



# Sonoma County Employees' Retirement Association 2018



**A Pension Trust Fund for The County of Sonoma, Santa Rosa, California  
Popular Annual Financial Report For the Year ended December 31, 2018**



Government Finance Officers Association

# Award for Outstanding Achievement in Popular Annual Financial Reporting

Presented to

**Sonoma County**

**Employees' Retirement Association**

**California**

For its Annual  
Financial Report  
for the Fiscal Year Ended

**December 31, 2017**

*Christopher P. Morill*

Executive Director/CEO

## **MEMBERS OF THE BOARD OF RETIREMENT**

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As of December 31, 2018

Chair  
**Brian Williams**

Elected by Safety Members.  
Present term expires  
December 31, 2018

Trustee  
**Christel Querijero**

Elected by General Members.  
Present term expires  
December 31, 2020

Trustee  
**Joe Tambe**

Appointed by  
Board of Supervisors.  
Present term expires  
December 31, 2020

Vice-Chair  
**Michael Gossman**

Elected by General Members.  
Present term expires  
December 31, 2019

Trustee  
**David Rabbitt**

Appointed by  
Board of Supervisors.  
Present term expires  
December 31, 2018

Trustee  
**Robert Williamson**

Appointed by  
Board of Supervisors.  
Present term expires  
December 31, 2019

Trustee  
**Greg Jahn**

Appointed by  
Board of Supervisors.  
Present term expires  
December 31, 2020

Trustee  
**Erick Roeser**

Auditor/Controller/  
Treasurer/Tax Collector  
Ex-Officio Trustee

Alternate Trustee  
**Neil Baker**

Elected by Retiree Members.  
Present term expires  
December 31, 2020

Trustee  
**John Pels**

Elected by Retiree Members.  
Present term expires  
December 31, 2020

## **COMMENTS FROM SCERA'S CHIEF EXECUTIVE OFFICER**

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I am pleased to present this summary of the Annual Financial Report for the year ending December 31, 2018. The Comprehensive Annual Financial Report (CAFR) provides a more complete overview of SCERA's financial position and operation results, and is available at the SCERA office or on-line at [www.scretire.org](http://www.scretire.org).

### **Actuarial Funding Status**

SCERA's funding objective is to meet benefit promises by achieving long-term full funding of the cost of benefits, seeking reasonable and equitable allocation of those costs, minimizing volatility of contributions where possible and consistent with other policy goals, and obtaining optimum returns consistent with the assumption of prudent risk. Pursuant to provisions in the County Employees Retirement Law of 1937, SCERA engages an independent actuarial firm to perform actuarial valuations of the System annually. As of this latest actuarial valuation, the actuarial funding status (the ratio of System assets to System liabilities) is 86.8%.

### **Investments**

The most significant development in SCERA's investment portfolio structure during 2018 was the migration of the stock (equity) portfolio from the previous 60% US/40% non-US mixture to a 50%/50% split. The historical overweight to US stocks made sense in the past because of the dominance of the US economy and the maturity and transparency of the US stock market. As foreign stock markets have matured with improved regulatory protections, larger size, increased liquidity and more competitive costs it made sense to increase the non-US stock exposure. The migration to a 50/50 split in 2018 was the last step in a series of steps over the last decade to increase the non-US stock exposure and now brings us roughly in-line with the US/non-US split based on the capitalization of the world's equity markets. (Capitalization is a measure of the market value of all the outstanding shares for a given stock, industry or market.) SCERA was able to effect this transition while minimizing the impact on the Plan's investment manager line-up. The Templeton Global Equity portfolio was the only account discontinued. The freed-up assets were reallocated to multiple non-US equity manager accounts including the Templeton non-US equity account, which continues. In addition, SCERA migrated the Dodge & Cox domestic stock portfolio to a global portfolio to effect the 50/50 split. Last, the Russell 1000 Growth Index fund, which had been a complement to the Dodge & Cox domestic portfolio, was converted to a Russell 1000 Index fund. All of these changes were completed by the end of the third quarter.

SCERA continued to invest its "Opportunistic" allocation in 2018, which has 0% to 6% policy weight. The allocation's purpose is to capitalize on outsized opportunities resulting from significant market dislocations. We expect there to be periods when this allocation goes unused because we believe accessible and meaningful dislocations are not common and they should not be long-lived. We have employed this allocation since 2015 by investing in a series of Special Opportunity Funds (SOFs) managed by Davidson Kempner (DK). The manager adds value by acquiring distressed credit portfolios at bargain prices and then reorganizing and selling off the assets. The maximum aggregate exposure at any one time to the series of DK funds is approximately 3% of Plan assets.

