Bonds	969	-	-	-	969
Commercial Mortgage-Backed	647,322	-	16,138	6,330	624,854
Commingled and Other					
Fixed Income Funds	405,805	396,657	574	54	8,520
Corporate Bonds	1,937,753	690,752	337,996	542,131	366,874
Corporate Convertible Bonds	308,367	15,824	181,592	44,384	66,567
Foreign Currencies and Cash Equivalents	332,610	332,610	-	-	-
Government Agencies	335,438	317,253	9,861	6,338	1,986
Government Bonds	517,527	16,256	323,157	119,474	58,640
Government Mortgage-					
Backed Securities	333,078	108,159	5,260	12,698	206,961
Index Linked Government Bonds	15,287	-	8,980	2,473	3,834
Mortgages	5	5	-	-	-
Municipal/Provincial Bonds	45,922	-	1,004	4,070	40,848
Non-Government Backed					
Collateralized Mortgage Obligations	162,844	-	1,894	7,318	153,632
Options	18	19	(1)	-	-
Short Term Investment Funds	323,267	323,267	-	-	-
Swaps	723	(2)	785	(17)	(43)
Total	\$ 5,623,313	\$ 2,206,597	\$ 1,023,108	\$ 793,914	\$ 1,599,694

(b) Credit Risk – Investments

Credit risk is the risk that an issuer or other counterparty to an investment may not fulfill its obligations. Fixed income investment managers retained by the Retirement System follow specific investment guidelines and are evaluated against specific market benchmarks that represent their investment style. Fixed income managers typically are limited within their portfolios to no more than 5% exposure in any single security, with the exception of United States Treasury and government agency securities. The Retirement System's credit risk policy is embedded in the individual investment manager agreements as prescribed and approved by the Retirement Board.

Investments are classified and rated using the lower of (1) Standard & Poor's (S&P) rating or (2) Moody's Investors Service (Moody's) rating corresponding to the equivalent S&P rating. If only a Moody's rating is available, the rating equivalent to S&P is used for the purpose of this disclosure.

The credit rating of the United States remains a point of concern for investors. In 2011, S&P lowered the credit rating for U.S. long-term debt to AA+ from AAA and continues to maintain that posture. Moody's and Fitch, the other two large credit rating agencies, continue to maintain a AAA rating for U.S. long-term debt, although Fitch placed the U.S. on negative watch in October 2013 – indicating the potential for a credit downgrade. The ongoing concern by the credit rating agencies about the credit worthiness of U.S. government debt has an impact on the credit risk and value of the Retirement System's investments in U.S. government agency securities, U.S. government bonds, and U.S. government mortgage-backed securities.

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Notes to Financial Statements
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The following table illustrates the Retirement System's exposure to credit risk as of June 30, 2016. Investments issued or explicitly guaranteed by the U.S. government of \$505,310 as of June 30, 2016 are exempt from the credit rating disclosures and are excluded from the table below.

Credit Ratings of Fixed Income Investments as of June 30, 2016

Credit Rating	Fair Value	Fair Value as a Percentage of Total
AAA	\$ 164,327	3.1%
AA	72,743	1.4%
A	247,306	4.7%
BBB	683,951	13.1%
BB	322,941	6.2%
B	294,025	5.6%
CCC	79,658	1.5%
CC	1,956	0.0%
C	4,240	0.1%
D	4,159	0.1%
Not Rated	3,352,732	64.2%
Total	\$ 5,228,038	100.0%

The following table illustrates the Retirement System's exposure to credit risk as of June 30, 2015. Investments issued or explicitly guaranteed by the U.S. government of \$1,024,648 as of June 30, 2015 are exempt from the credit rating disclosures and are excluded from the table below.

Credit Ratings of Fixed Income Investments as of June 30, 2015

Credit Rating	Fair Value	Fair Value as a Percentage of Total
AAA	\$ 212,642	4.6%
AA	148,151	3.2%
A	275,303	6.0%
BBB	792,990	17.2%
BB	346,598	7.5%
B	453,086	9.9%
CCC	83,710	1.8%
CC	2,245	0.0%
C	4,806	0.1%
D	4,033	0.1%
Not Rated	2,275,101	49.6%
Total	\$ 4,598,665	100.0%

The securities listed as "Not Rated" include short-term investment funds, government mortgage backed securities, and investments that invest primarily in rated securities, such as commingled funds and money market funds, but do not themselves have a specific credit rating. Excluding these investments, the "not rated" component of credit would be approximately 12.7% for 2016 and 19.8% for 2015.

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(c) Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of the Retirement System's investment in a single issuer. Guidelines for investment managers typically restrict a position to become no more than 5% (at fair value) of the investment manager's portfolio. Securities issued or guaranteed by the U.S. government or its agencies are exempt from this limit.

As of June 30, 2016 and 2015, the Retirement System had no investments of a single issuer that equaled or exceeded 5% of total Retirement System's investments or net position.

(d) Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government may not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The Retirement System does not have a specific policy addressing custodial credit risk for investments, but investments are generally insured, registered, or held by the Retirement System or its agent in the Retirement System's name. As of June 30, 2016 and 2015, \$153,613 and \$150,429, respectively, of the Retirement System's investments were exposed to custodial credit risk because they were not insured or registered in the name of the Retirement System, and were held by the counterparty's trust department or agent but not in the Retirement System's name.

For fiscal years 2016 and 2015, cash received as securities lending collateral is invested in a separate account managed by the lending agent using investment guidelines approved by the Retirement System and held by the custodial bank. Securities in this separately managed account are not exposed to custodial credit risk.

(e) Foreign Currency Risk

The Retirement System's exposure to foreign currency risk derives from its positions in foreign currency denominated cash, equity, fixed income, private equity investments, real assets, and swap investments. The Retirement System's investment policy allows international managers to enter into foreign exchange contracts, which are limited to hedging currency exposure existing in the portfolio. Derivatives are considered investments, rather than hedges, for accounting and financial reporting purposes.

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The Retirement System's net exposures to foreign currency risk as of June 30, 2016 are as follows:

Foreign Currency Risk Analysis as of June 30, 2016

Currency	Cash	Equities	Fixed Income	Private Equities	Real Assets	Foreign Currency Contracts	Total
Australian dollar	\$ 1,044	\$ 103,293	\$ -	\$ 10,641	\$ -	\$ 2,650	\$ 117,628
Brazilian real	(581)	26,060	19,870	-	-	(5,475)	39,874
British pound sterling	717	533,900	12,635	-	18,874	(45,288)	520,838
Canadian dollar	1,027	69,596	6,851	-	-	30,932	108,406
Chilean peso	-	2,012	-	-	-	94	2,106
Chinese yuan renminbi	-	-	-	-	-	(1,582)	(1,582)
Colombian peso	63	-	5,451	-	-	1,872	7,386
Czech koruna	101	337	-	-	-	(101)	337
Danish krone	273	39,118	-	-	-	(1,423)	37,968
Euro	(4,323)	745,341	108,816	148,583	39,685	(66,038)	972,064
Offshore Chinese yuan renminbi	-	-	-	-	-	(1,052)	(1,052)
Hong Kong dollar	567	162,696	-	-	-	3,862	167,125
Hungarian forint	137	327	-	-	-	2,515	2,979
Indian rupee	-	-	-	-	-	564	564
Indonesian rupiah	16	11,124	10,163	-	-	1,100	22,403
Japanese yen	4,587	532,091	-	-	23,343	98,308	658,329
Malaysian ringgit	315	20,649	6,628	-	-	4,087	31,679
Mexican peso	260	34,581	9,098	-	-	4,764	48,703
New Israeli shekel	73	9,685	-	-	-	5,513	15,271
New Romanian leu	21	-	2,138	-	-	(740)	1,419
New Taiwan dollar	1,851	66,010	-	-	-	(2,758)	65,103
New Zealand dollar	47	3,174	-	-	-	53,079	56,300
Norwegian krone	360	11,966	-	-	-	(1,661)	10,665
Peruvian nuevo sol	-	-	2,398	-	-	(319)	2,079
Philippine peso	(253)	2,641	811	-	-	(272)	2,927
Polish zloty	6	-	9,510	-	-	2,280	11,796
Qatari rial	-	5,448	-	-	-	-	5,448
Russian ruble	(571)	-	5,857	-	-	721	6,007
Singapore dollar	332	14,748	-	-	-	3,074	18,154
South African rand	(948)	24,765	8,183	-	-	2,250	34,250
South Korean won	1,361	98,501	-	-	-	(75)	99,787
Swedish krona	1,230	65,241	-	-	-	9,961	76,432
Swiss franc	279	192,496	147	-	-	(33,363)	159,559
Thai baht	14	7,354	2,198	-	-	6,696	16,262
Turkish lira	1,056	10,286	17,013	-	-	(7,381)	20,974
United Arab Emirates dirham	-	5,893	-	-	-	-	5,893
Total	\$ 9,061	\$ 2,799,333	\$ 227,767	\$ 159,224	\$ 81,902	\$ 66,794	\$ 3,344,081

