Popular Annual Financial Report for the Year ended June 30, 2018
City of San Jose, California
Police and Fire Department Retirement Plan

INTRODUCTION

The Police and Fire Department Retirement Plan (Plan) is pleased to present the Popular Annual Financial Report (PAFR) which summarizes the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2018. The financial data presented in the PAFR is derived from the CAFR and is consistent with Accounting Principles Generally Accepted in the United States of America (U.S. GAAP). The PAFR provides a concise summary of the Plan's financial position, investment performance and key accomplishments throughout the fiscal year. The Plan consists of a single employer Defined Benefit Pension Plan and a Postemployment Healthcare Plan.

For fiscal year 2018, the Defined Benefit Pension Plan returned 7.3% gross of fees and 6.9% net of fees, while the Policy Benchmark return for the same time period was 7.6%. The Plan's fiscal year performance was greater than the actuarial rate of return of 6.875%. For fiscal year 2018, the Postemployment Healthcare Plan returned 3.6% net of fees.

The Plan engages an independent actuary to conduct annual actuarial valuations. The June 30, 2017 actuarial valuations show that the Defined Benefit Pension Plan and the Postemployment Healthcare Plan are 77.1% and 21.0% funded, respectively. The Defined Benefit Pension Plan sponsor paid 100% of the Actuarially Determined Contribution in fiscal year 2018, while the Postemployment Healthcare Plan sponsor paid the amount that was agreed between the Plan sponsor and the employee bargaining units.

This report is not intended to replace the CAFR, which provides a more complete overview of the Plan's financial position and operating results. For more in-depth information, we encourage you to read the CAFR by visiting **www.sjretirement.com** and clicking on the Reports tab.

Board of Administration

The Plan's Board of Administration oversees the Chief Executive Officer of the Office of Retirement Services and staff in the performance of their duties. The Plan's Board Members as of June 30, 2018 were:

Net Position Held in Trust

As of June 30, 2018, the Plan's total plan net position for the Defined Benefit Pension Plan totaled $3.5 billion, while the Postemployment Healthcare Plan net position totaled $162.5 million. The funded ratio for the Defined Benefit Plan and Postemployment Healthcare Plan was 77.1% and 21.0%, respectively, as of June 30, 2017, the date of the Plan's most recent actuarial valuation.

NET POSITION FOR THE POLICE AND FIRE DEPARTMENT RETIREMENT PLAN'S DEFINED BENEFIT PENSION PLAN *As of June 30, 2018 and 2017 (In Thousands)*

	2018	2017	Increase/(Decrease) Amount	Increase/(Decrease) Percent
Receivables	$ 9,900	$ 19,014	$ (9,114)	(47.9)%
Investments at fair value	3,491,602	3,277,084	214,518	6.5 %
Capital assets	1,726	1,488	238	16.0 %
Total Assets	**3,503,228**	**3,297,586**	**205,642**	**6.2 %**
Current liabilities	7,037	4,329	2,708	62.6 %
Total Liabilities	**7,037**	**4,329**	**2,708**	**62.6 %**
Plan Net Position	**$ 3,496,191**	**$ 3,293,257**	**$ 202,934**	**6.2 %**

NET POSITION FOR THE POLICE AND FIRE DEPARTMENT RETIREMENT PLAN'S POSTEMPLOYMENT HEALTHCARE PLAN *As of June 30, 2018 and 2017 (In Thousands)*

	2018	2017	Increase/(Decrease) Amount	Increase/(Decrease) Percent
Receivables	$ 18,295	$ 3,859	$ 14,436	374.1 %
Investments at fair value	152,091	145,935	6,156	4.2 %
Capital assets	29	25	4	16.0 %
Total Assets	**170,415**	**149,819**	**20,596**	**13.7 %**
Current liabilities	7,895	137	7,758	5,662.8 %
Total Liabilities	**7,895**	**137**	**7,758**	**5,662.8 %**
Plan Net Position	**$ 162,520**	**$ 149,682**	**$ 12,838**	**8.6 %**

Changes in Net Position for the years ended June 30, 2018 and 2017

As of June 30, 2018, the net position restricted for pension benefits increased by $202.9 million or 6.2% over 2017, due to total additions being greater than total deductions. However, total additions decreased by $(35,243,000) mainly as a result of the decrease in net investment income of $(59,259,000), due to less favorable market conditions in 2018 compared to 2017, which was offset with the increase in employer contributions. In addition, total deductions increased by $11,427,000 due to an increase in benefit payments from rising pension benefit costs caused by an increase in the number of retirees, as well as the increase in the final average salary used to calculate the pension benefits.