Also in 2018, investment staff conducted a survey of California public retirement plans and their use of investment consultants. SCERA is well satisfied with the quality of service it receives from Aon, the Plan's investment consultant, and the survey confirmed the fee arrangement is competitive. After discussion and consideration, the Board elected to approve a new three-year consulting contract with two optional one-year extensions.

The Board also received an educational presentation in 2018 on ESG (Environmental, Social and Governance) investing, a topic currently receiving significant attention. Some proponents of ESG investing argue that investors often inadequately consider the risks relating to ESG matters. The advocated responses range from outright elimination of certain stocks or industries from portfolios to simply increased consideration of the issues. Our Board members are fiduciaries and they oversee the Plan's assets under California law, which requires that they perform their duties in the sole interest of Plan participants. The Board thoroughly debated ESG investing and a similar issue, that of local investing, and refined their position on these issues. The Plan's managers are expected to consider ESG factors but only when they materially impact the value of an investment being considered, either by influencing the risk or the expected return.

For calendar year 2018, the Plan's investment portfolio returned -3.0% gross-of-fees and, with annual fees of approximately 0.5%, -3.5% net-of-fees. This net-of-fee return of -3.5% is well below the current Actuarial Assumed Rate of Return (ROR) of 7.0%.

The weakness of 2018 eroded much of the strength of the previous two calendar years, producing a sub-par five-year return of 6.0%. The ten-year gross-of-fees return of 9.6% no longer contains the impact of the 2008 large market downturn, and is well above long-term expectations. The Plan's performance over twenty-five years is 7.6% gross-of-fees, which on an after-fee basis is in-line with long-term expectations. Given the long-term nature of the Plan, we view this to be the Plan's most relevant return.

### **Operations**

2018 was a year of recovery for Sonoma County in the wake of a major fire in October of 2017, but Trustees and SCERA staff were busy with operational policies. SCERA adopted several new policies to address correction of benefit payment or contribution errors, incompatible activities of Trustees and staff in pursuing outside employment, and benefit appeals. In addition SCERA amended its bylaws to remove election procedures and administrative hearing rules and developed separate policies to address those areas. The Sonoma County Board of Supervisors adopted, at SCERA's request, Article 8.4, which enables SCERA to establish separate accounts for members and nonmembers (spouses or domestic partners) upon a dissolution of marriage or domestic partnership. SCERA developed and adopted a policy to guide staff in the administration of separate accounts.

SCERA's Strategic Plan covers a five year period from 2018 through 2022, and in line with its strategic goals SCERA adopted an annual Business Plan that contains action items intended to be completed or substantially completed within a year. SCERA discussed the status of its reserves, pursuant to the Cost of Living Adjustment (COLA) policy, and communicated to the Sonoma County Administrator and Sonoma County Association of Retired Employees Board President the inability to recommend a COLA based upon the insufficiency of the reserves. We also communicated the loss of purchasing power since the last COLA was granted, and the cost of a COLA should one be able to be granted.

### **Retirement Board**

2018 saw the reelection of Brian Williams, the Safety Member, and the appointment of Sonoma County Board of Supervisors member Susan Gorin, who replaced Supervisor David Rabbitt. Ms. Gorin began her tenure on the Board in January of 2019. We are very pleased with the election and appointment of these Trustees and greatly appreciate the continuity of our Board. The Board officers consist of Michael Gossman, Chair, and Bob Williamson, Vice Chair, and our Investment Committee officers consist of Greg Jahn, Chair, and Brian Williams, Vice Chair.

### **Popular Annual Financial Reporting Award**

SCERA received from the GFOA an Award for Outstanding Achievement in Popular Annual Financial Reporting for its Popular Annual Financial Report (PAFR) for the fiscal year ended December 31, 2017. The PAFR is sent to all SCERA members and includes highlights of the annual CAFR. This was the fourteenth year the PAFR was submitted to the GFOA and we are very pleased that the PAFR again received the Certificate of Achievement.