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

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(Dollar amounts in thousands)

The Retirement System's net exposures to foreign currency risk as of June 30, 2015 are as follows:

Foreign Currency Risk Analysis as of June 30, 2015

Currency	Cash	Equities	Fixed Income	Private Equities	Real Assets	Foreign Currency Contracts	Total
Australian dollar	\$ 544	\$ 103,354	\$ 8,020	\$ 13,694	\$ -	\$ 60,897	\$ 186,509
Brazilian real	714	30,380	29,679	-	-	(18,590)	42,183
British pound sterling	2,359	639,515	21,261	-	-	(139,036)	524,099
Canadian dollar	171	88,056	15,912	-	-	(30,971)	73,168
Chilean peso	-	1,148	-	-	-	140	1,288
Colombian peso	324	-	6,111	-	-	750	7,185
Czech koruna	-	1,579	-	-	-	-	1,579
Danish krone	401	45,755	-	-	-	(3,774)	42,382
Euro	6,890	899,087	111,446	195,466	383	(9,779)	1,203,493
Hong Kong dollar	(1,077)	242,251	-	-	-	3,444	244,618
Hungarian forint	243	372	615	-	-	183	1,413
Indian rupee	-	-	-	-	-	4,277	4,277
Indonesian rupiah	409	14,589	9,371	-	-	8,521	32,890
Japanese yen	12,571	675,019	-	-	16,215	154,642	858,447
Malaysian ringgit	16	19,398	7,587	-	-	2,637	29,638
Mexican peso	506	15,878	19,895	-	-	(6,239)	30,040
New Israeli shekel	(125)	8,130	-	-	-	3,927	11,932
New Romanian leu	-	-	1,408	-	-	879	2,287
New Taiwan dollar	1,288	64,514	-	-	-	(145)	65,657
New Zealand dollar	12	3,610	11,991	-	-	(20,255)	(4,642)
Nigerian naira	186	-	309	-	-	-	495
Norwegian krone	279	16,688	-	-	-	(30,421)	(13,454)
Peruvian nuevo sol	-	-	1,487	-	-	(326)	1,161
Philippine peso	69	2,689	571	-	-	(130)	3,199
Polish zloty	16	1,069	11,231	-	-	1,331	13,647
Qatari rial	-	6,256	-	-	-	-	6,256
Russian ruble	3	-	4,796	-	-	62	4,861
Singapore dollar	163	21,740	-	-	-	5,416	27,319
South African rand	1,306	29,314	9,244	-	-	309	40,173
South Korean won	750	95,641	-	-	-	(1,006)	95,385
Swedish krona	582	75,637	-	-	-	15,510	91,729
Swiss franc	886	234,990	153	-	-	(56,846)	179,183
Thai baht	(188)	6,871	2,220	-	-	4,261	13,164
Turkish lira	-	16,353	7,462	-	-	2,926	26,741
United Arab Emirates dirham	-	10,161	-	-	-	-	10,161
Total	\$ 29,298	\$ 3,370,044	\$ 280,769	\$ 209,160	\$ 16,598	\$ (47,406)	\$ 3,858,463

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

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(Dollar amounts in thousands)

(f) Derivative Instruments

The Retirement System reports its derivative instruments under the provisions of GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. Pursuant to the requirements of this statement, the Retirement System has provided a summary of derivative instrument activities during the reporting periods presented and the related risks.

As of June 30, 2016 and 2015, the derivative instruments held by the Retirement System are considered investments and not hedges for accounting purposes. The gains and losses arising from this activity are recognized as incurred in the statement of changes in plan net position. All investment derivatives discussed below are included within the investment risk schedules, which precede this subsection. Investment derivative instruments are disclosed separately to provide a comprehensive and distinct view of this activity and its impact on the overall investment portfolio.

Valuation methods used by the Retirement System are described in more detail in Note 2(b). The fair value of the exchange traded derivative instruments, such as futures, options, rights, and warrants are based on quoted market prices. The fair values of forward foreign currency contracts are determined using a pricing service, which uses published foreign exchange rates as the primary source. The fair values of swaps are determined by the Retirement System's investment managers based on quoted market prices of the underlying investment instruments.

The tables below present the notional amounts, the fair values, and the related net appreciation (depreciation) in the fair value of derivative instruments that were outstanding at June 30, 2016 and 2015:

As of and for the Year Ended June 30, 2016			
Derivative Type / Contracts	Notional Amount	Fair Value	Net Appreciation (Depreciation) in Fair Value
Forwards			
Foreign Exchange Contracts	(a)	\$ 14,144	\$ 14,144
Other Contracts	(a)	(114)	(114)
Options			
Foreign Exchange Contracts	\$ 8,426	(64)	4
Swaps			
Credit Contracts	2,300	(18)	12
Interest Rate Contracts	43,514	968	766
Rights/Warrants			
Equity Contracts	23,123 shares	1,857	(6,406)
Total		\$ 16,773	\$ 8,406

^(a) SFERS' investment managers enter into a wide variety of forward foreign exchange and other contracts, which frequently do not involve the US dollar. As a result, a US dollar-based notional value is not included.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

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As of and for the Year Ended June 30, 2015

Derivative Type / Contracts	Notional Amount	Fair Value	Net Appreciation (Depreciation) in Fair Value
Forwards			
Foreign Exchange Contracts	(a)	\$ 749	\$ 749
Other Contracts	(a)	(308)	(308)
Options			
Foreign Exchange Contracts	\$ (6,939)	18	33
Swaps			
Credit Contracts	121,400	837	659
Interest Rate Contracts	40,315	(114)	(47)
Rights/Warrants			
Equity Contracts	6,059 shares	5,333	(2,407)
Total		\$ 6,515	\$ (1,321)

(a) SFERS' investment managers enter into a wide variety of forward foreign exchange and other contracts, which frequently do not involve the US dollar. As a result, a US dollar-based notional value is not included.

All investment derivatives are reported as investments at fair value in the statement of plan net position. Rights and warrants are reported in equity securities. Foreign exchange contracts are reported in foreign currency contracts, which also include spot contracts that are not derivatives. All other derivative contracts are reported in other debt securities. All changes in fair value are reported as net appreciation (depreciation) in fair value of investments in the statements of changes in plan net position.

Counterparty Credit Risk

The Retirement System is exposed to credit risk on non-exchange traded derivative instruments that are in asset positions. As of June 30, 2016, the fair value of forward currency contracts in asset positions (including foreign exchange contract options) to purchase and sell international currencies were \$14,872 and \$793, respectively. The Retirement System's counterparties to these contract held credit ratings of A or better on 99.6% of the positions, as assigned by one or more of the major credit rating organizations (S&P, Moody's and/or Fitch), while 0.4% was not rated. As of June 30, 2015, the fair value of forward currency contracts in asset positions (including foreign exchange contract options) to purchase and sell international currencies were \$1,724 and \$957, respectively. The Retirement System's counterparties to these contracts held credit ratings of A or better on 99.3% of the positions as assigned by one or more of the major credit rating organizations (S&P, Moody's and/or Fitch), while 0.7% were not rated.

Custodial Credit Risk

The custodial credit risk disclosure for exchange traded derivative instruments is made in accordance with the custodial credit risk disclosure requirements of GASB Statement No. 40. At June 30, 2016 and 2015, all of the Retirement System's investments in derivative instruments are held in the Retirement System's name and are not exposed to custodial credit risk.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Notes to Financial Statements
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Interest Rate Risk

The tables below describe the maturity periods of the derivative instruments exposed to interest rate risk at June 30, 2016 and 2015.