CHANGES IN PLAN NET POSITION FOR THE DEFINED BENEFIT PENSION PLAN

For the Fiscal Years Ended June 30, 2018 and 2017 (In Thousands)

	2018	2017	Increase/(Decrease) Amount	Increase/(Decrease) Percent
Employee contributions	$ 23,841	$ 20,580	$ 3,261	15.8 %
Employer contributions	157,712	136,957	20,755	15.2 %
Net investment income*	233,475	292,734	(59,259)	(20.2)%
Total Additions	**415,028**	**450,271**	**(35,243)**	**(7.8)%**
Retirement benefits	194,139	184,596	9,543	5.2 %
Death benefits	12,102	11,072	1,030	9.3 %
Refund of contributions	389	364	25	6.9 %
Administrative expenses	5,464	4,635	829	17.9 %
Total Deductions	**212,094**	**200,667**	**11,427**	**5.7 %**
Net Increase in Plan Net Position	**202,934**	**249,604**	**(46,670)**	**(18.7)%**
Beginning Net Position	**3,293,257**	**3,043,653**	**249,604**	**8.2 %**
Ending Net Position	**$ 3,496,191**	**$ 3,293,257**	**$ 202,934**	**6.2 %**

** Net of investment expenses of $18,845 and $19,288 in 2018 and 2017, respectively.*

As of June 30, 2018, the net position restricted for postemployment healthcare benefits increased by $12.8 million or 8.6% over 2017, due to total additions being greater than total deductions. However, total additions decreased by $(2,656,000) mainly as a result of the decrease in net investment income of $(5,382,000), due to less favorable market conditions in 2018 compared to 2017, which was offset with the increase in employer contributions. In addition, total deductions increased by $10,761,000, due to the implementation of the Voluntary Employee Beneficiary Association (VEBA), which transferred assets out of the postemployment healthcare plan and into the VEBA defined contribution plan. The VEBA is administered by the City and not the Office of Retirement Services.

CHANGES IN PLAN NET POSITION FOR THE POSTEMPLOYMENT HEALTHCARE PLAN

For the Fiscal Years Ended June 30, 2018 and 2017 (In Thousands)

	2018	2017	Increase/(Decrease) Amount	Increase/(Decrease) Percent
Employee contributions	$ 16,127	$ 18,116	$ (1,989)	(11.0)%
Employer contributions	25,382	20,667	4,715	22.8 %
Net investment income*	7,071	12,453	(5,382)	(43.2)%
Total Additions	**48,580**	**51,236**	**(2,656)**	**(5.2)%**
Healthcare insurance premiums	27,686	24,799	2,887	11.6 %
Administrative expenses	159	182	(23)	(12.6)%
VEBA transfer	7,897	-	7,897	100.00%
Total Deductions	**35,742**	**24,981**	**10,761**	**43.1 %**
Net Increase in Plan Net Position	**12,838**	**26,255**	**(13,417)**	**(51.1)%**
Beginning Net Position	**149,682**	**123,427**	**26,255**	**21.3 %**
Ending Net Position	**$ 162,520**	**$ 149,682**	**$ 12,838**	**8.6 %**

** Net of investment expenses of $405 and $434 in 2018 and 2017, respectively.*

Changes in Net Position for the years ended June 30, 2018 and 2017 (continued)

The primary sources (additions) used to fund benefits provided by the Plan are accumulated through employee and employer contributions and by investment earnings (net of investment expenses). The primary uses (deductions) of the Plan's assets include benefit payments to retirees and beneficiaries, contribution refunds to terminated employees and the costs of administering the Plan.

