MENDOCINO COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

(Pension Trust Fund and Component Unit of the County of Mendocino, California)

COMPREHENSIVE ANNUAL FINANCIAL REPORT

For the Years Ended
June 30, 2010 and 2009

TABLE OF CONTENTS

INTRODUCTION

Transmittal Letter....................................3
Board of Retirement................................7
Organizational Chart...............................8
Professional Consultants..........................9

FINANCIAL

Independent Auditor's Report................11
Management Discussion and Analysis...13

BASIC FINANCIAL STATEMENTS

Statements of Plan Net Assets Available for Benefits............................20
Statements of Changes in Plan Net Assets Available for Benefits.................21
Notes to the Financial Statements..........22

SUPPLEMENTARY INFORMATION

Schedule of Funding Progress 36
Schedule of Employer Contributions.....37
Schedule of Administrative Expenses ...38
Schedule of Investment Expenses..........39

INVESTMENT

Investment Consultants Report.............41
Asset Allocation....................................43

ACTUARIAL

Due to a Change in Primary Actuarial Consultants from Buck Consultants to The Segal Company in March of 2011, the Actuarial Section of this Report will be Continued in the June 30, 2011 and 2010 Report.

Introductory Section

James M. Andersen
Retirement Administrator

Telephone: (707) 463-4328
(707) 467-6473
Fax: (707) 467-6472

MENDOCINO COUNTY
EMPLOYEES' RETIREMENT ASSOCIATION
625-B KINGS COURT
UKIAH, CALIFORNIA 95482-5027

May 31, 2011

Board of Retirement
Mendocino County Employees' Retirement Association
Ukiah, CA 95482

Dear Board Members:

Please find enclosed the annual financial report of the Mendocino County Employees' Retirement Association (MCERA) for the fiscal years ending June 30, 2010 and 2009.

MCERA is a multi-agency public employees' retirement system, established by the County of Mendocino on January 1, 1948. MCERA is operated and administered by the Board of Retirement (Board) to provide retirement, disability, death and survivors benefits for its members under the California State Government Code, Section 31450 et seq. (County Employees' Retirement Law of 1937).

Report Contents

MCERA management is responsible for both the accuracy of the data and the completeness and fairness of the presentation of financial information within this CAFR, including all disclosures. The Comprehensive Annual Financial Report is divided into four sections:

The *Introductory Section* describes the organization and structure of MCERA, including this transmittal letter and a list of professional consultants.

The *Financial Section* presents the basic financial statements, report of the independent auditor, management discussion and analysis and supplemental schedules and notes to the financial statements.

The *Investment Section* reports on investment activity, investment policy, asset allocation and diversification and historical investment performance.

The *Actuarial Section* communicates the Plan's funding status and presents related actuarial information. It also contains the actuarial certification, actuarial assumptions and statistics and general plan information. As noted in the table of contents, the Actuarial Section is omitted from this report due to a change in primary actuaries in March of 2011. The Actuarial Section of the report will be prepared for the June 30, 2011 and 2010 report.

MCERA and its Services

MCERA was established by Mendocino County to provide retirement allowances and other benefits to general and safety members employed by Mendocino County. Currently Mendocino County, the Mendocino County Superior Courts, and the Russian River Cemetery District are participating agencies of MCERA.

MCERA is governed by the California Constitution, the County Employees Retirement Law of 1937 (CERL), and the bylaws, regulations, policies and procedures adopted by the Board of Retirement. The Mendocino County Board of Supervisors may also adopt resolutions, as permitted by CERL, which may affect benefits to MCERA members.

The Board of Retirement is responsible for the management of MCERA and is comprised of nine members and one alternate member; the alternate member is a retiree alternate. Four board members are appointed by the Mendocino County Board of Supervisors, one board member is elected by the safety members, two board members are elected by the general members, and one board member and the alternate retiree member are elected by the retired members. The County Treasurer serves as an ex-officio member. Board members, with the exception of the County Treasurer, serve three-year terms with no term limits.

Financial Information

The accompanying financial statements are prepared using the accrual basis of accounting. Contributions from employers and members are recognized as revenue when earned. Expenses are recorded when corresponding liabilities are incurred, regardless of when payment is due or made. Investments are recorded at the fair market value of the assets.

An overview of MCERA's fiscal operations for the years ended June 30, 2010 and 2009 are presented in Management's Discussion and Analysis (MD&A) located in the financial section of the CAFR. This transmittal letter, together with MD&A, provides an expanded view of the activities of MCERA.

MCERA's independent auditor, Jim Sligh, CPA, has audited the accompanying financial statements. Management believes an adequate system of internal control is in place and the accompanying statements, schedules and tables are fairly presented and free from material misstatements.

Actuarial Funding Status

MCERA's funding objective is to meet long-term benefit obligations by maintaining a well-funded plan status and obtaining optimum investment returns. Pursuant to CERL, MCERA engages an independent actuary to perform an actuarial valuation of the system on an annual basis. Economic assumptions are reviewed annually. Additionally, every three years, a triennial experience study is conducted, at which time non-economic assumptions are also updated. The most recent triennial experience study was conducted as of June 30, 2008 by Buck Consultants. Buck Consultants conducted the last actuarial valuation as of June 30, 2010 and determined the plan's funding ratio (ratio of plan assets to plan liabilities) to be 78.9% using the recommended assumptions, down from 83.4% in 2009. MCERA entered into an agreement with EFI Actuaries to audit the most recent triennial experience study and the June 30, 2009 actuarial valuation prepared by Buck Consultants. As a result of the findings and recommendations in the audit, MCERA exited its agreement with Buck Consultants and entered into an agreement with The Segal Company for primary actuarial services. The findings and recommendations of the audit will also be reviewed in the fall of 2011, when The Segal Company performs a triennial experience study for the fiscal years ending 2009 through 2011 and actuarial valuation for June 30, 2011.

Mendocino County issued $31 million of pension obligation bonds in December 1996 and $76 million of pension obligation bonds in December 2002 to satisfy the Unfunded Accrued Actuarial Liability (UAAL) for the County, calculated as of that date.

Investments

The Board of Retirement has exclusive control of all MCERA investments and is responsible for establishing investment objectives, strategies and policies. The California Constitution and Government Code Sections 31594 and 31595 authorized the Board of Retirement to invest in any investment deemed prudent in the Board's opinion.

The Board has adopted an Investment Policy Statement, which provides a framework for the management of MCERA's investments. This policy establishes MCERA's investment objectives and defines the duties of the Board of Retirement and investment managers. The asset allocation is an integral part of the Investment Policy Statement and is designed to provide an optimum mix of asset classes with return expectations to ensure growth of assets to meet future liabilities, minimize employer contributions and defray reasonable administrative costs. MCERA engages an Investment Consultant to analyze its investment policy and strategy, and to conduct periodic asset allocation studies. For fiscal years ended June 30, 2010 and June 30, 2009, the Plan's investments provided 14.47% and (16.5%) rates of return, respectively. A summary of the asset allocation can be found in the Investment Section of this report.

Service Efforts and Accomplishments

In June of 2010, the Board of Retirement concluded a review of its liabilities and assets, and developed a new Investment Policy Statement. The MD&A section of this report includes more on the asset allocations and rebalancing that have occurred since that date. In addition, the Board of Retirement adopted a new Interest Posting and Undistributed Earnings Policy, with the goal of investing all future excess earnings in pension assets until the retirement system's funded ratio is 100% (assets to liabilities).

The Board of Retirement directed and received an Information Technology Strategic Plan which will guide technology improvements into the future. The initiatives have been placed on hold while system assets and the MCERA's funded status recover, and while the plan sponsors develop long term financial plans for meeting their annually required contributions. Finally, the Board of Retirement completed an application to the Internal Revenue Service (IRS) for a Determination Letter and Voluntary Correction Program in an effort to ensure continued IRS compliance and tax-deferred status of the plan. The application process has shed light on several areas where policy and procedures need to be clarified or developed.

Acknowledgements

The compilation of this report reflects the combined effort of MCERA's staff. It is intended to provide reliable information as the basis for making management decisions, as a means for determining compliance with legal provisions and as a means of determining responsible stewardship of the funds of MCERA. Both the accuracy of the data presented and the completeness and fairness of the presentation of the CAFR is the responsibility of the management of MCERA.