Derivative Interest Rate Risk as of June 30, 2016

<u>Derivative Type / Contracts</u>	<u>Fair Value</u>	<u>Maturities</u>		
		<u>Less than 1 year</u>	<u>1-5 years</u>	<u>6-10 years</u>
Forwards				
Foreign Exchange Contracts	\$ 14,144	\$ 14,053	\$ 91	\$ -
Options				
Foreign Exchange Contracts	(64)	(64)	-	-
Swaps				
Credit Contracts	(18)	2	(20)	-
Interest Rate Contracts	968	(80)	851	197
Total	\$ 15,030	\$ 13,911	\$ 922	\$ 197

Derivative Interest Rate Risk as of June 30, 2015

<u>Derivative Type / Contracts</u>	<u>Fair Value</u>	<u>Maturities</u>			
		<u>Less than 1 year</u>	<u>1-5 years</u>	<u>6-10 years</u>	<u>10+ years</u>
Forwards					
Foreign Exchange Contracts	\$ 749	\$ 639	\$ 110	\$ -	\$ -
Other Contracts	(308)	(308)	-	-	-
Options					
Foreign Exchange Contracts	18	19	(1)	-	-
Swaps					
Credit Contracts	837	1	879	-	(43)
Interest Rate Contracts	(114)	(2)	(94)	(18)	-
Total	\$ 1,182	\$ 349	\$ 894	\$ (18)	\$ (43)

The following table details the reference rate, notional amount, and fair value of interest rate swaps that are highly sensitive to changes in interest rates as of June 30, 2016 and 2015:

Derivative Instruments Highly Sensitive to Interest Rate Changes as of June 30, 2016

<u>Investment Type</u>	<u>Reference Rate</u>	<u>Notional Value</u>	<u>Fair Value</u>
Interest Rate Swap	Receive Fixed 1.50%, Pay Variable 6-Month WIBOR	\$ 606	\$ (1)
Interest Rate Swap	Receive Fixed 1.93%, Pay Variable 6-Month THB	301	4
Interest Rate Swap	Receive Fixed 12.055%, Pay Variable 1-Day BIDOR	252	(2)
Interest Rate Swap	Receive Fixed 12.20%, Pay Variable 1-Day BIDOR	1,108	13
Interest Rate Swap	Receive Fixed 12.23%, Pay Variable 1-Day BIDOR	203	(1)
Interest Rate Swap	Receive Fixed 12.255%, Pay Variable 1-Day BIDOR	5,381	(71)
Interest Rate Swap	Receive Fixed 12.85%, Pay Variable 1-Day BIDOR	298	19
Interest Rate Swap	Receive Fixed 13.73%, Pay Variable 1-Day BIDOR	528	5
Interest Rate Swap	Receive Fixed 15.44%, Pay Variable 1-Day BIDOR	588	104
Interest Rate Swap	Receive Fixed 15.96%, Pay Variable 1-Day BIDOR	5,287	534

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Notes to Financial Statements
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(Dollar amounts in thousands)

Derivative Instruments Highly Sensitive to Interest Rate Changes as of June 30, 2016

(Continued)

Investment Type	Reference Rate	Notional Value	Fair Value
Interest Rate Swap	Receive Fixed 16.15%, Pay Variable 1-Day BIDOR	\$ 824	\$ 172
Interest Rate Swap	Receive Fixed 16.395%, Pay Variable 1-Day BIDOR	102	23
Interest Rate Swap	Receive Fixed 16.40%, Pay Variable 1-Day BIDOR	127	30
Interest Rate Swap	Receive Fixed 16.95%, Pay Variable 1-Day BIDOR	82	22
Interest Rate Swap	Receive Fixed 2.015%, Pay Variable 6-Month THB	569	10
Interest Rate Swap	Receive Fixed 2.12%, Pay Variable 6-Month THB	683	14
Interest Rate Swap	Receive Fixed 2.175%, Pay Variable 6-Month THB	643	16
Interest Rate Swap	Receive Fixed 2.19%, Pay Variable 6-Month THB	199	5
Interest Rate Swap	Receive Fixed 2.22%, Pay Variable 6-Month THB	398	10
Interest Rate Swap	Receive Fixed 2.58%, Pay Variable 6-Month THB	771	45
Interest Rate Swap	Receive Fixed 2.625%, Pay Variable 6-Month THB	1,190	75
Interest Rate Swap	Receive Fixed 2.78%, Pay Variable 6-Month THB	26	2
Interest Rate Swap	Receive Fixed 5.21%, Pay Variable 1-Day MXIBR	596	(6)
Interest Rate Swap	Receive Fixed 5.23%, Pay Variable 3-Month CIBR	124	(5)
Interest Rate Swap	Receive Fixed 5.31%, Pay Variable 3-Month CIBR	48	(2)
Interest Rate Swap	Receive Fixed 5.32%, Pay Variable 3-Month CIBR	567	(20)
Interest Rate Swap	Receive Fixed 5.33%, Pay Variable 3-Month CIBR	574	(40)
Interest Rate Swap	Receive Fixed 5.61%, Pay Variable 28-Day MXIBR	1,724	6
Interest Rate Swap	Receive Fixed 5.63%, Pay Variable 28-Day MXIBR	1,008	3
Interest Rate Swap	Receive Fixed 5.84%, Pay Variable 28-Day MXIBR	341	4
Interest Rate Swap	Receive Fixed 6.12%, Pay Variable 3-Month CIBR	112	(5)
Interest Rate Swap	Receive Fixed 6.20%, Pay Variable 3-Month CIBR	144	(5)
Interest Rate Swap	Receive Fixed 6.22%, Pay Variable 3-Month CIBR	151	(6)
Interest Rate Swap	Receive Fixed 6.24%, Pay Variable 28-Day MXIBR	136	4
Interest Rate Swap	Receive Fixed 7.50%, Pay Variable 3-Month JIBAR	868	(22)
Interest Rate Swap	Receive Fixed 8.00%, Pay Variable 3-Month JIBAR	901	4
Interest Rate Swap	Receive Fixed 8.50%, Pay Variable 3-Month JIBAR	1,831	36
Interest Rate Swap	Receive Fixed 8.75%, Pay Variable 3-Month JIBAR	1,072	37
Interest Rate Swap	Receive Fixed 9.00%, Pay Variable 3-Month JIBAR	205	9
Interest Rate Swap	Receive Fixed 9.50%, Pay Variable 3-Month JIBAR	498	38
Interest Rate Swap	Receive Variable 1-Day BIDOR, Pay Fixed 11.16%	96	7
Interest Rate Swap	Receive Variable 1-Day BIDOR, Pay Fixed 12.86%	651	7
Interest Rate Swap	Receive Variable 1-Day BIDOR, Pay Fixed 14.205%	5,133	(9)
Interest Rate Swap	Receive Variable 1-Day BIDOR, Pay Fixed 15.50%	1,125	(56)
Interest Rate Swap	Receive Variable 1-Day BIDOR, Pay Fixed 15.77%	1,635	(92)
Interest Rate Swap	Receive Variable 28-Day MXIBR, Pay Fixed 4.65%	423	2
Interest Rate Swap	Receive Variable 28-Day MXIBR, Pay Fixed 5.66%	721	14
Interest Rate Swap	Receive Variable 28-Day MXIBR, Pay Fixed 6.08%	1,241	(3)
Interest Rate Swap	Receive Variable 28-Day MXIBR, Pay Fixed 6.32%	363	(8)
Interest Rate Swap	Receive Variable 28-Day MXIBR, Pay Fixed 6.50%	244	(1)
Interest Rate Swap	Receive Variable 3-Month CIBR, Pay Fixed 6.42%	223	6
Interest Rate Swap	Receive Variable 3-Month CIBR, Pay Fixed 6.43%	69	2
Interest Rate Swap	Receive Fixed 2.81%, Pay Return THB	524	41
Total Interest Rate Swaps		<u>\$ 43,514</u>	<u>\$ 968</u>

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Notes to Financial Statements
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(Dollar amounts in thousands)

Derivative Instruments Highly Sensitive to Interest Rate Changes as of June 30, 2015