Membership (as of June 30, 2018 and 2017)

	Retirees and beneficiaries currently receiving benefits*		Terminated vested members not yet receiving benefits		Active Members		Total	
PENSION	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**
Police Tier 1	1,373	1,336	227	239	717	747	**2,317**	**2,322**
Police Tier 2	-	-	53	49	258	150	**311**	**199**
Fire Tier 1	877	856	39	39	561	586	**1,477**	**1,481**
Fire Tier 2	-	-	4	6	103	61	**107**	**67**
Total	**2,250**	**2,192**	**323**	**333**	**1,639**	**1,544**	**4,212**	**4,069**
HEALTHCARE								
Police Tier 1	1,272	1,251	16	12	684	747	**1,972**	**2,010**
Police Tier 2	-	-	-	-	-	150	**-**	**150**
Fire Tier 1	830	810	-	1	534	586	**1,364**	**1,397**
Fire Tier 2	-	-	-	-	-	61	**-**	**61**
Total	**2,102**	**2,061**	**16**	**13**	**1,218**	**1,544**	**3,336**	**3,618**

** The number of combined domestic relations orders recipients is not included in the count above, as their benefit payment is included in the member's count.*

Average Benefit Payments

The Average Benefit Payment chart is a broad representation of average benefits paid to retirees and survivors. All tiers are combined in the calculation. The chart includes all members who have retired through June 30, 2018.

PENSION	**Years of Service Credit**						
Time Periods	**0-5**	**6-10**	**11-15**	**16-20**	**21-25**	**26-30**	**31+**
Average monthly benefit*	$ 2,595	$ 3,902	$ 4,487	$ 5,630	$ 7,934	$10,174	$10,961
Avg final avg monthly salary (FAS)**	$ 6,169	$ 5,522	$ 7,284	$ 8,701	$ 9,285	$ 9,262	$ 8,558
Number of retired members***	12	49	122	183	461	791	160
Average monthly benefit (No FAS)*,	$ -	$ 2,112	$ 1,747	$ 3,290	$ 5,030	$ 7,580	$ 8,683
Number of retired members***	-	3	2	8	27	101	21

HEALTHCARE	**Years of Service Credit**						
Time Periods	**0-5**	**6-10**	**11-15**	**16-20**	**21-25**	**26-30**	**31+**
Average health subsidy	$ 600	$ 693	$ 797	$ 701	$ 759	$ 749	$ 654
Number of health participants ***	7	39	88	154	465	890	173
Average dental subsidy	$ 93	$ 105	$ 116	$ 112	$ 109	$ 109	$ 103
Number of dental participants ***	8	44	92	157	476	906	175

* *Includes cost of living increases*

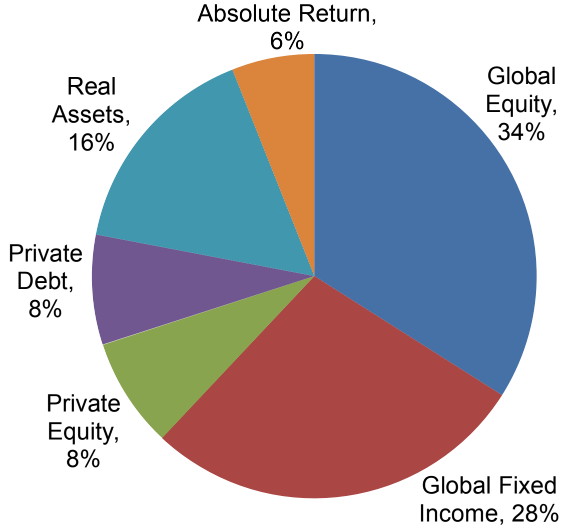
** *Final average salary not available for those that retired prior to April 1998, except for service-connected disability retirees. Those without final average salary are not included in average monthly benefit.*

*** *Does not include survivors and ex-spouses*

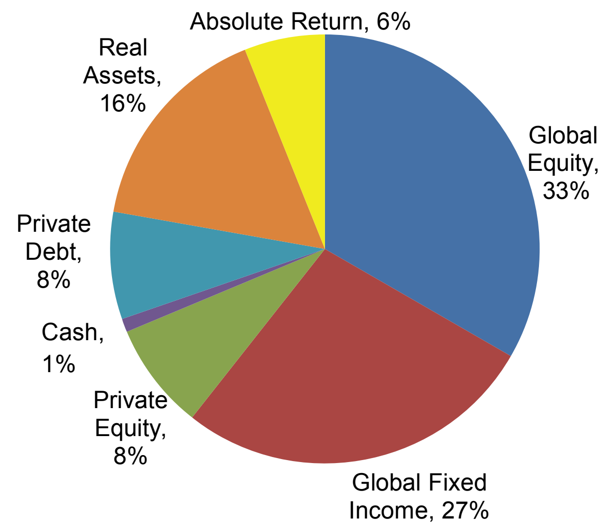
Asset Allocation (as of June 30, 2018)

The allocation of the Plan's assets is an integral part of the Plan's investment policy. As such, the Plan engages in periodic reviews of its asset allocation policy to ensure that assets are diversified in a manner which achieves the best risk adjusted returns for the Plan. In addition, the asset allocation is intended to minimize the volatility of the Plan's assets and mitigate the risk of large investment losses during times of prolonged market stress. The Plan's Chief Investment Officer and investment consultant, Meketa, assist the Board in designing the asset allocation and strategic diversification strategies within asset classes.