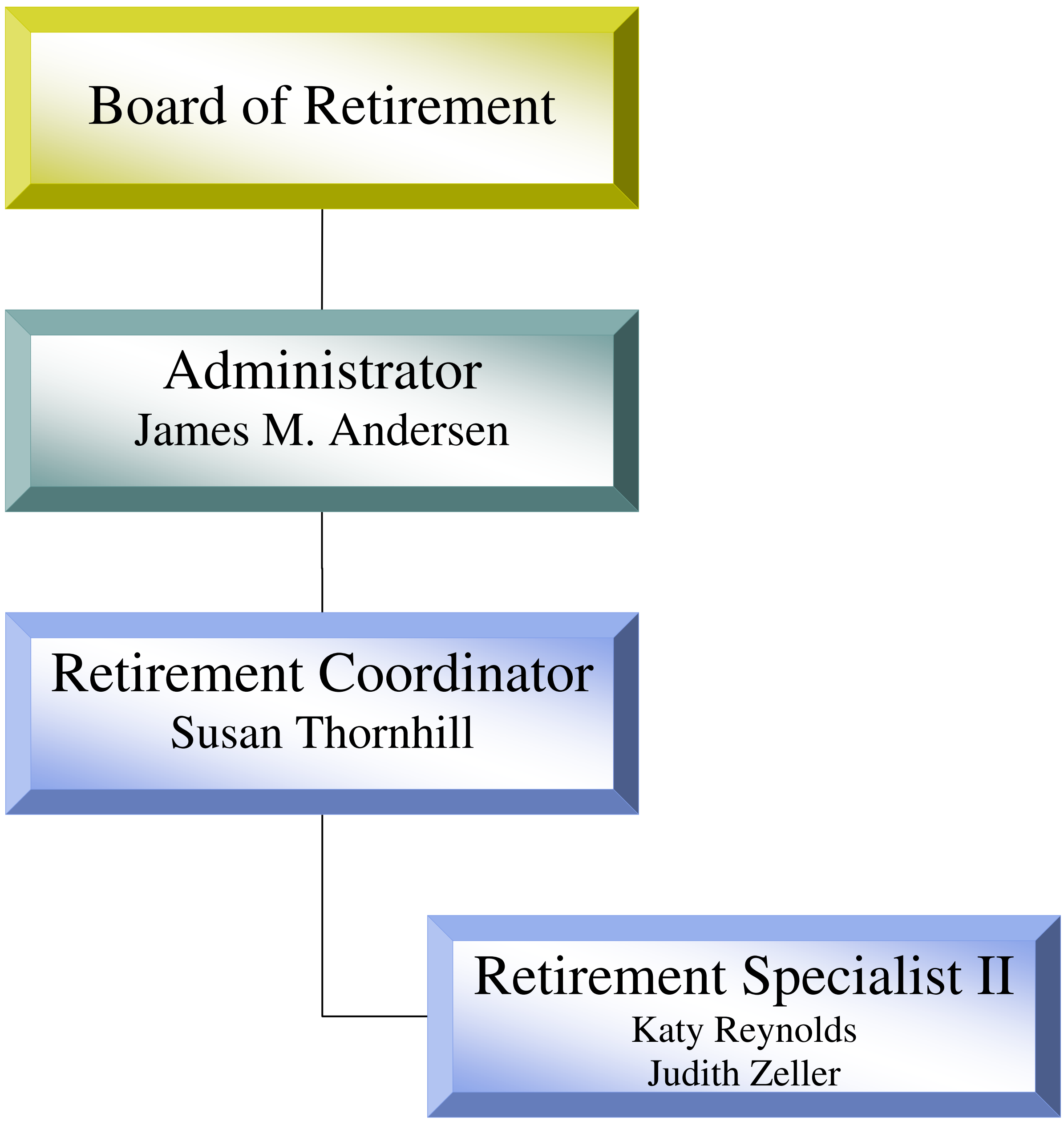
I commend the Board, staff and service providers of the Association for their commitment to MCERA and for their diligent work to assure the continued successful operation of MCERA.

Respectfully submitted,

James M. Andersen
Retirement Administrator

BOARD OF RETIREMENT
JUNE 30, 2010

MCERA ORGANIZATION CHART
AS OF JUNE 30, 2010



PROFESSIONAL CONSULTANTS

Consulting Services

Actuary
Buck Consultants

Auditor
V. James Sligh, MBA, CPA

Investment Custodian
The Bank of New York

Investment Consultant
Callan Associates

Legal Counsel
County Counsel, County of Mendocino
Law Office of Tony Graham

Technical and Data Service
Tyler Technologies
Munis Financial Management System

Investment Management Services

Fixed Income
Bradford, & Marzec
Dodge & Cox
PIMCO

Large Cap Value Equity
Selected American
Investment Co. of America
Vanguard Growth & Inc
Dodge & Cox Stock

Large Cap Growth Equity
American Growth
Harbor Capital Appreciation
Janus Research

Mid Cap Growth Equity
Morgan Stanley
Janus Enterprise

Mid Cap Value Equity
Fidelity Low Priced Stock
Royce Total Return

Small Cap Growth Equity
Alliance
R S Investments
Fremont U.S. Micro Cap

Small Cap Value Equity
Vanguard Small Cap Index

International Equity
Europacific
Harbor International
Acorn International
Artisan
Janus International
Oakmark

Real Estate
RREEF Commingled Fund
RREEF America REIT II

Financial Section

V. James Sligh
Certified Public Accountant

413 West Standley St., Suite A
Ukiah, CA 95482
Tel. & Fax (707) 462-8635
E-Mail slick@pacific.net

Board of Retirement
Mendocino County Employees' Retirement Association
Ukiah, California

INDEPENDENT AUDITOR'S REPORT

I have audited the accompanying statements of plan net assets of the Mendocino County Employees' Retirement Association (Association), component unit of the County of Mendocino, California, as of June 30, 2010 and 2009, and the related statements of changes in plan net assets for the years then ended, as listed in the table of contents. These financial statements are the responsibility of the Association's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit 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 I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. I believe that my audit provides a reasonable basis for my opinion.

In my opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of the Mendocino County Employees' Retirement Association as of June 30,2010 and 2009, and the changes in plan net assets for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, I have also issued my report dated January 25, 2011, on my consideration of the Association's internal control over financial reporting and on my tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of my testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of my audit.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 13 through 19, the Schedule of Funding Progress and the Schedule of Employer Contributions, as information in accordance with auditing standards generally accepted in the United States of America, which consisted principally of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to my inquiries, the basic financial statements, and other knowledge I obtained during my audit of the basic financial statements. I do not express an opinion or provide any assurance on the information because the limited procedures do not provide me with sufficient evidence to express an opinion or provide any assurance.

My audit was conducted for the purpose of forming an opinion on the basic financial statements. The introductory section, supplementary information section, investment section, and the actuarial section are presented for purposes of additional analysis and are not a required part of the basic financial statements. The supplementary information, as described in the table of contents as the Schedule of Administrative Expenses, and the Schedule of Investment Expenses, has been subjected to the auditing procedures applied in the audit of the basic financial statements for the years ended June 30, 2010 and 2009, taken as a whole. The introductory, investment, and actuarial sections have not been subjected to auditing procedures applied in the audit of the basic financial statements and, accordingly, I do not express an opinion or provide any assurance on them.

V. James Sligh

V. James Sligh, CPA
Ukiah, California
January 25, 2011

Management's Discussion and Analysis

The following section provides an overview and analysis of the Mendocino County Employees' Retirement Association (MCERA) financial activities for the years ended June 30, 2010 and 2009. We encourage readers to take into account the information presented here in conjunction with additional information we have furnished in the financial statements.

Financial Highlights

MCERA net assets as of June 30, 2010 and 2009 are $300 million and $272 million, respectively. This reflects an increase of 10.3% in net assets during Fiscal Year 2009-2010.

MCERA's funding objective is to meet the long-term benefit obligations through contributions and investment income. As of June 30, 2010, the date of our last actuarial valuation, the funding ratio was 78.94%, down from 83.4% at June 30, 2009. In general, this indicates that for every dollar of benefits owed we had approximately $.79 of assets available for payment as of that date. In June of 2010, the MCERA Board changed its interest posting and excess earnings policy to direct all future excess earnings toward unfunded accrued actuarial liability (UAAL), with the intent of improving the funded status of the plan.

Revenues (additions to plan assets) for the year were $52.9 million, compared to negative revenues (losses) of $35.5 million in 2009. The 2010 additions were comprised of $8.2 million of employer contributions, $6.5 million of member contributions and an investment return of $38.1 million.

Expenses (deductions in plan assets) for the year were $ 24.9 million, an increase of $2.1 million, or 9.2 %, over the prior year. The increase in expenses primarily came from pension benefits. After the conclusion of the 2009-10 fiscal year, the legislature passed Assembly Bill 609, which was signed into law by the Governor, providing for a more stable funding source for retirement system administrative expenses. AB 609 provided funding of 21/100ths of 1% of the accrued actuarial liabilities (AAL), or $2 million, whichever is greatest, for administrative expenses.

Overview of Financial Statements

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

- Statement of Plan Net Assets (page 20)
- Statement of Changes in Plan Net Assets (page 21)
- Notes to the Financial Statements (page 22)

The Statement of Plan Net Assets is a snapshot of account balances at year-end. It indicates the assets available for future payments to retirees and any current liabilities owed.