Investment Type	Reference Rate	Notional Value	Fair Value
Interest Rate Swap	Receive Fixed 11.61%, Pay Variable 1-Day BIDOR	\$ 1,586	\$ (66)
Interest Rate Swap	Receive Fixed 12.055%, Pay Variable 1-Day BIDOR	334	(5)
Interest Rate Swap	Receive Fixed 12.18%, Pay Variable 1-Day BIDOR	370	(10)
Interest Rate Swap	Receive Fixed 12.23%, Pay Variable 1-Day BIDOR	718	(8)
Interest Rate Swap	Receive Fixed 12.36%, Pay Variable 1-Day BIDOR	4,754	(94)
Interest Rate Swap	Receive Fixed 12.85%, Pay Variable 1-Day BIDOR	370	18
Interest Rate Swap	Receive Fixed 13.68%, Pay Variable 1-Day BIDOR	3,899	(14)
Interest Rate Swap	Receive Fixed 13.775%, Pay Variable 1-Day BIDOR	414	(1)
Interest Rate Swap	Receive Fixed 13.82%, Pay Variable 1-Day BIDOR	2,447	(4)
Interest Rate Swap	Receive Fixed 2%, Pay Variable 6-Month WIBOR	160	(14)
Interest Rate Swap	Receive Fixed 2.12%, Pay Variable 6-Month THB	711	(15)
Interest Rate Swap	Receive Fixed 2.175%, Pay Variable 6-Month THB	669	3
Interest Rate Swap	Receive Fixed 2.58%, Pay Variable 6-Month THB	225	(2)
Interest Rate Swap	Receive Fixed 4.36%, Pay Variable 28-Day MXIBR	2,396	9
Interest Rate Swap	Receive Fixed 5.32%, Pay Variable 3-Month CIBR	635	2
Interest Rate Swap	Receive Fixed 5.33%, Pay Variable 3-Month CIBR	642	(16)
Interest Rate Swap	Receive Fixed 5.61%, Pay Variable 28-Day MXIBR	2,027	(4)
Interest Rate Swap	Receive Fixed 5.63%, Pay Variable 28-Day MXIBR	1,185	(6)
Interest Rate Swap	Receive Fixed 5.84%, Pay Variable 28-Day MXIBR	402	3
Interest Rate Swap	Receive Fixed 6.2%, Pay Variable 3-Month CIBR	162	1
Interest Rate Swap	Receive Fixed 6.22%, Pay Variable 3-Month CIBR	169	(1)
Interest Rate Swap	Receive Fixed 6.53%, Pay Variable 28-Day MXIBR	76	1
Interest Rate Swap	Receive Fixed 7.25%, Pay Variable 3-Month JIBAR	140	(3)
Interest Rate Swap	Receive Fixed 7.5%, Pay Variable 3-Month JIBAR	1,046	(27)
Interest Rate Swap	Receive Fixed 8.5%, Pay Variable 3-Month JIBAR	453	4
Interest Rate Swap	Receive Variable 1-Day BIDOR, Pay Fixed 10.91%	290	13
Interest Rate Swap	Receive Variable 1-Day BIDOR, Pay Fixed 11.16%	99	7
Interest Rate Swap	Receive Variable 1-Day BIDOR, Pay Fixed 11.32%	1,305	12
Interest Rate Swap	Receive Variable 1-Day BIDOR, Pay Fixed 12.225%	857	9
Interest Rate Swap	Receive Variable 1-Day BIDOR, Pay Fixed 12.255%	4,805	49
Interest Rate Swap	Receive Variable 1-Day BIDOR, Pay Fixed 13.9%	5,968	2
Interest Rate Swap	Receive Variable 28-Day MXIBR, Pay Fixed 5.66%	924	44
Interest Rate Swap	Receive Variable 3-Month CIBR, Pay Fixed 6.43%	77	(1)
Total Interest Rate Swaps		\$ 40,315	\$ (114)

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Foreign Currency Risk

At June 30, 2016, the Retirement System is exposed to foreign currency risk on its investments in forwards, rights, warrants and swaps denominated in foreign currencies.

Derivative Instruments Foreign Currency Risk Analysis as of June 30, 2016

Currency	Forwards	Rights/ Warrants	Swaps	Total
Australian dollar	\$ 2,650	\$ -	\$ -	\$ 2,650
Brazilian real	(5,349)	-	703	(4,646)
British pound sterling	(43,351)	-	-	(43,351)
Canadian dollar	31,384	-	-	31,384
Chilean peso	94	-	-	94
Chinese yuan renminbi	(1,582)	-	-	(1,582)
Colombian peso	1,872	-	(74)	1,798
Czech koruna	(45)	-	-	(45)
Danish krone	(1,423)	-	-	(1,423)
Euro	(67,878)	75	-	(67,803)
Hong Kong offshore				
Chinese yuan renminbi	(1,052)	-	-	(1,052)
Hong Kong dollar	3,569	-	-	3,569
Hungarian forint	2,652	-	-	2,652
Indian rupee	564	-	-	564
Indonesian rupiah	1,100	-	-	1,100
Japanese yen	100,599	-	-	100,599
Malaysian ringgit	4,087	-	-	4,087
Mexican peso	3,471	-	16	3,487
New Israeli shekel	5,513	-	-	5,513
New Romanian Leu	(740)	-	-	(740)
New Russian ruble	150	-	-	150
New Taiwan dollar	(2,758)	-	-	(2,758)
New Zealand dollar	53,079	-	-	53,079
Norwegian krone	(1,656)	87	-	(1,569)
Peruvian nuevo sol	(319)	-	-	(319)
Philippine peso	(272)	-	-	(272)
Polish zloty	1,865	-	(1)	1,864
Singapore dollar	3,074	-	-	3,074
South African rand	2,689	-	101	2,790
South Korean won	(75)	-	-	(75)
Swedish krona	10,958	-	-	10,958
Swiss franc	(33,477)	-	-	(33,477)
Thai baht	6,696	-	222	6,918
Turkish lira	(6,647)	-	-	(6,647)
Total	\$ 69,442	\$ 162	\$ 967	\$ 70,571

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Notes to Financial Statements
Years Ended June 30, 2016 and 2015

(Dollar amounts in thousands)

At June 30, 2015, the Retirement System is exposed to foreign currency risk on its investments in forwards, rights, warrants and swaps denominated in foreign currencies.

Derivative Instruments Foreign Currency Risk Analysis as of June 30, 2015

Currency	Forwards	Rights/ Warrants	Swaps	Total
Australian dollar	\$ 116	\$ -	\$ -	\$ 116
Brazilian real	565	-	(91)	474
British pound sterling	(4,585)	-	-	(4,585)
Canadian dollar	189	-	-	189
Chilean peso	(9)	-	-	(9)
Colombian peso	(18)	-	(14)	(32)
Euro	(60)	84	28	52
Hong Kong dollar	(517)	-	-	(517)
Hungarian forint	(3)	-	-	(3)
Indian rupee	5	-	-	5
Indonesian rupiah	96	-	-	96
Japanese yen	2,443	-	-	2,443
Malaysian ringgit	(26)	-	-	(26)
Mexican peso	219	-	47	266
New Israeli shekel	65	-	-	65
New Romanian leu	(1)	-	-	(1)
New Russian ruble	(1)	-	-	(1)
New Zealand dollar	1,505	-	-	1,505
Norwegian krone	152	-	-	152
Peruvian nuevo sol	8	-	-	8
Polish zloty	15	-	(14)	1
Singapore dollar	16	-	-	16
South African rand	83	-	(27)	56
Swedish krona	(257)	-	-	(257)
Swiss franc	374	-	-	374
Thai baht	(29)	-	(15)	(44)
Turkish lira	96	-	-	96
Total	\$ 441	\$ 84	\$ (86)	\$ 439

Contingent Features

At June 30, 2016 and 2015, the Retirement System held no positions in derivatives containing contingent features.

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(5) Fair Value Measurement of Investments

In Fiscal Year 2016, the Retirement System adopted GASB Statement No. 72, *Fair Value Measurement and Application*. The Retirement System categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles.