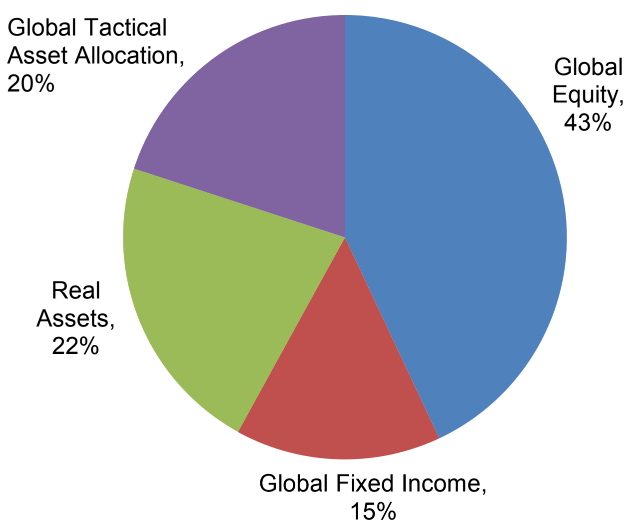
Pension - Target Asset Allocation



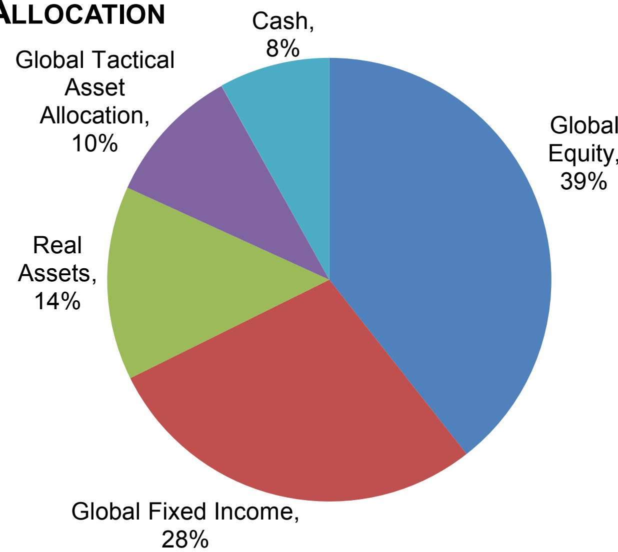
Pension - Actual Asset Allocation



Healthcare - Target Asset Allocation



Healthcare - Actual Asset Allocation



Real assets include real estate, commodities and infrastructure.

Absolute return includes hedge funds.

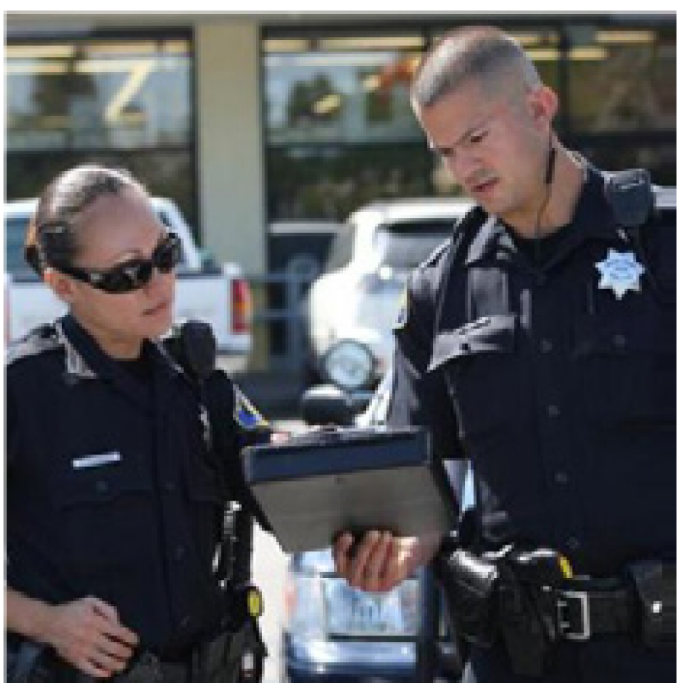
Investment Returns Based on Fair Value* (as of June 30, 2018)