Respectfully submitted,

Julie Wyne  
Chief Executive Officer

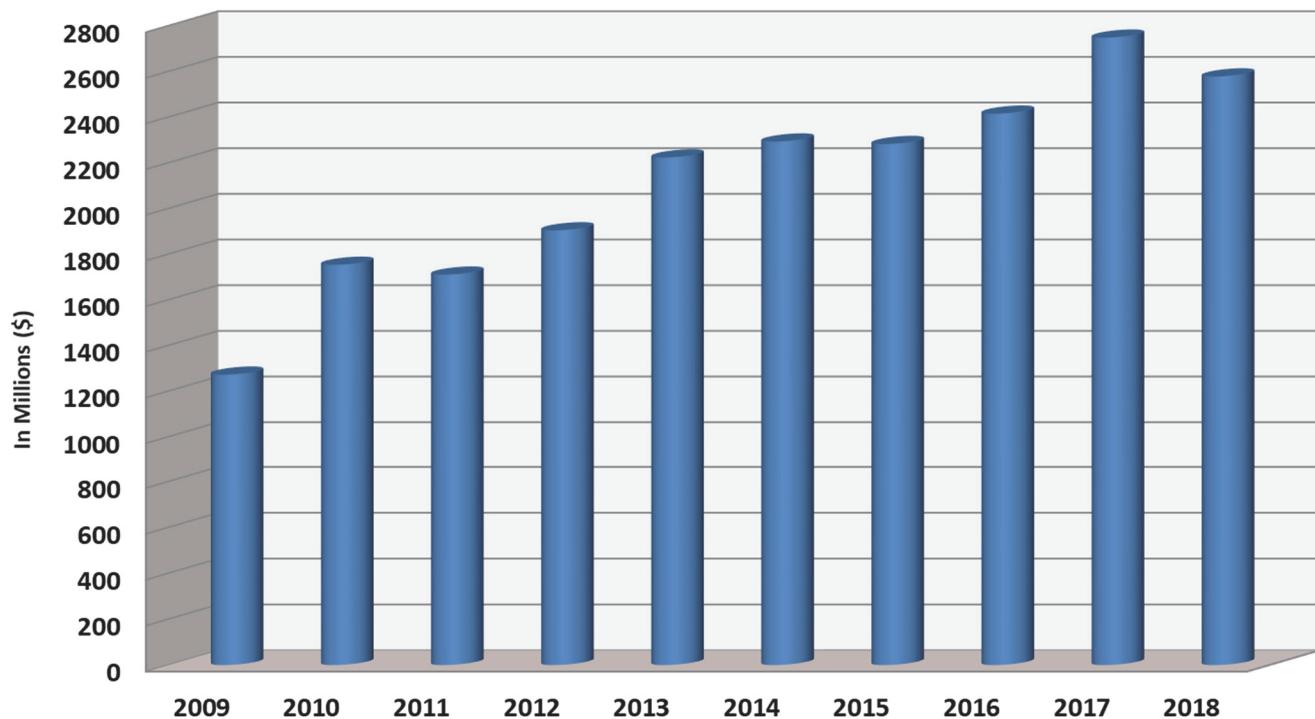
## FIDUCIARY NET POSITION RESTRICTED FOR PENSION BENEFITS

(All \$ in Millions)

Fiscal year ending 12/31	Total Fund Net Position	Increase (Decrease) in Net Position
2018	\$2,577.8	\$ (170.2)
2017	2,748.0	333.2
2016	2,414.8	132.7
2015	2,282.1	(11.4)
2014	2,293.5	70.7
2013	2,222.8	317.9
2012	1,904.9	195.1
2011	1,709.8	(43.0)
2010	1,752.8	480.3
2009	1,272.5	\$ 215.4

Fiduciary Net Position represents the net assets at fair value available to pay benefits. SCERA's Net Position as of December 31, 2018 is \$2,577.8 million. This amount reflects a decrease of 6%, primarily as a result of a net investment loss of \$107.1 million.

### SCERA Fiduciary Net Position Restricted for Pension Benefits



## INVESTMENT RETURNS

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## PENSION BENEFIT ASSETS AND INVESTMENT RETURNS

(All \$ in Millions) Fiscal Year Ended December 31, 2018

Investment	Market Value	Percent Actual	2018 Return	3-Year Return	5-Year Return
Fixed Income	\$ 491.1	18.7%	1.1%	3.4%	3.1%
Benchmark: BC Aggregate			0.0%	2.1%	2.5%
Real Assets	483.6	18.4%	8.3%	7.6%	9.1%
Benchmark: NCREIF ODCE Index			8.4%	8.2%	10.4%
Domestic Equity	497.0	18.9%	-6.0%	10.6%	9.6%
Benchmark: Russell 3000			-5.2%	9.0%	7.9%
Non-US Equity	514.2	19.6%	-13.3%	4.9%	1.4%
Benchmark: MSCI AC World ex-US IMI			-14.8%	4.4%	0.9%
Global Equity	357.1	13.6%	-11.2%	4.8%	3.0%
Benchmark: MSCI Global Equity Blend			-9.8%	6.8%	4.4%
Global Asset Allocation	127.0	4.9%	-5.8%	5.0%	2.6%
Benchmark: Global Asset Allocation Blend			-6.1%	5.4%	4.0%
Opportunistic	58.4	2.2%	14.0%	N/A	N/A
Cash	98.3	3.7%	1.8%	0.9%	0.6%
Total SCERA Fund	\$2,626.7	100%	-3.0%	7.3%	6.0%
Benchmark: SCERA Policy Index			-4.0%	6.4%	5.4%