The Retirement System has the following recurring fair value measurements as of June 30, 2016 and June 30, 2015:

<u>As of June 30, 2016</u>	<u>Total</u>	<u>Quoted Prices in Active Markets for Identical Assets (Level One)</u>	<u>Significant Other Observable Inputs (Level Two)</u>	<u>Unobservable Inputs (Level Three)</u>
Investments by fair value level				
Short-term investments	\$ 1,009,676	\$ -	\$ -	\$ 1,009,676
Debt securities:				
U.S. government and agency securities	695,309	-	695,309	-
Other debt securities	2,246,680	-	2,134,644	112,036
Equity securities:				
Domestic	4,296,051	4,198,957	7,508	89,586
International	3,087,999	3,077,546	7,961	2,492
Foreign currency contracts, net	14,125	-	-	14,125
Invested securities lending collateral	865,681	-	389,095	476,586
Total investments by fair value level	<u>\$ 12,215,521</u>	<u>\$ 7,276,503</u>	<u>\$ 3,234,517</u>	<u>\$ 1,704,501</u>
Investments measured at the net asset value (NAV)				
Fixed income funds invested in:				
U.S. government and agency securities	952,962			
Other debt Securities	822,065			
Equity funds invested in:				
Domestic	674,787			
International	1,216,026			
Real assets	2,341,500			
Private equity	2,750,619			
Total investments measured at the NAV	<u>8,757,959</u>			
Investments not subject to the fair value hierarchy				
City investment pool	6,656			
Total investments measured at fair value	<u>\$ 20,980,136</u>			

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

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(Dollar amounts in thousands)

As of June 30, 2015	Total	Quoted Prices in Active Markets for Identical Assets (Level One)	Significant Other Observable Inputs (Level Two)	Unobservable Inputs (Level Three)
Investments by fair value level				
Short-term investments	\$ 656,185	\$ -	\$ 300	\$ 655,885
Debt securities:				
U.S. government and agency securities	760,004	-	757,810	2,194
Other debt securities	2,847,301	-	2,554,768	292,533
Equity securities:				
Domestic	4,565,235	4,502,309	17,480	45,446
International	3,584,911	3,580,792	1,580	2,539
Foreign currency contracts, net	722	-	-	722
Invested securities lending collateral	1,001,231	-	432,990	568,241
Total investments by fair value level	<u>\$ 13,415,589</u>	<u>\$ 8,083,101</u>	<u>\$ 3,764,928</u>	<u>\$ 1,567,560</u>
Investments measured at the net asset value (NAV)				
Fixed income funds invested in:				
U.S. government and agency securities	314,200			
Other debt Securities	1,045,623			
Equity funds invested in:				
Domestic	755,118			
International	1,549,266			
Real assets	1,975,926			
Private equity	2,484,299			
Total investments measured at the NAV	<u>8,124,432</u>			
Total investments measured at fair value	<u>\$ 21,540,021</u>			

Investments, at Fair Value

Equity securities classified in Level 1 of the fair value hierarchy are valued using prices quoted in active markets. Debt and equity securities classified in Level 2 of the fair value hierarchy are valued using prices determined by the use of matrix pricing techniques maintained by the various pricing vendors for these securities. Debt securities including short-term instruments are priced based on evaluated prices. Such evaluated prices may be determined by factors which include, but are not limited to, market quotations, yields, maturities, call features, ratings, institutional size trading in similar groups of securities and developments related to specific securities. For equity securities not traded on an active exchange, or if the closing price is not available, corroborated indicative quotes obtained from pricing vendors are generally used. Debt and equity securities classified in Level 3 of the fair value hierarchy are securities whose stated market prices are unobservable by the market place. Many of these securities are priced using uncorroborated indicative quotes, adjusted prices based on inputs from different sources, or evaluated prices using unobservable inputs, such as extrapolated data, proprietary models, and indicative quotes from pricing vendors.

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Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In some cases, a valuation technique may have multiple inputs used to measure fair value, and each input might fall into a different level of the fair value hierarchy. The level in the fair value hierarchy within which a fair value measurement falls in its entirety is determined based on the lowest level input that is significant to the measurement. The prices used in determining the fair value hierarchy are obtained from various pricing sources by the Retirement System's custodian bank.

Investments, at Net Asset Value (NAV)

(a) Equity and Debt Funds

The equity and debt funds are commingled funds that are priced at net asset value by industry vendors and fund families. NAV is the market value of all securities owned by a fund, minus its total liabilities, divided by the number of shares issued and outstanding. The NAV of an open-end fund is its price.

(b) Real Assets, Private Equity, and Opportunistic Fixed Income Investments

The fair value of the Retirement System's investments in real assets, private equity, and opportunistic fixed income investments are based on net asset values provided by the investment managers and general partners (hereinafter collectively referred to as the "General Partners"). Such value generally represents the Retirement System's proportionate share of the net assets of the limited partnerships. The partnership financial statements are audited annually as of December 31 and the net asset value are adjusted by additional contributions to and distributions from the partnership, the Retirement System's share of net earnings and losses, and unrealized gains and losses resulting from changes in fair value, as determined by the General Partners.

The General Partners may use one or more valuation methodologies outlined in FASB ASC 820, *Fair Value Measurement*. For some investments, little market activity may exist. The General Partners' determination of fair value is then based on the best information available in the circumstances and may involve subjective assumptions and estimates, including the General Partners' assessment of the information that market participants would use in valuing the investments. The General Partners may take into consideration a combination of internal and external factors, including but not limit to, appropriate risk adjustments for nonperformance and liquidity. Such fair value estimates involve subjective judgments of unrealized gains and losses.

The values provided by the General Partners may differ significantly from the values that would have been used had a ready market existed for these investments.

(6) Securities Lending

The Retirement System lends U.S. government obligations, domestic and international bonds, and equities to various brokers with a simultaneous agreement to return collateral for the same securities plus a fee in the future. The securities lending agent manages the securities lending program and receives securities and cash as collateral. Cash and non-cash collateral is pledged at 102% and 105% of the fair value of domestic securities and international securities lent, respectively. There are no restrictions on the number of securities that can be lent at one time. However, starting in the year ended June 30, 2009, the Retirement System engaged in a systematic reduction of the value of securities on loan with a target of no more than ten percent (10%) of total fund assets on loan at any time. The term

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(Dollar amounts in thousands)

to maturity of the loaned securities is generally not matched with the term to maturity of the investment of the corresponding collateral.

The Retirement System does not have the ability to pledge or sell collateral securities unless a borrower defaults. The securities collateral is not reported on the statements of plan net position. As of June 30, 2016 and 2015, the Retirement System has no credit risk exposure to borrowers because the amounts the Retirement System owes them exceed the amounts they owe the Retirement System. As with other extensions of credit, the Retirement System may bear the risk of delay in recovery or of rights in the collateral should the borrower of securities fail financially. However, the lending agent indemnifies the Retirement System against all borrower defaults.

As of June 30, 2016, the Retirement System has lent \$1,196,354 in securities and received collateral of \$863,536 and \$368,251 in cash and securities, respectively, from borrowers. The cash collateral is invested in a separate account managed by the lending agent using investment guidelines approved by the Retirement Board. Due to the increase in the fair value of assets held in the separately managed account, the Retirement System's invested cash collateral was valued at \$865,681. The net unrealized gain of \$2,145 is presented as part of the net appreciation (depreciation) in fair value of investments in the statement of changes in plan net position in the year in which the unrealized gains and losses occur. The Retirement System is exposed to investment risk including the possible loss of principal value in the separately managed securities lending account due to the fluctuation in the fair value of the assets held in the account.

The Retirement System's securities lending transactions as of June 30, 2016 are summarized in the following table.

Securities Lending as of June 30, 2016

Investment Type	Fair Value of Loaned Securities	Cash Collateral	Fair Value of Non- Cash Collateral
Securities on Loan for Cash Collateral			
International Corporate Fixed Income	\$ 5,600	\$ 5,842	\$ -
International Equities	40,741	42,797	-
International Government Fixed Income	1,105	1,153	-
U.S. Government Agencies	204	208	-
U.S. Corporate Fixed Income	114,536	116,353	-
U.S. Equities	439,182	445,863	-
U.S. Government Fixed Income	247,020	251,320	-
Securities on Loan for Non-Cash Collateral			
International Corporate Fixed Income	8,736	-	9,163
International Equities	295,913	-	315,144
International Government Fixed Income	105	-	110
U.S. Corporate Fixed Income	6,132	-	6,225
U.S. Equities	37,080	-	37,609
	<u>\$ 1,196,354</u>	<u>\$ 863,536</u>	<u>\$ 368,251</u>

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The following table presents the segmented time distribution for the reinvested cash collateral account based upon the expected maturity (in years) as of June 30, 2016.

Fair Value of Cash Collateral Account as of June 30, 2016

Investment Type	Fair Value	Maturity Less Than 1 Year
Commercial Paper	\$ 44,260	\$ 44,260
Negotiable Certificates of Deposit	345,116	345,116
Repurchase Agreements	419,000	419,000
Short Term Investment Funds	57,305	57,305
Total	\$ 865,681	\$ 865,681

The Retirement System's exposure to credit risk in its reinvested cash collateral account as of June 30, 2016 is as follows:

Credit Rating of Cash Collateral Account as of June 30, 2016

Credit Rating	Fair Value	Fair Value as a Percentage of Total
AA	\$ 153,323	17.7%
A	337,078	38.9%
Not Rated *	375,280	43.4%
Total	\$ 865,681	100.0%

* Repurchase agreements of \$270,000 are not rated by Moody's, but are held by counterparties with S&P ratings of A or AA.