The Statement of Changes in Plan Net Assets provides a view of the current year additions to and deductions from the plan. This statement covers the activity over a one-year period of time.

Both statements are in compliance with Government Accounting Standards Board (GASB) Statements No. 25, 28, 33, 34, 37, and 38. These pronouncements require certain disclosures and require the state and local governments report using the full accrual method of accounting. MCERA complies with all material aspects of the pronouncements.

The Statement of Plan Net Assets and Statement of Changes in Plan Net Assets report information about MCERA activities. These statements include all assets and liabilities, using the full accrual basis of accounting which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when the cash is received or paid. All investment gains and losses are shown at trade date, not settlement date. In addition, both realized and unrealized gains and losses are shown on investments. All capital assets are depreciated over their useful lives.

Over time, increases and decreases in MCERA's net assets are one indicator of whether its financial health is improving or deteriorating. Other factors, such as recent market conditions, should also be considered in measuring MCERA's overall financial health.

Notes to the Financial Statements provide additional information that is essential to a full understanding of the data provided in the financial statements. Please note that this report also contains other supplemental information in addition to the basic financial statements themselves.

MCERA's Net Assets

For the Fiscal Years ended June 30, 2010 and 2009

(Dollars in Thousands)

	2010	**2009**	**Amount Increase/ (Decrease)**	**% Change Increase/ (Decrease)**
Cash and Short Term Investments	16,192	16,021	171	1.1%
Receivables	2,016	1,843	173	9.4%
Investments, at Fair Value	283,670	254,779	28,891	11.3%
Total Assets	301,878	272,643	29,235	10.7%
Accounts Payable	293	83	210	253.0%
Accrued Expenses	22	24	(2)	-8.3%
Investment Purchases	1,520	495	1,025	207.1%
Total Liabilities	1,835	602	1,233	204.8%
Net Assets Held in Trust for Benefits	300,043	272,041	28,002	10.3%

The Retirement Fund as a Whole

MCERA's net assets increased10.3 % in 2010 reflecting investment returns of 14.47 %. Investment returns can vary significantly from year to year. For example, investment returns for 2009 were (16.5%). MCERA maintains a diversified investment portfolio and asset allocation that is structured to meet the long term funding requirements of the plan. Five year investment returns, net of fees, are 3.99%. A long-term investment strategy incorporating structured diversification and a balanced investment portfolio are critical to meeting return targets over time. MCERA management and its actuary concur that MCERA remains in a financial position that will enable the plan to meet its obligations to participants and beneficiaries. MCERA and its investment consultants conducted a liability and asset allocation study in June of 2010, and the MCERA Board adopted new investment targets that the Board believes will result in MCERA coming closer to meeting its actuarial assumed rate of return (8%) while taking on little increased risk. The Board, upon advice of the investment consultants, strived to create a portfolio that takes advantage of the returns of stocks, especially international stocks. The portfolio provides a better balance of large capitalized investments with smaller capitalized investments, and value to growth investment philosophies.

The MCERA Board is also currently reviewing its fund managers, which have performed well during the market downturn and recovery. Fund managers contributed 2.82% above investment benchmarks for the one year period ending June 30, 2010. MCERA changed investment consultants in October of 2009, so managers' contributions to investment returns are not available for June 30, 2009.

Investment Analysis

As stated above, investment returns increased in 2010 with a 14.47 % return at the total portfolio level. During the period of 2008 through March of 2009, there was a decline in worldwide markets greater than any since the Great Depression. This market decline drove the five year annualized portfolio return down to 3.99%, net of fees. MCERA's asset allocation from June 30, 2009 to 2010 included 39% U.S. equities, 20% international equities, 31% fixed income and 10% real estate. As noted above, the MCERA Board conducted a study and amended its asset allocation slightly reducing investments in fixed income and real estate, and increasing its investments in international equities. MCERA's total portfolio returns were 14.47%, -2.76% and 3.33% for the one, three and five year periods ended June 30, 2010, respectively.

MCERA's Reserves

For the Fiscal Years ended June 30, 2010, 2009 and 2008

(Dollars in Thousands)

	2010	**2009**	**2008**
Member Reserve	63,975	64,102	62,348
Employer Reserve	(15,618)	(2,559)	3,459
Annuitant Reserve	167,440	155,083	150,148
Cost of Living Reserve	82,667	83,221	83,594
Retiree Health Insurance Reserve	2,449	6,345	9,994
Contingency Reserve	3,000	2,720	3,313
Miscellaneous Reserves	3	7	4
Total Reserves	303,916	308,919	312,860

Reserves

MCERA's reserves are established from contributions and the accumulation of investment income after satisfying investment and administrative expenses. Under GASB 25, investments are stated at fair value instead of cost and include the recognition of unrealized gains and losses in the current period. MCERA has adopted a five-year smoothing methodology for investment gains and losses. This has the effect of smoothing both positive and negative fluctuations in investment performance versus assumptions and has a stabilizing effect on contribution rates. In May of 2010, the MCERA Board directed its staff to conduct a procurement process for an actuarial audit. The audit tested both the accuracy of work conducted by our primary actuary and the assumptions used by the actuary. The results of the audit were received in February of 2011.

Additions to MCERA's Net Assets
For the Fiscal Years ended June 30, 2010 and 2009
(Dollars in Thousands)

	2010	**2009**	**Amount Increase/ (Decrease)**	**% Change Increase/ (Decrease)**
Employer Contributions	8,234	8,561	(327)	-3.8%
Member Contributions	6,502	6,836	(334)	-4.9%
Administrative Expense Reimbursement	4	322	(318)	-98.8%
Net Investment Income	38,128	(52,214)	90,342	-173.0%
Total Additions	52,868	(36,495)	89,363	-244.9%

Deductions to MCERA's Net Assets
For the Fiscal Years ended June 30, 2010 and 2009
(Dollars in Thousands)

	2010	**2009**	**Amount Increase/ (Decrease)**	**% Change Increase/ (Decrease)**
Retirement Benefits	19,272	16,620	2,652	16.0%
Health Benefits	3,889	4,860	(971)	-20.0%
Refund of Contributions	1,061	734	327	44.6%
Administrative Expenses	645	602	43	7.1%
Total Deductions	24,867	22,816	2,051	9.0%
Change in Net Assets	28,001	(59,311)	87,312	-147.2%

Revenues (Additions to Plan Assets)

The primary sources to finance the benefits MCERA provides to its members are accumulated through income on investments and through the collection of employee and employer contributions. These income sources for the fiscal year ended June 30, 2010 totaled $52.9 million, compared to a negative income (loss) of ($36.5) million for the fiscal year ending June 30, 2009. The increase in revenues from 2009 to 2010 can be attributed primarily to investment income. The increase in investment income is primarily a result of the emerging recovery from the world-wide market decline described above. The total balance of net assets increased from approximately $272 million in 2009 to $301 million in 2010.

Expenses (Deductions in Plan Assets)

The primary uses of MCERA assets are the payment of benefits to retirees and their beneficiaries, refunds of contributions to terminated employees, and the cost of administering the system. These expenses for the fiscal year ended June 30, 2010 were $644 thousand, an increase of $43 thousand compared to the year ended June 30, 2009. Pension benefits increased $1.6 million almost exclusively due to an increase in the number of retirees. As discussed above, AB 609 increased the amount of investment returns that could be used for administrative expenses. The MCERA Board will be reviewing staffing levels and information technology needs during the upcoming year.

Financial Change

Since June 30, 2010, the U.S. and International equity markets have experienced a significant recovery in market value. In this environment, the MCERA assets increased in value roughly $50 million, or 16.5%, to a value at March 31, 2011, of just under $354 million. The asset allocation of the portfolio was reviewed and adjusted in 2010. The Board, working with our investment consultants, Callan Associates, has reviewed all asset classes and replaced Bradford & Marzec and Dodge & Cox fixed income managers with the Dodge & Cox Income fund. The Board also replaced Artisan Funds with Mondrian All Countries World Ex-U.S. Equity fund as an investment in international equities, and has added Robeco and Prudential Investments to fulfill large cap and small cap value domestic equities, respectively, in the portfolio. Prudential will be replacing investments in Vanguard’s small cap domestic equity index fund. The only remaining manager selection, based upon its asset allocation review, is private real estate.

Also, during the downturn in the markets, MCERA chose not to rebalance its assets given the lack of distinguishable fundamentals governing the movement of investment values. Since the recovery of the markets, MCERA has rebalanced its asset classes to targets contained in its investment policy and will review the need to rebalance on a quarterly basis. Of further note is a change in the strategy for investment income. MCERA historically received investment income from its fixed income managers and fund (PIMCO) in the form of interest and principal pay-downs. The cash was used for operational needs of the Association, but was also accruing in a low yielding cash account rather than being immediately reinvested in higher yielding securities or fixed income vehicles. MCERA issued letters of instruction to its fixed income managers to reinvest
all income. MCERA now maintains approximately $3 million, or .8% of assets in cash. Cash flows will be determined and investments sold (and cash proceeds raised) on an as needed basis.