PENSION	One Year	Three Years	Five Years	Ten Years
Global equity	10.3%	8.2%	9.3%	6.2%
Private equity	13.6%	10.4%	11.9%	8.9%
Global fixed income	3.0%	3.7%	3.6%	6.1%
Real assets	9.2%	4.5%	N/A	N/A
Private debt	1.2%	N/A	N/A	N/A
Absolute return	4.4%	1.9%	2.6%	N/A
Total fund (net)	**6.9%**	**5.2%**	**5.6%**	**4.6%**
Policy benchmark	**7.6%**	**6.0%**	**6.2%**	**4.9%**

HEALTHCARE	One Year	Three Years	Five Years	Ten Years
Global equity	11.1%	8.5%	9.8%	N/A
Global fixed income	(0.4)%	1.7%	2.2%	N/A
Real assets	4.9%	3.9%	N/A	N/A
Global tactical asset allocation	0.8%	1.5%	N/A	N/A
Total fund (net)	**3.6%**	**3.6%**	**4.6%**	**N/A**
Policy benchmark	**7.4%**	**6.0%**	**6.1%**	**N/A**

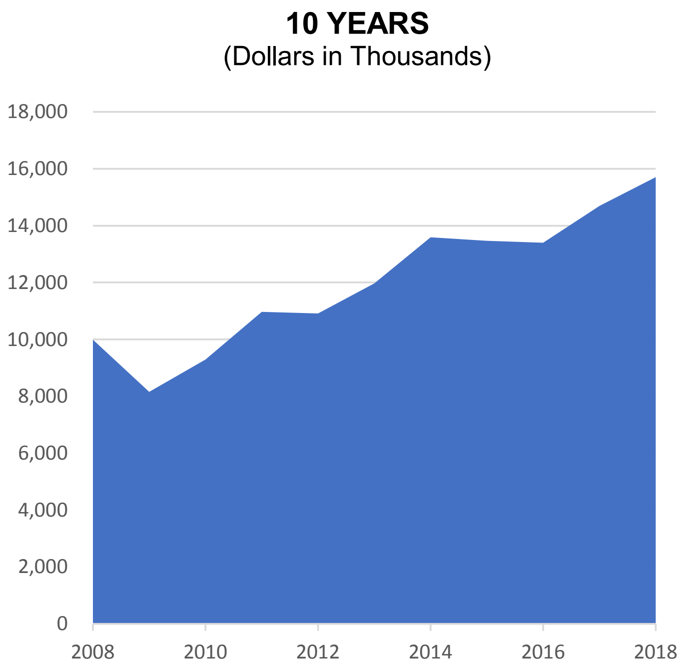
** Using time-weighted rate of return based on the market rate of return*

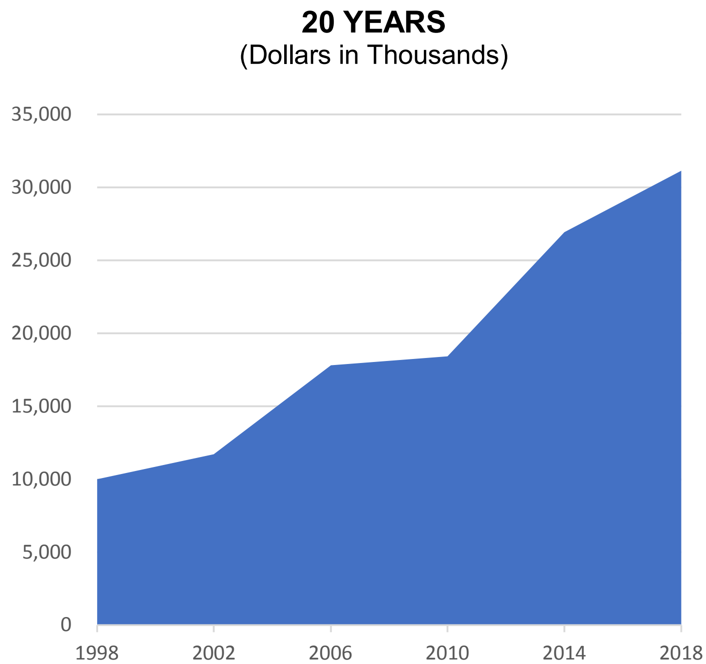
As stated in the Plan's investment policy, "the primary objective of the investment portfolio is to satisfy the Plan's obligations to pay benefits to members of the Plan and their beneficiaries. To do so, the Fund will seek to achieve long-term net returns in excess of the actuarial investment return assumption while maintaining a reasonable level of investment risk." In order to achieve this objective, the Investment Policy further states that "the Plan's fund will be managed as an ongoing concern with a long-term investment time horizon, consistent with the demographic profile of the Plan's members and beneficiaries." As such, "Investments shall be diversified with the intent to minimize the risks of large investment losses. Consequently, the total portfolio will be constructed and maintained to provide prudent diversification with regard to the concentration of holdings in individual asset classes, issues, issuers, geographics, or industries. Furthermore, assets will be assigned to a variety of investment managers that employ a range of investment management strategies." For the year ended June 30, 2018, the Defined Benefit Pension Plan returned 7.3% gross of fees and 6.9% net of fees, while the Policy Benchmark return for the same period was 7.6%.