As of June 30, 2015, the Retirement System has lent \$1,442,293 in securities and received collateral of \$1,001,546 and \$496,053 in cash and securities, respectively, from borrowers. The cash collateral is invested in a separate account managed by the lending agent using investment guidelines approved by the Retirement Board. Due to the decline in the fair value of assets held in the separately managed account, the Retirement System's invested cash collateral was valued at \$1,001,231. The net unrealized loss of \$315 is presented as part of the net appreciation (depreciation) in fair value of investments in the statement of changes in plan net position in the year in which the unrealized gains and losses occur. The Retirement System is exposed to investment risk including the possible loss of principal value in the separately managed securities lending account due to the fluctuation in the fair value of the assets held in the account.

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(Dollar amounts in thousands)

The Retirement System's securities lending transactions as of June 30, 2015 are summarized in the following table.

Securities Lending as of June 30, 2015			
Investment Type	Fair Value of Loaned Securities	Cash Collateral	Fair Value of Non- Cash Collateral
Securities on Loan for Cash Collateral			
International Corporate Fixed Income	\$ 14,704	\$ 15,559	\$ -
International Equities	40,737	43,286	-
International Government Fixed Income	1,952	2,110	-
U.S. Government Agencies	260	265	-
U.S. Corporate Fixed Income	187,469	191,358	-
U.S. Equities	443,154	452,384	-
U.S. Government Fixed Income	290,880	296,584	-
Securities on Loan for Non-Cash Collateral			
International Corporate Fixed Income	6,415	-	6,776
International Equities	352,198	-	381,165
International Government Fixed Income	13,491	-	13,965
U.S. Corporate Fixed Income	12,370	-	12,624
U.S. Equities	78,423	-	81,279
U.S. Government Fixed Income	240	-	244
	<u>\$ 1,442,293</u>	<u>\$ 1,001,546</u>	<u>\$ 496,053</u>

The following table presents the segmented time distribution for the reinvested cash collateral account based upon the expected maturity (in years) as of June 30, 2015.

Fair Value of Cash Collateral Account as of June 30, 2015

Investment Type	Fair Value	Maturity Less Than 1 Year
Commercial Paper	\$ 51,095	\$ 51,095
Negotiable Certificates of Deposit	401,996	401,996
Repurchase Agreements	503,000	503,000
Short Term Investment Funds	45,140	45,140
Total	<u>\$ 1,001,231</u>	<u>\$ 1,001,231</u>

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Notes to Financial Statements
Years Ended June 30, 2016 and 2015

(Dollar amounts in thousands)

The Retirement System's exposure to credit risk in its reinvested cash collateral account as of June 30, 2015 is as follows:

Credit Rating of Cash Collateral Account as of June 30, 2015

Credit Rating	Fair Value	Fair Value as a Percentage of Total
AA	\$ 165,124	16.5%
A	406,006	40.5%
Not Rated *	430,101	43.0%
Total	\$ 1,001,231	100.0%

* Repurchase agreements of \$430,000 are not rated, but are held by counterparties with an S&P rating of A.

(7) Investments in Real Assets

Real assets investments represent the Retirement System's interests in real assets limited partnerships and separate accounts. The changes in these investments during the years ended June 30, 2016 and 2015 are summarized as follows:

	2016	2015
Investments:		
Beginning of the year	\$ 1,975,926	\$ 1,784,244
Capital investments	1,318,111	255,252
Equity in net earnings	48,492	40,378
Net appreciation in fair value	168,196	258,911
Capital distributions	(1,169,225)	(362,859)
End of the year	\$ 2,341,500	\$ 1,975,926

(8) Benefits

Allowances and benefits incurred during the year are summarized as follows:

	2016	2015
Service retirement benefits	\$ 937,388	\$ 878,834
Disability retirement benefits	179,056	175,620
Death benefits	8,990	7,492
COLA benefit adjustments	118,012	51,447
DROP accrued retirement benefits	(186)	5,298
Total	\$ 1,243,260	\$ 1,118,691

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Notes to Financial Statements
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(9) Funding Policy

Contributions are made to the Plan by both the employers and the participating employees. The basic employer contributions are the amounts deemed necessary on an actuarial basis using the entry age normal cost method to provide the Retirement System with assets sufficient to pay the basic benefits that are not provided for by employees' contributions. Contribution rates used in fiscal years 2016 and 2015 are based on a schedule of rates determined from actuarial studies by the consulting actuary as of July 1, 2014 and 2013, respectively.

Required and actual employer contribution rates for the years ended June 30, 2016 and 2015 as a percentage of covered payrolls were as follows:

	<u>Fiscal Year 2016</u>	<u>Fiscal Year 2015</u>
Police plan members	18.30% - 19.30%	22.26% - 23.26%
Fire plan members	18.30% - 19.30%	22.26% - 23.26%
Miscellaneous Non-Safety members	18.80% - 22.80%	22.76% - 26.76%
Sheriff and Miscellaneous Safety members	18.80% - 19.30%	22.76% - 23.26%

Employee contributions are mandatory as required by the Charter. Employee contribution rates for fiscal years 2016 and 2015 as a percentage of gross covered salary were as follows:

	<u>Fiscal Year 2016</u>	<u>Fiscal Year 2015</u>
Participants entering the Retirement System prior to November 2, 1976		
Police and fire	11.5%	11.5%
Miscellaneous	8.0% - 12.0%	8.0% - 12.0%
Participants entering the Retirement System after November 2, 1976 and prior to July 1, 2010		
Police and fire	12.0%	12.0%
Miscellaneous	7.5% - 11.5%	7.5% - 11.5%
Participants entering the Retirement System on or after July 1, 2010		
Police and fire	12.5% - 13.0%	12.5% - 13.0%
Miscellaneous	7.5% - 11.5%	7.5% - 11.5%
Sheriff and Miscellaneous Safety hired on or after January 7, 2012	12.5% - 13.0%	12.5% - 13.0%

Beginning in the year ended June 30, 2006, most employee groups agreed through collective bargaining for employees to contribute all or a portion of the employee contributions, per memorandums of understanding (MOU's), on a pretax basis. As of July 1, 2011, substantially all employee groups have agreed through collective bargaining for employees to contribute all employee contributions on a pre-tax basis.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Notes to Financial Statements Years Ended June 30, 2016 and 2015

(Dollar amounts in thousands)

Prior to the early 1950s, all Retirement System members were covered by the Federal Old-Age and Survivors Disability Insurance provisions of the Federal Social Security Act. In the early 1950s, the City and County agreed to exclude uniformed police officers and firefighters from Social Security coverage. Prior to 1990, miscellaneous members covered by Social Security were able to elect to reduce the above stated rate of employee contributions in consideration of their anticipated Social Security benefit payments. All participants who elected such reduction must repay the amount of unpaid employee contributions with interest or there will be an appropriate actuarial reduction in benefits.

Participants terminating service with the employers may withdraw employee contributions plus interest. The interest rate applied to accumulated employee contributions is determined by the Retirement System's consulting actuary and recommended to the Retirement Board. The Retirement Board reviews and sets the crediting interest rate for the Plan on an annual basis. Interest for the years ended June 30, 2016 and 2015 accumulated at 4.00%.

(10) Net Pension Liability of Employers

The components of the employers' net pension liability at June 30, 2016 and 2015 were as follows:

	June 30, 2016	June 30, 2015
Total pension liability	\$ 25,967,281	\$ 22,724,102
Plan net position	\$ 20,154,503	\$ 20,428,069
Net pension liability	\$ 5,812,778	\$ 2,296,033
Plan net position as a percentage of total pension liability	77.6%	89.9%

(a) Actuarial Assumptions

The total pension liabilities as of June 30, 2016 and 2015 were determined by actuarial valuations as of June 30, 2015 and 2014, respectively, which were rolled forward to June 30, 2016 and 2015 using standard roll forward procedures. The June 30, 2016 total pension liabilities include an adjustment for the October 2015 State Appeals Court determination that the "full funding" requirement for Supplemental COLAs of Proposition C does not apply to members who worked after November 6, 1996 and were hired prior to January 7, 2012. Retroactive lump sums were paid during fiscal year 2015-16 for the restoration of 2013 and 2014 Supplemental COLAs to this subgroup of members. The updated adjustment procedures also include the increased expectation of future Supplemental COLAs for these members.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Notes to Financial Statements
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The following is a summary of actuarial methods and assumptions used at the June 30, 2016 measurement date:

Inflation	3.25%
Salary increases	3.75% plus merit component based on employee classification and years of service
Investment rate of return	7.50%, net of pension plan investment expense, including inflation

Mortality rates for active members and healthy annuitants were based upon adjusted Employee and Healthy Annuitant CalPERS mortality tables projected generationally from the 2009 base year using a modified version of the MP-2015 projection scale.