Fiduciary Responsibility

MCERA's Board and staff are fiduciaries of the pension fund. Under the California Constitution the assets can only be used for the benefit of plan participants and their beneficiaries.

Request for Information

The financial report is designed to provide the Retirement Board, our membership, tax-payers, investment managers and creditors with a general overview of MCERA finances and to account for the money it receives. Questions concerning any of the information in this report or requests for additional financial information should be addressed to:

MCERA
625 B Kings Court
Ukiah, CA 95482

Respectfully submitted,

James M. Andersen

James Andersen
Retirement Administrator

STATEMENT OF PLAN NET ASSETS AVAILABLE FOR BENEFITS

ASSETS	**6/30/2010**	**6/30/2009**
Cash and Cash Equivalents	16,191,776	16,021,408
Receivables		
Employers	46,281	62,607
Investment Sales	814,942	630,928
Interest and Dividends	1,002,293	1,145,550
Other Receivables	152,918	4,266
Total Receivables	2,016,434	1,843,351
Investments, at fair value		
U.S. Government Bonds	51,969,718	32,731,309
International Bonds	7,080,383	4,888,512
Domestic Corporate Bonds	44,148,272	62,002,452
Domestic Stocks	104,627,860	88,805,143
International Stocks	52,327,297	45,196,570
Real Estate	23,516,305	21,154,632
Total Investments	283,669,835	254,778,618
Total Assets	301,878,045	272,643,377
LIABILITIES		
Accounts Payable	293,357	83,391
Accrued Expenses	22,063	23,921
Investment Purchases	1,520,063	495,155
Total Liabilities	1,835,483	602,467
Net Assets Held in Trust for Pension Benefits	300,042,562	272,040,910

(A schedule of funding progress is included in the accompanying Required Supplementary Information)

The accompanying notes are an integral part of these financial statements

STATEMENT OF CHANGES IN PLAN NET ASSETS AVAILABLE FOR BENEFITS

ADDITIONS	**6/30/2010**	**6/30/2009**
Contributions		
Employer	8,234,253	8,561,368
Plan Members	6,502,080	6,836,202
Total Contributions	14,736,333	15,397,570
Other Income		
Employer Reimbursement of		
Administrative Expenses	4,057	321,910
Total Other Income	4,057	321,910
Investment Income		
Net Appreciation (Depreciation)		
In Fair Value of Investments	31,278,606	(61,420,271)
Building Income Net of Expenses	92,159	91,191
Interest	5,054,338	6,019,378
Dividends	2,298,834	3,531,770
Total Investment Income	38,723,937	(51,777,932)
Less Investment Expenses	595,494	436,606
Net Investment Income (Loss)	38,128,443	(52,214,538)
Total Additions	52,868,833	(36,495,058)
DEDUCTIONS		
Retirement Benefits	19,272,443	17,366,916
Refund of Contributions	1,061,327	734,403
Health Care Benefits	3,888,546	4,113,551
Administrative Expenses	644,865	601,879
Total Deductions	24,867,181	22,816,749
Net Increase (Decrease)	28,001,652	(59,311,807)
Net Assets Held in Trust		
for Pension Benefits		
Beginning of Year	272,040,910	331,352,717
End of Year	300,042,562	272,040,910

The accompanying notes are an integral part of these financial statements

NOTES TO THE FINANCIAL STATEMENTS

For the Years ended June 30, 2010 and 2009

DESCRIPTION OF PLAN

Description of the Association and Applicable Provisions of Law

The Mendocino County Employees' Retirement Association (Association) is an integrated public retirement system established under and subject to the legislative authority of the State of California as enacted and amended the County Retirement Act of 1937 (Chapter 677 Statutes of 1937). It is a multiple-employer "Cost-Sharing" defined benefit plan for the County of Mendocino, the Mendocino County Courts, and the Russian River Cemetery District. The Association was approved by the Board of Supervisors to become effective January 1, 1948, and was integrated with Social Security on January 1, 1956.

Membership in the plan at June 30 consisted of the following:

	2010	**2009**
Retirees and beneficiaries receiving benefits	1,084	1,009
Terminated plan members entitled to but not yet receiving benefits	391	309
Active plan members	1,274	1,391
Total	2,749	2,709
Number of participating employers	3	3

While the total members increased by only 40 from June 30, 2009 to 2010, retirees increased by 75 members.

A cost-sharing multiple employer plan is a single plan with pooling (cost-sharing) arrangements for the participating employers. All risks, rewards, and costs, including benefit costs, are shared and are not attributed individually to the employers. A single actuarial valuation covers all plan members. Other special districts within Mendocino County are eligible, but have not elected to participate.

All permanent employees who work at least 32 hours per week become members of the plan on the first day of the pay period following employment. Employees are classified as either general or safety (law enforcement) members, and are assigned to one of three tiers based on entry date and job classification.

Retirement benefits offered by the plan include normal retirement, disability retirement and service-connected disability retirement. A death benefit is available to beneficiaries. An annual cost of living adjustment of no more than 3 percent may be granted by the Board of Retirement.

For 2010, the Board of Retirement approved cost of living increases ranging from 2.5% to 3%, depending on date of retirement, and became effective April 1, 2010. This compares to an increase from 0% to 3% in 2009.

Health benefits for retired employees have been funded by the plan in the past. As of September 1, 1998, the County of Mendocino has assumed responsibility for funding the cost of health care for the retired employees of the County of Mendocino, and will be responsible for the cost of health care when Association earnings on investments are not in excess of required transfers of earnings to retirement reserve accounts. For eligibility for health care coverage, prior to September 1, 1998, retirees must have served ten years prior to retirement with the County of Mendocino, and retire as an active member. The retiree health benefit program qualifies under section 401(h) of the Internal Revenue Code. Health care payments to reimburse the County for the cost of retiree health care are made from a special reserve that has been established as a result of prior excess earnings. This health care subsidy amounted to $3,888,546 for the year ended June 30, 2010, and is included in the line item for benefit payments and subsidies on the Statement of Changes in Net Assets. This subsidy is net of all health care payments of retirees.

Beginning January 1, 2009 and ending December 31, 2009, all retirees under the age of 65 were required to pay $96.40 each month as a premium for health care paid by the Association, and $595.44 for each covered dependent of a retiree. Beginning January 1, 2010, and ending July 31, 2010, all retirees under age of 65 were required to pay $171.40 each month, retirees over 65 were required to pay $75 per month, and the dependent coverage increased to $605.02 per month. As of August 1, 2010, and ending December 31, 2010, retirees under age 65 were required to pay $531.2 per month, through the date of this report, with an increase for dependent coverage to $731.20 per month. In addition, as of August 1, 2010 the County subsidizes the cost of premiums for both Medicare-eligible and other retirees, which is offset by accrued excess earnings of the Association. The subsidy for premiums is $100 for retirees 65 and over beginning August 1, 2010, and those retirees are referred to Extend Health to purchase supplemental coverage. Retirees under 65 are given a supplement of $200 per month beginning August 1, 2010 and ending December 31, 2010. The subsidy for each retiree in the under-65 group is $288 per month beginning January 1, 2011. The premium for each dependent increased to $819.20 per month beginning January 1, 2011. The reserve is adjusted to actual medical costs at the end of each fiscal year.

As of the date of this report, the balance in the health care reserve was approximately $658,000. The health reserve, funded by excess earnings calculated as a result of actuarial valuations in prior years, will no longer be funded by excess earnings, as of June 16, 2010, until the accrued actuarial liability of the system is funded at 100 percent. In addition, excess earnings will be calculated using generally accepted accounting principles, not actuarial valuations.

Summary of Significant Accounting Policies

Reporting Entity

The Association is governed by the Board of Retirement and is considered an independent entity. The Association is a component unit of the County of Mendocino and is being reported as a Pension Trust Fund in the County's Financial Report in accordance with Governmental Accounting Standards Board Statement No. 14.

Basis of Accounting

The Association follows Governmental Accounting Standards Board (GASB) accounting principles and reporting guidelines, and financial statements are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions to the plan are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

Cash and 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. Mortgage securities are valued on the basis of future principal and interest payments, and are discounted at prevailing interest rates for similar instruments. Investments that do not have an established market are reported at estimated fair value. All investments listed in the Statement of Plan Net Assets are registered securities held by the Association's agent in the Association's name. The Board of Retirement has exclusive control over all investments of the Association and is responsible for establishing investment objectives, strategies and policies.