Growth of $10,000 **(as of June 30, 2018)**

Below are the graphic trends to show how much an initial investment of $10,000 would be worth in the Retirement Plan's pension portfolios after 10 years and 20 years. There is not enough data available to show 30 years.

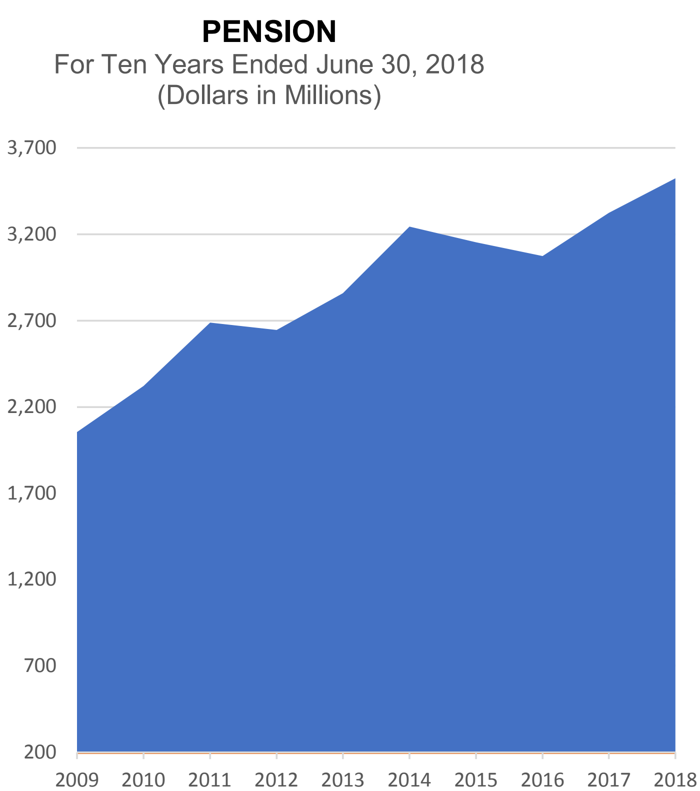


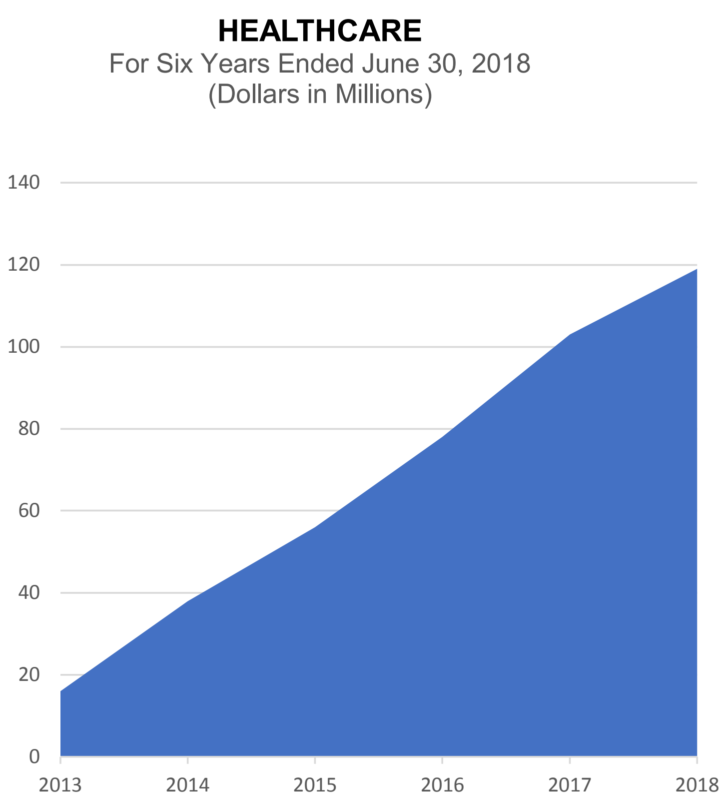


Source: State Street

Market Value Growth of Plan Assets **(as of June 30, 2018)**

Below are the market value growth of pension and healthcare plan assets for the years ended June 30, 2018.





Funding Status

The Plan hires an independent consultant to conduct annual actuarial valuations of pension assets and expenses. The actuarial values are compared to determine the annual contribution rates that the employer is required to pay to meet ongoing pension obligations. The actuarial value of assets differs from the market value of assets because gains and losses are "smoothed" over a 5 year period to minimize the effect of market volatility on contribution rates. The table below represents the actuarial report that was current as of June 30, 2017; please check the Plan's website for more current numbers and information on the Net Pension Liability calculation required by GASB 67 and the Net OPEB Liability calculation required by GASB 74.

SCHEDULE OF FUNDING PROGRESS - DEFINED BENEFIT PENSION PLAN (Unaudited)
(Amounts in thousands)

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Liability (AL)	Unfunded AL	Funded Ratio	Covered Payroll	Unfunded AL as a % of Covered Payroll
June 30, 2017	$3,439,922	$4,464,402	$1,024,480	77.1%	$203,816	502.6%
June 30, 2016	$3,303,550	$4,355,990	$1,052,440	75.8%	$194,072	542.3%
June 30, 2015	$3,212,776	$4,058,410	$845,634	79.2%	$184,733	457.8%
June 30, 2014	$3,025,101	$3,813,825	$788,724	79.3%	$188,189	419.1%
June 30, 2013	$2,771,924	$3,578,031	$806,107	77.5%	$184,645	436.6%

SCHEDULE OF FUNDING PROGRESS - POSTEMPLOYMENT HEALTHCARE PLAN (Unaudited)
(Amounts in thousands)