This chart shows the fair value at fiscal year end, the actual percent of each asset type as a percentage of the entire portfolio and the investment returns for 1-year, 3-year and 5-year periods. The returns are shown before investment fees and administrative expenses. Benchmarks are market return comparisons for investments similar to the SCERA investment portfolio. The SCERA Policy Index provides an overall market return measure for the SCERA fund and represents the weighted average market return for SCERA investment classes.

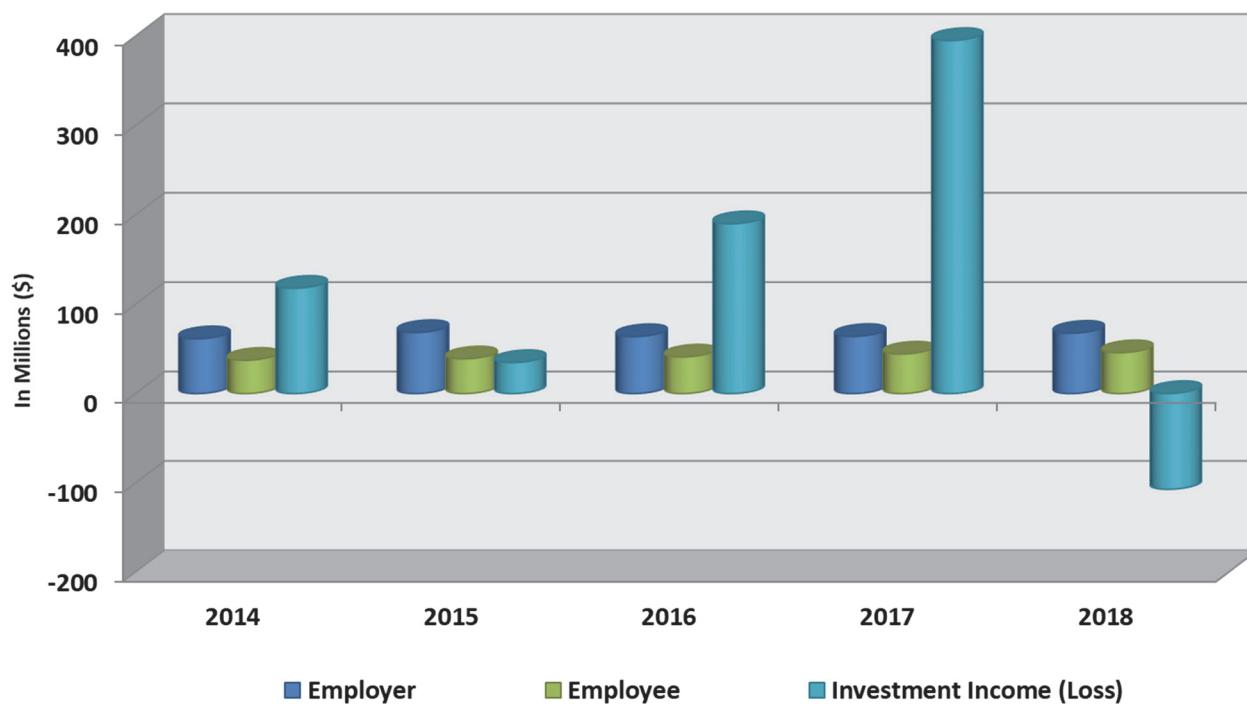
## FUND REVENUE

(All \$ in Millions)

Fiscal year ending 12/31	Employer Pension Contributions	Employee Pension Contributions	Net Investment Income (Loss)*	Total
2018	\$67.4	\$45.6	\$(107.1)	\$ 5.9
2017	63.8	44.2	394.9	502.9
2016	63.6	40.8	190.0	294.4
2015	68.2	38.7	34.6	141.5
2014	\$61.2	\$37.1	\$ 117.7	\$216.0

The primary sources to finance the benefits SCERA provides to its members are accumulated through income on investments and through the collection of employee and employer contributions. The income sources for the fiscal year ended December 31, 2018 totaled \$5.9 million. Negative investment income in 2018 was the result of weak returns across all asset classes other than real assets.