The Board of Retirement has adopted an Investment Policy, which provides the framework for the management of the Association's investments. The Investment policy establishes the Association's investment objectives and defines the principal duties of the Board of Retirement and the investment managers. The asset allocation plan is an integral part of the Investment Policy and is designed to provide an optimum and diversified mix of asset classes with return expectations to satisfy expected liabilities while minimizing risk exposure. The Association currently employs investment managers to manage its assets subject to the provisions of the Investment Policy.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash in trust with the Treasurer of the County of Mendocino and cash held for investment by bond investment managers. Cash from deposits and cash needed for daily operational purposes is held in a pooled account with other County funds. The County Treasurer is responsible for the management, control, and safekeeping of all investments in the pooled fund. Interest on funds in the County investment pool is computed quarterly based on average daily balance. A deposit in the pooled account approximates fair value. Cash and cash equivalents are highly liquid investments with a short maturity and are recorded at cost, which approximates fair value.

Security transactions are accounted for on a trade date basis. Interest income is recognized when earned and dividend income is recognized on the ex-dividend date. Stock dividends or stock splits are recorded as memo items and do not affect the total value of the securities. Unrealized gains and losses on investments are reported as “net appreciation (depreciation) in the fair value of investments.” The calculation of realized gains and losses is independent of the calculation of net appreciation (depreciation) in the fair value of plan investments. The Association’s cash and investments stated at fair value as of June 30 are as follows:

	2010	**2009**
Cash in Trust - Mendocino County	15,115,875	16,021,391
Cash in Trust - Bond Managers	1,075,884	
Short-Term Investments - LAIF	17	17
Total Cash Equivalents	16,191,776	16,021,408
U.S. Government and Agency Bonds	51,969,718	32,731,309
International Bonds	7,080,383	4,888,512
Corporate Bonds	44,148,272	62,002,452
Domestic Stocks - Mutual Funds	101,646,920	86,352,155
Domestic Stocks	2,980,940	2,452,988
International Stocks - Mutual Funds	52,327,297	45,196,570
Real Estate	23,516,305	21,154,632
Total Investments	283,669,835	254,778,618
Total Cash Equivalents and Investments	299,861,611	270,800,026

In accordance with GASB Statement No. 40 disclosure requirements, cash invested in external investment pools and in open-end mutual funds are not exposed to custodial credit risk because their existence is not evidenced by securities that exist in physical or book entry form.

In addition, at June 30, 2010, there are short-term investments of $954,120 at the Bank of New York, and $115,668 at Pimco Fund (a bond mutual fund) that are reported in the financial statements as interest, dividends, and investment sales receivable because these amounts represent current period earnings and securities sales that are to be immediately transferred to the Association. At June 30, 2010 the Association was owed $814,942 by investment managers for sales of securities. These dollar amounts are consistent with those of June 30, 2009, when $630,928 was owed by investment managers.

Custodial Credit Risk

Custodial credit risk for deposits is the risk that in the event of a failure in a depository financial institution, a government will not be able to recover its deposits or recover collateral securities that are in the possession of an outside party.

Custodial risk for deposits in the Mendocino County trust is assumed by the County of Mendocino. Short-term investments with the Bank of New York are not insured and are subject to risk of loss through market fluctuations, but risk of loss for fraudulent acts and lack of fidelity on the part of investment managers is covered by fidelity bonds for the Bank of New York investments. All the above short-term investments are stated at fair value.
In accordance with GASB Statement No. 40 disclosure requirements, cash invested in external investment pools and in open-end mutual funds are not exposed to custodial credit risk because their existence is not evidenced by securities that exist in physical or book entry form.

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty, the government will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. Except for a statement that duties of the Board of Retirement, Association officers and employees shall be discharged with care, skill, prudence, and diligence, the Association has no formal policy for managing custodial credit risk.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to a debt instrument will not fulfill its obligations. This risk is measured by the assignment of ratings by nationally recognized statistical rating organizations. Investment allocation guidelines according to the investment policy are as follows:

	Minimum	Maximum	Target
Fixed Income	23%	33%	28%
United States Stocks	33%	43%	38%
International Stocks	20%	30%	25%
Real Estate	4%	14%	9%

The Association's Investment Policy does not allow for a single investment in real estate that is in excess of 5% of total assets. No single common stock investment, based on cost, shall exceed 2% of the assets of the Association, and may not exceed 5% of the shares outstanding. With respect to common stocks, the Association has a goal of diversifying the portfolio among a cross-section of industries that have sound long-term growth potential. Similar restrictions apply to fixed income securities. Single security restrictions do not apply to investments in mutual funds. For fixed income investments, corporate debt issues must be rated "A" or better by the Standard and Poor corporation (S&P).

An exception to this policy is that one particular fixed income investment manager is authorized to purchase corporate debt issues with a "BBB" rating by S&P to the extent of 25% of the total portfolio if the weighted average rating of the portfolio remains at "AA". Other fixed income securities allowed by the Association are instruments issued by agencies of, or guaranteed by, the U.S. Government; United States Treasury Bonds, Notes and Bills; certificates of deposit and Bankers Acceptances; Commercial paper of the highest quality. No more than 20% of the portfolio managed by one particular investment manager shall be invested in non-U. S. dollar bonds.

As of June 30, 2010, the Association's quality distribution of fixed income investments was as follows:

Quality (S&P)	Percentage of Total Fixed Income Securities
U.S. Treasury	4.7%
Government Agency	32.5%
AAA	16.2%
AA	3.5%
A	16.1%
BAA	19.4%
BA	3.7%
Other	3.9%
	100.0%

The quality distribution of fixed income was comparable at June 30, 2009, with a slightly higher percentage (21.5%) invested in A securities.

The above analysis of quality distribution of fixed assets does not include fixed income investments in Pimco Funds. No specific quality or duration data is available from Pimco. Duration does not appear relevant for Pimco Funds because it is a mutual fund and the Association does not own specific fixed income investments in the fund, and shares in the mutual fund owned by the Association have no maturity. The total fair market value of Pimco shares owned by the Association at June 30, 2010 is $45,164,284, compared to $41,492,191 at June 30, 2009. Interest income of $1,752,672 attributable to Pimco Funds for the Year ended June 30, 2010, includes an undetermined amount of short term capital gains because all earnings of the fund are lumped together and labeled "Dividends & Short-Term Capital Gains" because it is a mutual fund.

Interest Rate Risk

Interest rate risk is the risk that changes in the interest rate will adversely affect the fair value of an investment. The Association has not adopted a formal policy to manage interest rate risk.

As of June 30, 2010, the Association had the following fixed income investments:

Investment Type	Fair Value	Weight of Total Fixed Income	Effective Duration (In Years)
U.S. Treasuries	2,701,252	4.7%	2.3
Government Agencies	4,307,582	7.4%	4.7
Asset-Backed Securities	177,219	0.3%	0.2
Corporate Bonds	26,635,050	45.9%	5.7
Mortgages	23,003,960	39.6%	2.5
International	1,209,026	2.1%	4.6
Bond Mutual Fund (PIMCO)	45,164,284	NA	NA
Total Fair Value	103,198,373	100.0%	
Portfolio Effective Duration*			4.25

*Directly Owned Securities as of June 30, 2010

Portfolio Effective Duration of fixed income securities owned directly by the Association was 4.25 as of June 30, 2010, the same as in 2009. The weighting of Corporate Bonds and Mortgages increased from 2009 to 2010, while low yielding Government Agencies decreased.

Highly Sensitive Investments

As of June 30, 2010, there were no known investments that were sensitive to interest rate fluctuations.

Derivatives

The Association's investment policy permits the use of derivative instruments to minimize the exposure of certain of its investments to adverse fluctuations in financial and currency markets and enhance yields. The Association does not use derivatives for speculative use or to create leverage.

During the year ended June 30, 2010 The Association had no derivatives in its portfolio.

Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The following tables represent securities held in a foreign currency (in U.S. dollars) as of June 30, 2010:

Local Currency Name	Cash	Equity	Fixed Income	Total
Australian Dollars	1,280	0	500,841	502,121
Canadian Dollars	0	0	160,160	160,160
United Kingdom Gilts	0	0	165,733	165,733
New Zealand Dollars	0	0	382,292	382,292
Total	1,280	0	1,209,026	1,210,306

The following tables represent securities held in a foreign currency (in U.S. dollars) as of June 30, 2009:

Local Currency Name	Cash	Equity	Fixed Income	Total
Australian Dollars	1,001	0	152,728	153,729
Germany - Euros	0	0	664,385	664,385
New Zealand Dollars	0	0	337,102	337,102
Total	1,001	0	1,154,215	1,155,216

Investments in Australian cash and fixed income increased from $153,729 in 2009. In addition, $664,385 in Germany (Euros) were sold between June 30, 2009 and 2010.

Foreign currency is comprised of international investment proceeds and income to be repatriated into U.S. dollars and funds available to purchase international securities. Foreign currency is not held as a form of investment, but held temporarily in foreign accounts until it is repatriated or expended.

The investments of the Association are governed primarily by an investment authority known as "The prudent person rule." The prudent person rule, as set forth in Section 31595 of the California Government Code, establishes a standard for all fiduciaries, which includes anyone that has authority with respect to the Association.