The actuarial assumptions used at the June 30, 2016 measurement date were based upon the results of a demographic experience study for the period July 1, 2009 through June 30, 2014 and an economic experience study as of July 1, 2015.

The probability of a Supplemental COLA as of June 30, 2016 was developed based upon the probability and amount of Supplemental COLA for each future year. The table below shows the net assumed Supplemental COLA for members with a 2.00% basic COLA for sample years.

Assumed Supplemental COLA for Members with a 2.00% Basic COLA

<u>July 1,</u>	<u>11/6/1996 – Prop C</u>	<u>Before 11/6/1996 or After Prop C</u>
2018	0.750%	0.000%
2023	0.750%	0.220%
2028	0.750%	0.322%
2033	0.750%	0.370%
2038+	0.750%	0.375%

The long-term expected rate of return on pension plan investments was 7.50%. It was set by the Retirement Board after consideration of both expected future returns and historical returns experienced by the Retirement System. Expected future returns were determined by using a building-block method in which best-estimate ranges of expected future real rates of return were developed for each major asset class. These ranges were 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.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

**Notes to Financial Statements
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The target allocation and best estimates of geometric long-term expected real rates of return (expected returns, net of pension plan investment expense and inflation) for each major asset class as of June 30, 2016 are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Global Equity	40.0%	5.1%
Fixed Income	20.0%	1.1%
Private Equity	18.0%	6.3%
Real Assets	17.0%	4.3%
Hedge Funds/Absolute Return	5.0%	3.3%
	100.0%	

The following is a summary of actuarial methods and assumptions used at the June 30, 2015 measurement date:

Inflation	3.25%
Salary increases	3.75% plus merit component based on employee classification and years of service
Investment rate of return	7.50%, net of pension plan investment expense, including inflation

Mortality rates for active members were based upon the RP-2000 Employee Tables for Males and Females projected using Scale AA to 2030 for females and to 2005 for males. Mortality rates for healthy annuitants were based upon the RP-2000 Healthy Annuitant Tables for Males and Females projected using Scale AA to 2020.

The actuarial assumptions used at the June 30, 2015 measurement date were based upon the results of a demographic experience study for the period July 1, 2004 through June 30, 2009 and an economic experience study as of July 1, 2014.

The probability of a Supplemental COLA as of June 30, 2015 was developed based upon the probability and amount of Supplemental COLA for each future year. The table below shows the net assumed Supplemental COLA for members with a 2.00% basic COLA for sample years.

**Assumed Supplemental COLA for Members
with a 2.00% Basic COLA**

Fiscal Year Ending June 30	Assumption
2016	0.000%
2021	0.345%
2026	0.375%
2031	0.375%
2036+	0.375%

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

Notes to Financial Statements Years Ended June 30, 2016 and 2015

(Dollar amounts in thousands)

The long-term expected rate of return on pension plan investments was 7.50%. It was set by the Retirement Board after consideration of both expected future returns and historical returns experienced by the Retirement System. Expected future returns were determined by using a building-block method in which best-estimate ranges of expected future real rates of return were developed for each major asset class. These ranges were 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 best estimates of geometric long-term expected real rates of return (expected returns, net of pension plan investment expense and inflation) for each major asset class as of June 30, 2015 are summarized in the following table:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
Global Equity	40.0%	5.1%
Fixed Income	20.0%	1.2%
Private Equity	18.0%	7.5%
Real Assets	17.0%	4.1%
Hedge Funds/Absolute Return	5.0%	3.5%
	<u>100.0%</u>	

(b) Discount Rate

The discount rate used to measure the total pension liability at June 30, 2016 was 7.50%. The projection of cash flows used to determine the discount rate assumed that plan member contributions will continue to be made at the rates specified in the Charter. Employer contributions were assumed to be made in accordance with the contribution policy in effect for the July 1, 2015 actuarial valuation. Based on these assumptions, the System's fiduciary net position was projected to be available to make projected future benefit payments for current members until FY 2092-93 when only a portion of the projected benefit payments are expected to be made from the projected fiduciary net position. Projected benefit payments are discounted at the long-term expected return on assets of 7.50% to the extent the fiduciary net position is available to make the payments and at the municipal bond rate of 2.85% to the extent that they are not available. The single equivalent rate used to determine the total pension liability as of June 30, 2016 is 7.50%.

The discount rate used to measure the total pension liability at June 30, 2015 is determined in a similar fashion (but based upon the contribution policy in effect for the July 1, 2014 valuation) and is 7.46%. The System's fiduciary net position was projected to be available to make projected future benefit payments for current members until FY 2075-76 when only a portion of the projected benefit payments were expected to be made from the projected fiduciary net position. Projected benefit payments are discounted at the long-term expected return on assets of 7.50% to the extent the fiduciary net position is available to make the payments and at the municipal bond rate of 3.85% to the extent that they are not available. The single equivalent rate used to determine the total pension liability as of June 30, 2015 is 7.46%.

The municipal bond rates of 2.85% and 3.85% were used for the determination of the above discount rates, which represent the yields available at June 30, 2016 and June 30, 2015, respectively, on the Bond Buyer 20-Bond GO Index.

SAN FRANCISCO CITY AND COUNTY EMPLOYEES' RETIREMENT SYSTEM

**Notes to Financial Statements
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(Dollar amounts in thousands)

(c) Sensitivity of the net pension liability to changes in the discount rate

The following presents the net pension liability as of June 30, 2016 and 2015, calculated using the discount rate of 7.50% and 7.46%, respectively, as well as what the total net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower or 1-percentage-point higher than the discount rates:

	Net Pension Liability	
	June 30, 2016	June 30, 2015
1% Decrease	\$9,211,449	\$5,077,324
Current Discount Rate	\$5,812,778	\$2,296,033
1% Increase	\$3,001,677	\$(36,503)

(d) Money Weighted Rate of Returns

For the year ended June 30, 2016 and 2015, the annual money-weighted rates of return on pension plan investments, net of investment expenses, adjusted for the changing amounts actually invested, were 0.96% and 4.03%, respectively.

(11) Postemployment Healthcare Plan

(a) Health Care Benefits

Health care benefits of the Retirement System's employees, retired employees and their beneficiaries are financed by the City and County through the City and County of San Francisco Health Service System (Health Service System).

The City and County has determined a City-wide annual required contribution (ARC), interest on net OPEB obligation, ARC adjustment, and OPEB cost based upon an actuarial valuation performed in accordance with GASB Statement No. 45, by the City and County's actuary. The City and County's allocation of the OPEB-related costs to the Retirement System for the years ended June 30, 2016 and 2015 based upon its percentage of City-wide payroll costs is presented below. Included in the Retirement System's payments for all health care benefits amounts are approximately \$533 and \$543 for the years ended June 30, 2016 and 2015, respectively, to provide postretirement benefits for retired employees on a pay-as-you-go basis. The OPEB expense for the Retirement System is included in other administrative expenses for fiscal years 2015-16 and 2014-15.

<u>Plan Fiscal Year Ended June 30</u>	<u>Annual OPEB Cost</u>	<u>Percentage of OPEB Cost Contributed</u>	<u>Net OPEB Obligations</u>
2013	\$1,349	39.6%	\$4,800
2014	1,195	36.0%	5,464
2015	1,154	35.0%	6,075
2016	1,100	35.0%	6,642

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Notes to Financial Statements Years Ended June 30, 2016 and 2015

(Dollar amounts in thousands)

The following table shows the components of the City and County's annual OPEB allocations for the Retirement System, for the amount contributed to the OPEB plan, and changes in the Retirement System's net OPEB obligation:

	2016	2015
Annual required contribution	\$ 1,038	\$ 1,112
Interest on net OPEB obligation	330	253
Adjustment to annual required contribution	<u>(268)</u>	<u>(211)</u>
Annual OPEB cost	1,100	1,154
Contribution made	<u>(533)</u>	<u>(543)</u>
Increase in net OPEB obligation	567	611
Net OPEB obligation - beginning of year	<u>6,075</u>	<u>5,464</u>
Net OPEB obligation - end of year	<u><u>\$ 6,642</u></u>	<u><u>\$ 6,075</u></u>

The City and County issues a publicly available financial report that includes the complete note disclosures and RSI related to the City and County's postemployment health care obligations. The report may be obtained by writing to the City and County of San Francisco, Office of the Controller, 1 Dr. Carlton B. Goodlett Place, Room 316, San Francisco, California 94102, or by calling (415) 554-7500.