**SCERA Revenue**



\*Net Investment Income/(Loss) is the total interest and dividends earned by all investments as well as the change in fair value of all investments, less investment fees.

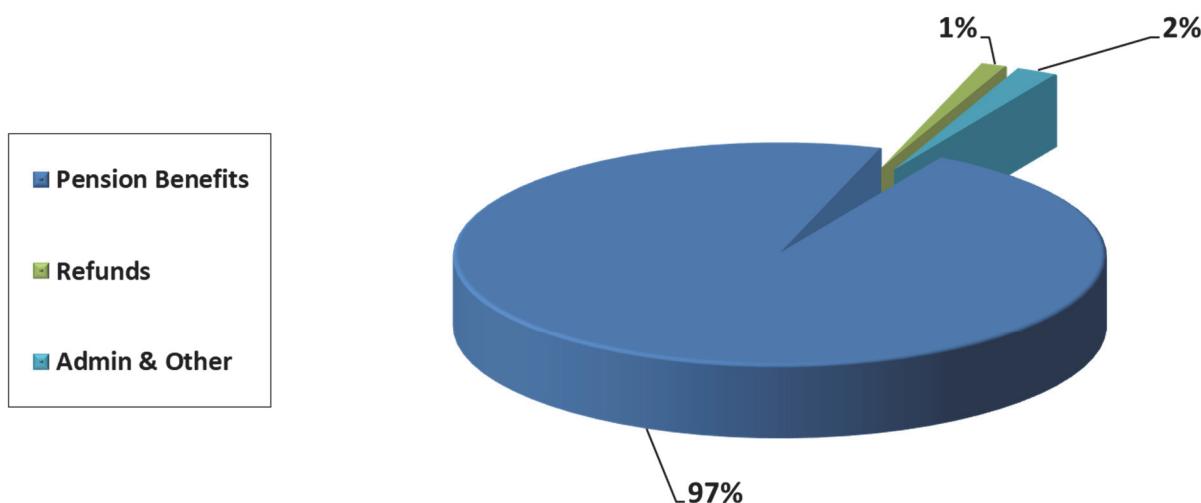
## FUND EXPENSES

(All \$ in Millions)

Fiscal year ending 12/31	Pension Benefits	Refunds	Admin & Other Expense	Total
2018	\$170.4	\$2.2	\$3.6	\$176.2
2017	163.0	3.0	3.7	169.7
2016	155.2	2.3	4.2	161.7
2015	147.3	2.1	3.5	152.9
2014	\$140.4	\$1.3	\$3.6	\$145.3

The primary uses of assets are the payment of pension benefits to retirees and their beneficiaries, refund of contributions to former employees, and the cost of administering the system. Pension Benefits increased 5% in 2018 due to an increasing number of retirees. Administrative and other expenses decreased by 4% in 2018, attributable mostly to a decrease in staff salaries.

**SCERA Expenses**



## FUNDED RATIO

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Actuarial Valuation Date	Funded Ratio
12/31/18	86.8%
12/31/17	87.7%
12/31/16	85.5%
12/31/15	84.9%
12/31/14	86.3%

SCERA's funding objective is to meet benefit promises by achieving long-term funding of the cost of benefits, seeking reasonable and equitable allocation of those costs, minimizing volatility of contributions where possible and consistent with other policy goals, and obtaining optimum returns consistent with the assumption of prudent risk. As of the latest actuarial valuation, the funded status (the ratio of SCERA assets to SCERA liabilities) is 86.8%.

## HISTORICAL MEMBERSHIP

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Fiscal year ending 12/31	Number of Active Members	Number of Retired Members & Beneficiaries	Average Annual Benefit Received
2018	4,021	5,096	\$34,247
2017	4,110	4,936	33,591
2016	4,112	4,812	32,961
2015	4,071	4,653	32,286
2014	3,922	4,506	\$31,739

Membership includes the total number of active employees paying into the plan and the total number of retired members and beneficiaries drawing monthly pension benefits.

Average Annual Benefit is the average benefit received including the basic retirement pension plus COLAs.

## **ISSUED BY**

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Julie Wyne, *Chief Executive Officer*

Kelly Jenkins, *Assistant Chief Executive Officer*

Cathy Austin, *Finance and Retiree Services Manager*

James Failor, *Chief Investment Officer*

More detailed information can be found in the  
CAFR which is available at:

SCERA  
433 Aviation Boulevard, Suite 100  
Santa Rosa, CA 95403

or on our website at [www.scretire.org](http://www.scretire.org).

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433 Aviation Boulevard, Suite 100  
Santa Rosa, CA 95403-9089

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