Use of Estimates

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

Contributions

Actuarially determined member contribution rates averaged 9.85 percent for the year ended June 30, 2010. The actual rate depends on the member's age at the time of hire, whether regular or safety, and tier. Employers are also required to contribute an actuarially determined rate, averaging 10.35 percent of salary for the year ended June 30, 2010, the same percentage of payroll as in the year ended June 30, 2009. The employers' rate is adjusted periodically to maintain the appropriate funding status of the plan.

The recommended rates for employees and employers for the year ended June 30, 2011 are 9.84 and 13.25 percent, respectively. The employer rates are actuarially determined to provide for the balance of the contributions needed to fund the benefits promised (basic and cost of living), and the amortization of the unfunded actuarial accrued liability.

The plan had an unfunded actuarially accrued liability of $47,154,000 at June 30, 2001. This unfunded liability was being amortized through June 30, 2017, at which time it was anticipated the plan would be fully funded. In December, 1996, the County of Mendocino issued pension obligation bonds, of which $30,112,488 of the proceeds were contributed to the plan. In December, 2002, due to a continued downward spiral of market values for Association investments, the County of Mendocino issued additional pension obligation bonds. The total of bonds sold was $92,208,602, of which $76,299,000 was transferred to the Association for additional investment, $13,220,061 was used to defease fifty percent of the 1996 pension obligation bonds, and the remainder of $2,689,541 was used to pay the costs of issuing the bonds. The proceeds from the 2002 pension obligation bonds reduced the unfunded pension liability to less than 10 percent of the actuarially accrued liability at June 30, 2004. The funding agreement in effect prior to July 1, 2009 indicated that the County was not required to fund the unfunded actuarially accrued liability (UAAL) that was not in excess of the target of 10 percent of the total pension liability. In November, 2009 that funding agreement was voided by mutual agreement between the Association Board of Retirement and the Mendocino County Board of Supervisors. Subsequent to the funding agreement, the Board of Retirement stipulated that the County of Mendocino must amortize the UAAL over a 30-year period from June, 2009.

For the actuarial valuation for the year ended June 30, 2010, the actuary changed their assumptions regarding withdrawals by inactive members. This change in assumption affected the projected number of inactive members who would withdraw their contributions and forego a retirement, compared to those who would leave their contributions and vested benefits with the Association and retire at a later date. The actuary formerly used each inactive member's age when determining who would withdraw their funds; now the actuary uses age and years of service for all inactive members. The result was an increase of $3.3 million in the County's contribution for the fiscal year ended June 30, 2012.

The UAAL as of June 30, 2010 is $91.8 million, up from $66.9 million in 2009, which the County of Mendocino is required to amortize in the future. The funded ratio at June 30, 2010 is 78.9%, as indicated on the Schedule of Funding Progress on Page 36 of this report. The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated.

Additional information as of the latest actuarial valuation follows:

Valuation date	June 30, 2010
Actuarial cost method	Entry Age Normal
Asset valuation method	Smoothed Market Value
Actuarial assumptions:	
Investment rate of return*	8%
Interest credited to employees	8%
Projected salary increases*	Standard salary scale
*Includes inflation at 4%	
Spouses and Dependents	90% of male employees and 50% of female employees assumed married at retirement, with wives assumed three years younger than husbands.
Rates of employment termination	Standard tables
Years of life expectancy after retirement	Standard tables
Years of life expectancy after disability	Standard tables
Life expectancy after retirement For employee contribution rate purposes	General members - 1994 Group Annuity Table for Males, setback 3 years. Safety members - 1994 Group Annuity Table for Males, with no setback.
Reciprocity assumption	50% of members who terminate with a vested benefit are assumed to enter a reciprocal system.
Deferral Age for vested terminations	62 for general members, 55 for safety.
Sex	All safety members are assumed to be male.

Reserves

The Association had contingency reserves of $3,000,426, at June 30, 2010, up roughly $280,000 from 2009 due to the increased asset value against which the 1% reserve requirement is calculated. The contingency reserves are used to fund transfers to retirement reserve accounts in the event that sufficient earnings on investments are not received in the future to fulfill the requirement of transferring current earnings, up to 8 %, to those reserves.

Member and employer contributions are allocated to various legally required reserve accounts based on actuarial determinations. A summary of the various reserve accounts, which comprise net assets available for pension and other benefits at June 30 (under the five-year smoothed market asset valuation method for actuarial valuation purposes) is as follows:

		2010	**2009**
Employee reserves	$	63,974,619	64,102,442
Employer reserves		(15,617,693)	(2,559,708)
Retiree reserves		250,107,010	238,303,919
Retiree health care benefit reserves		2,448,788	6,345,030
1% Contingency reserve		3,000,426	2,720,409
Miscellaneous reserves		3,704	7,335
Total reserves		303,916,854	308,919,427
Excess earnings undesignated		42,288,744	30,066,179
Total allocated reserves (smoothed market actuarial value)		346,205,598	338,985,606
Net assets in excess (deficit) of reserves		(46,163,036)	(66,944,696)
Net assets available for benefits, at fair value	$	300,042,562	272,040,910

Note: For 2009 Total Reserves $300 less than audit due to footing error.

The reserve for health care benefits of retirees was derived from excess earnings of the Association in prior years.

Risk Management

The Association is exposed to various risks of losses related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; natural disasters; and major downturns in financial markets. For the past several years, the Association has obtained coverage from commercial insurance companies for errors and omissions coverage related to activities of the Board of Retirement, but all other risks of loss, except losses due to depreciation in the fair market value of investments, is assumed by the sponsoring employers. The Association has effectively managed risk through various employee education and prevention programs and careful selection of investments. Expenditures and claims are recognized when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated.

The Mendocino County Department of Human Resources has assumed the duties of administering the health care claims of retirees. The Association no longer pays a flat amount per covered retiree, with the exception of offsetting the County subsidies mentioned above. During the fiscal year ended June 30, 2010 the Association reimbursed the County for claims to health care providers after the health care services were performed and billed. Beginning in the fiscal year ended June 30, 2011 the Association is coming into full compliance with Internal Revenue Code Section 401(h) for any flow of funding.

Based on Mendocino County Board of Supervisors Resolution No. 98-147, County Counsel concluded that the County Board of Supervisors was ultimately responsible for the funding, administration and decision-making dealing with all aspects of the Plan. As a result, no Incurred But Not Reported (IBNR) claims were included as liabilities on the financial statements for the year ended June 30, 2010. For the year ended June 30, 2010, the Association had no excess earnings that can be used for the payment of retiree health benefits.

Member Termination

Upon separation from the Association, members' accumulated contributions are refundable with interest accrued through the prior June 30 or December 31. Interest on member accounts is credited semiannually on June 30 and December 31. Withdrawal of such accumulated contributions results in forfeiture of the related vested benefits.

Plan Termination

The Association is administered in accordance with the provisions of California Government Code Section 31450 and accompanying code sections. California Government Code Section 31483 allows the governing body of the County, the County Courts, or special district, through the adoption of an ordinance or resolution, to terminate the applicability of the plan to employees of the County, Courts, or district whose services commence after a given future date.

Current and Future Accounting Pronouncements

GASB Statement No. 53 - Accounting and Reporting for Derivative instruments became effective for all years beginning after June 15, 2009. This statement provides a comprehensive framework for the measurement, recognition, and disclosure of derivative instrument transactions. If the Association invests in derivative instruments in the future, this statement will be used to measure, recognize, and disclose those transactions.

GASB Statement No. 61 - The Financial Reporting Entity: Omnibus - an amendment of GASB Statements No. 14 and No. 34 modifies certain requirements for inclusion of component units in the financial reporting entity, and amends the criteria for reporting component units as if they were part of the primary government. Although the provisions for this statement are effective for fiscal years beginning after June 15, 2012, it seems to clarify and confirm the existing relationship of the Association as a component unit of the County of Mendocino.

GASB Statement No. 62 - Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements. This Statement, effective for periods beginning after December 15, 2011, will improve financial reporting by contributing to the GASB's efforts to codify all sources of generally accepted accounting principles for state and local governments so that they derive from a single source.

Subsequent Events

Subsequent events are those events or transactions that occur subsequent to the effective date of the financial statements, but prior to the issuance of final reports, which may have a material effect on the financial statements or disclosures therein.

On July 21, 2010 the Board of Retirement approved the writeoff of the $9,557,912 balance of an account labeled "Actuarial Value of Unrecorded Earnings". The posting of this transaction in a prior year was the result of recording an increase in the Retiree Health Care Benefit Reserve based on actuarial values of assets. Because actuarial values are no longer used as a basis for determining excess earnings, the Association considered this writeoff an important step to acknowledge that significant change in policy.