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Liability (AL)	Unfunded AL	Funded Ratio	Covered Payroll	Unfunded AL as a % of Covered Payroll
June 30, 2017	$142,517	$680,246	$537,729	21.0%	$203,816	263.8%
June 30, 2016	$135,207	$778,871	$643,664	17.4%	$194,072	331.7%
June 30, 2015	$114,565	$739,753	$625,188	15.5%	$184,733	338.4%
June 30, 2014	$93,605	$706,710	$613,105	13.2%	$188,189	325.8%
June 30, 2013	$75,035	$700,525	$625,490	10.7%	$184,645	338.8%

Schedule of Employer and Employee Contributions

Employer and employee basic and COLA (Cost of Living Adjustment) contributions are based on statute and rates recommended by an independent actuary and adopted by the Retirement Board. The rates are set to provide a retirement benefit equal to a fractional part of the highest year(s) salary, depending on membership and tier.

(In Thousands)	PENSION		HEALTHCARE	
Year Ended	Employer Contributions	Employee Contributions	Employer Contributions	Employee Contributions
June 30, 2018	$157,712	$23,841	$25,382	$16,127
June 30, 2017	$136,957	$20,580	$20,667	$18,116
June 30, 2016	$132,480	$21,508	$21,065	$18,007
June 30, 2015	$129,279	$20,747	$20,910	$17,017
June 30, 2014	$123,583	$21,115	$17,267	$15,674

The Plan's actuarial valuations are calculated as of June 30 of each year. Actuarially determined contribution rates are calculated based on the actuarial valuation one year prior to the beginning of the plan year.

Noteworthy Accomplishments

The Office of Retirement Services began the implementation of its new pension administration system in March 2015. The implementation process is expected to last approximately 42 months and is estimated at $9 million. ORS has completed the user acceptance testing for Software Deliverable 5 (the last planned deliverable) and is currently training staff on the new system, as well as starting the parallel processing phase of the implementation. The project completion was extended to the summer of 2019 for the implementation of Measure F-related calculations in the system.