(12) Commitments and Contingencies

(a) Unfunded Investments Commitments

The Retirement System has unfunded commitments to contribute capital for real assets in the amount of \$1,929,866, private equities in the amount of \$2,532,929, and opportunistic fixed income in the amount of \$271,382 totaling \$4,734,177 as of June 30, 2016.

(b) Legal

Proposition C, a pension reform Charter amendment approved by voters in November 2011, included changes in the calculation of certain supplemental cost of living adjustments and was intended to reduce pension costs. These Proposition C changes in the calculation of certain supplemental cost of living adjustments were the subject of litigation and a decision of the California Court of Appeals. The California Court of Appeals held that the changes to the supplemental cost of living adjustments in Proposition C could not be applied to retirees who retired after November 1996. That decision was appealed to the California Supreme Court. On June 17, 2015, the California Supreme Court denied review of the Court of Appeals decision. On October 25, 2015, the San Francisco Superior Court entered an amended judgment consistent with the Court of Appeals decision.

After due consideration and in consultation with Board legal counsel, at its July 2016 regular Board meeting, the Retirement Board determined, in light of the conclusions recited in the Court of Appeals decision, Proposition C should be interpreted to provide payment of the supplemental cost of living adjustments to pre-1996 retirees without a "fully funded" precondition to payment. On September 19, 2016, the City and County of San Francisco and the Controller filed an action against the Retirement Board and the Retirement System's Executive Director, seeking to prevent the

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Retirement System from paying supplemental COLA benefits to pre-1996 retirees on the same basis that those benefits have been paid to the post-1996 retirees in accordance with the Court's decision in *Protect Our Benefits v. City and County of San Francisco*. On October 5, 2016, the San Francisco Superior Court granted the City's motion for preliminary injunction, thus preventing the Retirement System from making retroactive supplemental cost of living adjustments to the pre-1996 retirees. The City's motion for a permanent injunction to prevent the Retirement System from paying the supplemental cost of living adjustments to the pre-1996 retirees is under review by the San Francisco Superior Court. The amount of the retroactive cost of living adjustments to be paid to eligible retirees and beneficiaries cannot be reasonably estimated at this time.

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Schedule of Changes in Net Pension Liability and Related Ratios

	<u>Year Ended</u> <u>June 30, 2016</u>	<u>Year Ended</u> <u>June 30, 2015</u>	<u>Year Ended</u> <u>June 30, 2014</u>
Total pension liability:			
Service cost	\$ 567,576	\$ 523,644	\$ 509,200
Interest on total pension liability	1,669,996	1,621,582	1,542,266
Changes of benefit terms	1,293,714	-	-
Differences between expected and actual experience	(119,270)	(197,981)	-
Changes of assumptions	1,087,309	216,845	(73,315)
Benefit payments, including refunds of contributions	<u>(1,256,146)</u>	<u>(1,131,030)</u>	<u>(1,072,526)</u>
Net change in total pension liability	3,243,179	1,033,060	905,625
Total pension liability - beginning of year	<u>22,724,102</u>	<u>21,691,042</u>	<u>20,785,417</u>
Total pension liability - end of year (a)	<u>25,967,281</u>	<u>22,724,102</u>	<u>21,691,042</u>
Plan net position:			
Contributions - member	322,764	301,682	289,020
Contributions - employer	526,805	592,643	532,882
Net investment income	150,190	763,429	3,175,431
Benefit payments, including refunds of contributions	(1,256,146)	(1,131,030)	(1,072,526)
Administrative expense	<u>(17,179)</u>	<u>(19,262)</u>	<u>(15,745)</u>
Net change in plan net position	(273,566)	507,462	2,909,062
Plan net position - beginning of year	<u>20,428,069</u>	<u>19,920,607</u>	<u>17,011,545</u>
Plan net position - end of year (b)	<u>20,154,503</u>	<u>20,428,069</u>	<u>19,920,607</u>
Net pension liability - end of year (a) - (b)	<u>\$ 5,812,778</u>	<u>\$ 2,296,033</u>	<u>\$ 1,770,435</u>
Plan net position as a percentage of total pension liability	77.6%	89.9%	91.8%
Covered payroll	\$ 2,836,498	\$ 2,642,752	\$ 2,507,162
Net pension liability as a percentage of covered payroll	204.9%	86.9%	70.6%

* This schedule is intended to show information for 10 years. Additional years will be displayed as they become available.

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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 a Percentage of Covered Payroll
2016	\$ 526,805	\$ 526,805	\$ -	\$ 2,836,498	18.6%
2015	592,643	592,643	-	2,642,752	22.4%
2014	532,882	532,882	-	2,507,162	21.3%
2013	442,870	442,870	-	2,448,734	18.1%
2012	410,797	410,797	-	2,360,413 *	17.4%
2011	308,823	308,823	-	2,398,823 *	12.9%
2010	223,614	223,614	-	2,544,939 *	8.8%
2009	119,751	119,751	-	2,457,196 *	4.9%
2008	134,060	134,060	-	2,376,221 *	5.6%
2007	132,601	132,601	-	2,161,261 *	6.1%

* Covered compensation from actuarial projection.

Schedule of Money-Weighted Rate of Return

<u>Year Ended June 30</u>	<u>Money-Weighted Rate of Return</u>
2016	0.96%
2015	4.03%
2014	19.10%
2013	13.91%
2012	0.81%
2011	22.65%
2010	14.53%
2009	-22.28%
2008	-4.09%
2007	19.81%

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Note to Schedule of Changes in Net Pension Liability and Related Ratios

The total pension liability contained in the schedule was determined by the Retirement System's actuary, Cheiron, Inc. The net pension liability is measured as the total pension liability less the amount of the plan net position of the Retirement System. The discount rate was 7.50% as of June 30, 2016, 7.46% as of June 30, 2015, and 7.58% as of June 30, 2014. The June 30, 2016 total pension liabilities include an adjustment for the October 2015 State Appeals Court determination that the "full funding" requirement for Supplemental COLAs of Proposition C does not apply to members who retired on or after November 6, 1996 and were hired prior to January 7, 2012. The restoration of and the resulting increased expectation of future Supplemental COLAs are accounted for as a change in benefits in the measurement of the total pension liability as of June 30, 2016. A summary of assumptions may be found in the Note 10 to the financial statements. A complete description of methods and assumptions may be found in the Retirement System's *GASB 67/68 Report* for the corresponding fiscal years.

Note to Schedule of Employer Contributions

Actuarially determined contribution rates are calculated based on the actuarial valuation one year prior to the beginning of the fiscal year in which contributions are reported. Methods and assumptions used to determine contribution rates are:

Year Ended June 30	Valuation Date	Discount Rate	Salary Increase/Amortization Growth	Mortality	Significant Changes in Assumptions from Prior Year
2016	7/1/2014	7.50%	3.75%	RP2000 Mortality projected with Scale AA	Investment return and wage inflation assumptions
2015	7/1/2013	7.58%	3.83%		None
2014	7/1/2012	7.58%	3.83%		Investment return and wage inflation assumptions
2013	7/1/2011	7.66%	3.91%		Investment return and wage inflation assumptions
2012	7/1/2010	7.75%	4.00%		Wage inflation and demographic assumptions including salary merit increases based upon experience study
2011	7/1/2009	7.75%	4.50%	1994 GAM	None
2010	7/1/2008	7.75%	4.50%		Investment return
2009	7/1/2007	8.00%	4.50%		None
2008	7/1/2006	8.00%	4.50%		None
2007	7/1/2005	8.00%	4.50%		Asset smoothing method, disability mortality assumption and other assumption and valuation methodology changes

A complete description of the methods and assumptions used to determine contribution rates can be found in the corresponding actuarial valuation reports.