In late October, 2010 the Association directed the investment managers of separate fixed income accounts to liquidate, or transfer in-kind, all securities. The proceeds or in-kind transfers were placed in the Dodge & Cox Income Fund. As of January 25, 2011 there were no separately managed accounts in the Association portfolio, except for one corporate bond that is being held by the Bank of New York until a proper valuation can be established for disposition. The status of the portfolio will remain the same unless the Board of Retirement takes action to make investments in separately managed accounts.

Subsequent events have been reviewed through the date of this report, January 25, 2011.

EVENT (UNAUDITED) SUBSEQUENT TO THE DATE OF THE INDEPENDENT AUDITOR'S REPORT

During the review of the audited financial statements by the Board of Retirement on February 16, 2011, it was noted that there were questions regarding differences between the audited financial statements, the Management's Discussion and Analysis, and the Report on the Actuarial Valuation as of June 30, 2010. The Board of Retirement has requested these differences be addressed in the notes to the audited financial statements, as follows:

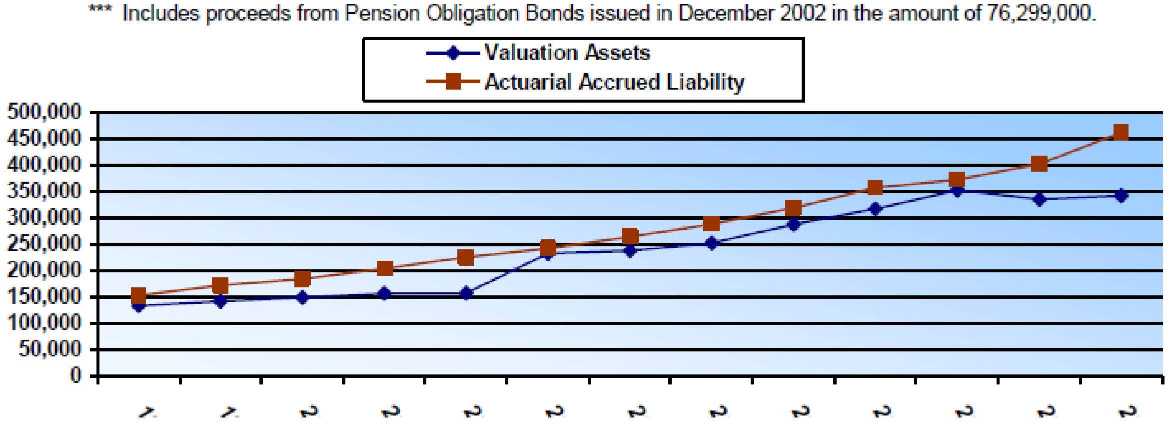
1) On page 16 of the Report on Actuarial Valuation, the actuary has indicated a rate of return of 17% for the year ended June 30, 2010, whereas management has indicated a rate of return of 14.47% that was calculated by the investment advisor, Callan Associates, in the Management's Discussion and Analysis on page 6 of the financial report. Management believes the primary difference is due to the actuary's unaudited overstatement of income (see #2).

2) On page 24 of the Report on the Actuarial Valuation, the Actuary indicated total investment income of $44,658,046, whereas the audited financial statements on page 10 of the financial report indicated investment income of $38,128,443. In addition, the actuary indicated $299,741,053 as the actual market value of assets at June 30, 2010 on page 24 of the Report on Actuarial Valuation, whereas page 10 of the audited financial statements indicate net assets were $300,042,562. Management believes the primary reason for the difference in investment income is the inclusion of internal transfers to the insurance claims fund as investment income. Management believes the primary reason for the difference in market value of assets is the actuary's use of unaudited and unadjusted financial data.

SCHEDULE OF FUNDING PROGRESS
GASB 25
(dollar amounts in thousands)

Actuarial Valuation Date	Valuation Assets	Actuarial Accrued Liability (AAL)	Unfunded AAL (UAAL)	Funded Ratio	Covered Payroll	UAAL as a Percent of Covered Payroll
7/1/93*	$ 72,062	$ 105,866	$ 33,804	68.1%	$ 25,930	130.4%
7/1/94	$ 75,976	$ 112,535	$ 36,559	67.5%	$ 27,185	134.5%
7/1/95	$ 79,322	$ 121,027	$ 41,705	65.5%	$ 29,603	140.9%
7/1/96	$ 84,992	$ 130,036	$ 45,044	65.4%	$ 29,587	152.2%
7/1/97	$ 124,286	$ 140,783	$ 16,497	88.3%	$ 32,481	50.8%
7/1/98	$ 134,836	$ 154,263	$ 19,427	87.4%	$ 35,586	54.6%
7/1/99	$ 142,775	$ 173,250	$ 30,475	82.4%	$ 39,209	77.7%
7/1/00	$ 150,056	$ 185,423	$ 35,367	80.9%	$ 44,132	80.1%
7/1/01	$ 157,545	$ 204,699	$ 47,154	77.0%	$ 53,188	88.7%
7/1/02	$ 158,115**	$ 226,883	$ 68,768	69.7%	$ 57,701	119.2%
7/1/03	$ 233,764***	$ 243,342	$ 9,578	96.1%	$ 59,865	16.0%
7/1/04	$ 239,191	$ 265,141	$ 25,950	90.2%	$ 59,075	43.9%
7/1/05	$ 253,487	$ 289,467	$ 35,980	87.6%	$ 57,664	62.4%
7/1/06	$ 288,461	$ 320,123	$ 31,662	90.1%	$ 57,665	54.9%
7/1/07	$ 317,937	$ 358,259	$ 40,322	88.7%	$ 65,899	61.2%
7/1/08	$ 353,421	$ 373,832	$ 20,411	94.5%	$ 70,880	28.8%
7/1/09	$ 336,263	$ 403,196	$ 66,933	83.4%	$ 72,235	92.7%
7/1/10	$ 343,202	$ 434,987	$ 91,785	78.9%	$ 69,004	133.0%

* Prepared by the prior actuary and unaudited by Buck Consultants.
** Excludes proceeds from Pension Obligation Bonds issued in December 2002.
*** Includes proceeds from Pension Obligation Bonds issued in December 2002 in the amount of 76,299,000.



Schedule of Employer Contributions
GASB 25
(dollar amounts in thousands)

Year Ended	Annual Recommended Contribution	Percentage Contributed
12/31/92	$ 2,939	100%
12/31/93	$ 2,939	100%
6/30/95*	$ 5,182	100%
6/30/96	$ 4,348	100%
6/30/97	$33,691**	100%
6/30/98	$ 2,661	100%
6/30/99	$ 3,165	100%
6/30/00	$ 3,787	100%
6/30/01	$ 7,216	100%
6/30/02	$ 6,348	100%
6/30/03	$ 6,663	100%
6/30/04	$ 4,158	63%
6/30/05	$ 3,221	47%
6/30/06	$ 4,996	79%
6/30/07	$ 7,533	100%
6/30/08	$ 7,232	100%
6/30/09	$ 6,046	141%
6/30/10	$ 9,571	91%

* Reflects 18 months of contributions due to a change in the financial reporting year.

** Includes proceeds from Pension Obligation Bonds.

SCHEDULE OF ADMINISTRATIVE EXPENSES
For the Years ended June 30, 2010

	2010	2009
Personal Services:		
Salaries and Wages	322,220	285,096
Other Benefits	65,680	44,737
Salaries, Wages & Benefits Charged to Investments	(92,453)	0
Employee Retirement	50,771	44,857
Total Personal Services	346,218	374,690
Professional Services:		
Outside Legal Counsel – Disability	72,904	43,932
Disability Hearing Officer/Medical Exams	75,588	58,900
External Audit Fees	11,860	9,700
Total Professional Services	160,352	112,532
Miscellaneous:		
Office Expenses *	78,229	83,178
New Building Equipment	0	1,627
Insurance General	1,266	1,266
Memberships	4,250	4,250
Prof & Spec Services – Other	36,338	7,900
Transportation & Travel	18,212	16,436
Total Miscellaneous	138,295	114,657
Total Administrative Expenses	644,865	601,879

* Includes Imputed Rent and 1/2 of Building Expenses.