ORS continued to implement the pensionable pay correction project (PPC) for the members of the Plan. The purpose is to correct retirement benefits paid to some retirees, due to errors in the City's reporting to ORS of pensionable pay information that was then used in the member's benefit calculation. The project was completed in December 2017, after the corrections to the ongoing benefit payments and the remittance of the past total underpayments for the non-FLSA (Fair Labor Standard Act) group were made.

In November 2016, Measure F passed, and on March 31,2017, the ordinance implementing the Framework and Measure F became effective for employees in the Plan. The provisions of the Framework include, but are not limited to, revising Tier 2 benefit, allowing rehired Tier 1 employees to remain in Tier 1, creating a Voluntary Employee Beneficiary Association (VEBA) for retiree healthcare and an irrevocable opt-out of the defined benefit retiree healthcare plan for eligible employees, defining the qualifications for members of the independent medical panel, and creating a Guaranteed Purchasing Power (GPP) benefit for Tier 1 retirees. The VEBA is being administered by the City, not ORS, and therefore it is also not under the jurisdiction of the Retirement Board.

During this fiscal year, ORS completed most of the implementation of Measure F, with the transfer of the contributions of members who opted in to the VEBA. In addition, ORS made the first payments to those affected by the GPP and included the retiree healthcare in-lieu premium credit as part of the open enrollment process for retirees. Retirees who are eligible for medical insurance and/or dental insurance but who opt not to take it, can elect to be in the in-lieu credit program. These members are given credits worth 25% of the lowest cost plan, which can be used in future years if the retiree opts to enroll in a City medical or dental plan. There are still a few aspects of Measure F that are outstanding such as the medical panel and the refinement of the Municipal Code to be consistent with the current procedures of the City.

In October 2017, the City Auditor issued report 17-06, *Audit of Retirement Services: Greater Transparency Needed in the Budgeting Process, Interactions Among Stakeholders, Investment Policies, and Plan Administration*. This audit was a result of a request from the Mayor’s Office, in which concern was expressed that although ORS’ administrative budget has increased since fiscal year 2005-2006, the plans had seen losses in the two fiscal years prior to fiscal year 2017. The report was published with five separate findings which are covered in 25 different recommendations. Four of the 25 recommendations are addressed to the City, and ORS has addressed and completed most of the findings over which they have control. In addition to this audit, the City Auditor conducted a pensionable earnings audit but the result was favorable, and no recommendations to ORS came out of it.

Awards for Excellence in Financial Reporting

The Plan's CAFR for the year ended 2018, from which information on pages 1-9 has been drawn, was awarded the Certificate of Achievement for Excellence in Financial Reporting by Government Finance Officers Association of the United States and Canada (GFOA) for the fiscal year ended June 30, 2017. The Certificate of Achievement is the highest form of recognition for excellence in state and local government financial reporting.

In order to be awarded a Cerfiticate of Achievement, a government unit must publish an easily readable and efficiently organized CAFR, whose contents conform to program standards. Such a CAFR must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe that our current CAFR continues to conform to the Certificate of Achievement's Program's requirements, and we are submitting it to GFOA to determine its eligibility for another Certificate.

GFOA has given an award for Oustanding Achievement in Popular Annual Financial Reporting to the Plan for its PAFR for the fiscal year ended June 30, 2017. The Award for Outstanding Achievement in Popular Annual Financial Reporting is a prestigious national award recognizing conformance with the highest standards for preparation of state and local government popular reports. In order to receive an Award for Outstanding Achievement in Popular Annual Financial Reporting, a government unit must publish a PAFR, whose contents conform to program standards of creativity, presentation, understandability, and reader appeal.

An Award for Outstanding Achievement in Popular Annual Financial Reporting is valid for a period of one year only. The Plan has received a Popular Award for the second year for the fiscal year ended June 30, 2017. We believe our current report continues to conform to the Popular Annual Financial Reporting requirements, and we are submitting it to GFOA to determine its eligibility for another Award.

The Plan has also earned the Public Pension Coordinating Council's (PPCC) Public Standards Award for 2003, 2007, and 2009 through 2017. The Public Pensions Standards are intended to reflect the minimum expectations for public retirement system management and administration, and to serve as a benchmark by which all defined benefit public plans should be measured.