SCHEDULE OF INVESTMENT MANAGEMENT FEES AND OTHER INVESTMENT EXPENSES
For the Year ended June 30, 2010

	2010	2009
Investment Management Fees:		
Bradford & Marzec	46,200	44,963
Dodge & Cox	92,128	136,679
Alliance Bernstein	25,269	23,704
Less Commission Recapture	(6,538)	(6,840)
Total Investment Management Fees	157,059	198,506
Investment Consultant Fees	163,500	64,000
Investment Custodian Fees	52,788	48,797
Fiduciary Insurance	30,815	36,400
Actuary Fees	98,879	87,841
Other Investment Expense	92,453	1,062
Total Investment Expenses	595,494	436,606

Investment Section

INVESTMENT SUMMARY
FOR THE YEAR ENDED JUNE 30, 2010

	Market Value	% of Assets	Current Yr Return	3 Year Return	5 Year Return
Domestic Equities	**104,627,860**	**36.88%**	**17.82%**	**-8.13%**	**0.48%**
Russell 3000 Index			15.72%	-9.47%	-0.48%
Large Cap Equities	**56,332,467**	**19.86%**			
Selected American	9,585,265	3.38%	15.68%	-10.24%	-0.64%
Dodge & Cox Stock	5,758,440	2.03%	15.34%	-13.82%	-2.45%
Investment Co of America	9,633,528	3.40%	10.20%	-9.18%	0.11%
Vanguard Growth & Income	8,867,385	3.13%	14.23%	-11.37%	-2.24%
S&P 500 Index			14.43%	-9.81%	-0.79%
Russell 1000 Value Index			16.92%	-12.32%	-1.64%
Growth Fund of America	6,730,586	2.37%	10.76%	-8.22%	1.13%
Harbor Cap Appreciation	8,320,170	2.93%	10.63%	-5.15%	0.80%
Janus Research	7,437,093	2.62%	17.15%	-6.61%	2.28%
S&P 500 Index			14.43%	-9.81%	-0.79%
Russell 1000 Growth Index			13.62%	-6.91%	0.38%
Mid Cap Equities	**29,351,936**	**10.35%**			
Fidelity Low Priced Stock	7,384,148	2.60%	21.12%	-6.44%	2.28%
Royce Total Return	7,315,773	2.58%	21.12%	-6.79%	1.50%
Russell 2000 Index			21.48%	-8.60%	0.37%
Russell MidCap Value Index			28.91%	-9.44%	0.71%
Morgan Stanley	7,568,653	2.67%	29.79%	-2.19%	-
Janus Enterprise	7,083,362	2.50%	20.81%	-	-
Russell MidCap Growth Index			21.30%	-7.53%	1.37%
Small Cap Equities	**18,943,457**	**6.68%**			
Vanguard Small Cap Value	11,011,023	3.88%	27.50%	-7.97%	-
US Small Cap Value Index			27.44%	-8.10%	0.32%
Russell 2000 Value Index			25.07%	-9.85%	-0.51%
Alliance US Small Growth	2,980,940	**1.05%**	21.52%	-6.73%	2.51%
RS Investments	2,457,293	0.87%	24.09%	-7.26%	0.81%
Managers Inst Micro Cap	2,494,201	0.88%	14.63%	-7.52%	0.10%
Russell 2000 Growth Index			17.96%	-7.54%	1.14%
International Equities	**52,327,297**	**18.45%**	**15.78%**	**-7.50%**	**6.37%**
EuroPacific	8,647,530	3.05%	9.86%	-7.63%	5.30%
Harbor International	8,124,842	2.86%	13.64%	-9.09%	-
Columbia Acorn Int'l	8,843,640	3.12%	18.91%	-7.21%	7.82%
Artisan International	7,633,586	2.69%	8.01%	-11.73%	-
Janus Overseas	9,466,892	3.34%	21.41%	-3.23%	-
Oakmark International	9,610,807	3.39%	22.06%	-7.21%	-
MSCI EAFE Index			5.92%	-13.38%	0.88%
MSCI ACWI ex-US Index			10.87%	-10.28%	3.84%

INVESTMENT SUMMARY - Continued

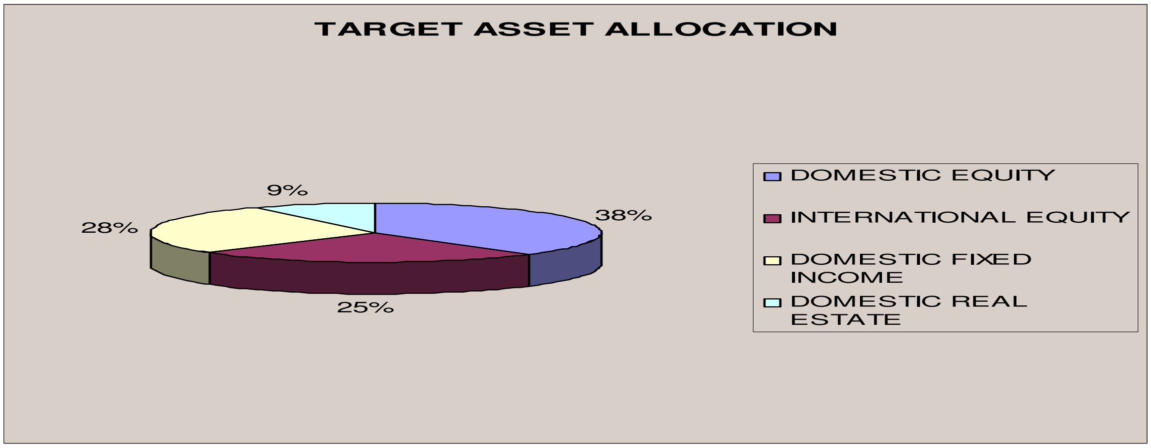
Domestic Fixed Income	**103,198,373**	**36.38%**	**11.78%**	**8.29%**	**6.28%**
Bradford & Marzec	16,890,232	5.95%	12.36%	9.20%	6.62%
Dodge & Cox	41,143,857	14.50%	13.88%	8.87%	6.77%
PIMCO	45,164,284	15.92%	13.31%	-	-
BC Aggregate Index			9.50%	7.55%	5.54%
Real Estate	**23,516,305**	**8.29%**	**12.17%**	**-12.05%**	**-1.19%**
RREEF Public Fund	9,882,144	3.48%	52.00%	-10.02%	0.22%
NAREIT			50.98%	-9.59%	-0.98%
RREEF Private Fund	12,895,169	4.55%	-5.87%	-13.33%	-2.83%
NFI-ODCE Equal Weight Net			-8.48%	-12.26%	-1.51%
625 Kings Court	738,992	0.26%	2.17%	0.72%	0.43%
Total Fund	**283,669,835**	**100.00%**	**14.47%**	**-2.76%**	**3.99%**
Total Fund Benchmark			12.74%	-4.47%	2.27%

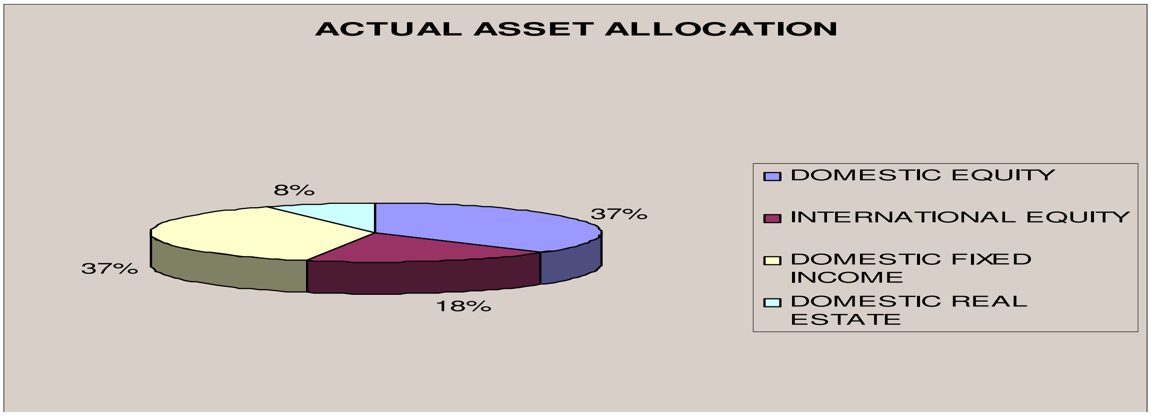
Market Values and percent of assets are from the June 30, 2010 audited financial statements and working papers. The 1, 3 & 5 year returns are from the Callan Associates June 30, 2010 performance report.

ASSET ALLOCATION
JUNE 30, 2010 (1)

Asset Class	Market Value	Actual Allocation	Target Allocation
Fixed Income	103,198,373	36.38%	28.00%
Domestic Equities	104,627,860	36.88%	38.00%
International Equities	52,327,297	18.45%	25.00%
Real Estate	23,516,305	8.29%	9.00%
Total Portfolio	283,669,835	100.00%	

Notes:
(1) Does not include cash; accounts receivables, or prepaid expenses





Actuarial Section

IN MARCH OF 2011, MCERA ENDED ITS CONTRACT WITH BUCK CONSULTANTS AND ENTERED INTO AN AGREEMENT WITH THE SEGAL COMPANY TO PROVIDE PRIMARY ACTUARIAL SERVICES. THIS SECTION OF THE CAFR WILL BE COMPLETED BY THE SEGAL COMPANY FOR THE YEARS ENDING JUNE 30, 2011 AND 2010 (NEXT YEAR). MCERA APOLOGIZES FOR THE INCONVENIENCE.