Merced County Employees' Retirement Association

A Pension Trust Fund of the County of Merced, California

MCERA

COMPREHENSIVE ANNUAL FINANCIAL REPORT

FOR THE FISCAL YEAR ENDED JUNE 30, 2006

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

A Pension Trust Fund of the County of Merced, California

Comprehensive Annual Financial Report

For the years ended June 30, 2006 and 2005

Issued By

Maria L. Arevalo
Plan Administrator

Gale Garcia
Fiscal Operations

MCERA
MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION
3199 M Street
Merced, CA 95348

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MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

TABLE OF CONTENTS

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

TABLE OF CONTENTS

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

Introductory Section

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Merced, California 95348
Telephone 209-725-3636
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Maria L. Arevalo
Plan Administrator

LETTER OF TRANSMITTAL

September 1, 2006

Dear Board Members:

As the Administrator of the Merced County Employees' Retirement Association (MCERA), I am pleased to present this Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2006 and 2005.

The Comprehensive Annual Financial Report (CAFR)

The **Introductory Section** describes MCERA's management and organizational structure; identifies the members of the MCERA Board of Retirement (the Board); provides a listing of the professional consultants utilized by MCERA; and presents this Letter of Transmittal.

The **Financial Section** presents the report of the independent auditor, Macias, Gini & O'Connell, LLP, along with MCERA management's discussion and analysis of MCERA's financial statements and supplementary financial information; and the financial statements, explanatory notes and supplementary schedules themselves.

The **Investment Section** contains a report on MCERA's investment performance from MCERA's investment consultant, Milliman USA, along with information regarding MCERA's investment policies, asset allocation, investment holdings and investment management fees.

The **Actuarial Section** communicates MCERA's funding status, and presents other actuarial-related information, including the certification of MCERA's actuary, Buck Consultants.

The **Statistical Section** presents information pertaining to MCERA's operations on a multi-year basis.

The accuracy of the data and the completeness and fairness of the presentation of the CAFR, including all disclosures, is the responsibility of MCERA management.

The discussion that follows serves as a brief introduction to and overview of the information contained in the sections of the CAFR noted above.

MCERA and its Services

The Merced County Employees' Retirement Association is a public employee retirement system established by the County of Merced on July 1, 1950. MCERA is administered by the Board of Retirement to provide retirement, disability, death, and survivor benefits for eligible employees of the County of Merced, Superior Court of California, County of Merced and the Merced Cemetery District pursuant to the California Constitution, the County Employees' Retirement Law of 1937 (Government Code Sections 31450 et. seq.) (the 1937 Act), and the by-laws, policies and procedures adopted by the MCERA Board. The County of Merced Board of Supervisors may also adopt resolutions, as permitted by the 1937 Act, which may affect benefits of MCERA members.

The MCERA Board of Retirement is responsible for the general management of the retirement system, including making benefit determinations and managing the investment of the system's assets. The day-to-day management of MCERA is vested in an Administrator appointed by the Board.

The Board is comprised of nine members and one alternate; two elected by the active general membership, one regular and one alternate elected by the active safety membership, one elected by the retired membership, four appointed by the County of Merced Board of Supervisors, and the County of Merced Treasurer, who serves as an ex-officio member. With the exception of the County Treasurer, Board members serve three-year terms, with no term limits.

Financial Information

A review of MCERA's fiscal affairs for the year ended June 30, 2006 is presented in Management's Discussion and Analysis (MD&A), which is located in the Financial Section of this CAFR. Together, the MD&A and this Letter of Transmittal provide an expanded overview of MCERA's financial activities for the year.

The audit of MCERA's financial statements has been performed by an independent auditor, Macias Gini & O'Connell, LLP, who has attested that the financial statements are presented in conformity with generally accepted accounting principles and are free of material misstatement. MCERA's management is responsible for establishing and maintaining the internal control structure designed to ensure that MCERA's assets are protected from loss, theft or misuse. Sufficient internal controls exist to provide reasonable assurance regarding the safekeeping of assets and fair presentation of the financial statements and supporting schedules.

MCERA's financial statements were prepared using the accrual basis of accounting, which recognizes revenue when earned and liabilities when they are incurred, regardless of when payment is due or made. The ***Statement of Plan Net Assets*** is a point in time presentation of account balances as of the fiscal year end. It indicates the assets available for future payments to retirees and any current liabilities. The ***Statement of Changes in Plan Net Assets*** presents the current year additions and deductions to the retirement plan. Both statements comply with the pronouncements of the Governmental Accounting Standard Board (GASB), which require certain disclosures and methods of accounting. The ***Notes to Basic Financial Statements*** provide additional information that is essential to a full understanding of the data provided in the financial statements.

In addition, the ***Required Supplementary Schedules*** and supporting ***Notes to Required Supplementary Schedules*** provide information concerning the retirement system's progress in funding its obligation to provide pension benefits to MCERA members. Finally, the ***Other Supplementary Schedules*** present information concerning MCERA's operations on a multi-year basis.

The information in these financial statements, schedules and supporting notes regarding the retirement system's net assets held in trust to pay pension benefits is generally considered to be a good measure of the retirement system's financial position. Over time, increases or decreases in the retirement system's net assets is one indicator of whether the system's financial health is improving or deteriorating. Other factors however, such as investment market conditions, should also be considered in measuring the retirement system's overall health.

As of June 30, 2006, MCERA's net assets held in trust totaled approximately $445.9 million reflecting an increase of approximately $26.8 million (approximately 6.4%) over the net assets held in trust at the end of the previous fiscal year. This increase was primarily due to increased employer and employee contributions and a modest upturn in the investment markets as explained more fully in the report of MCERA's investment consultant, which is located in the Investment Section of this CAFR.

Actuarial Funding Status

MCERA's funding objective is to meet long-term benefit promises by maintaining a well-funded plan status and obtaining optimum investment returns consistent with the assumption of prudent risk. The greater the level of plan funding, the larger the ratio of assets accumulated to actuarial accrued liability and the greater the level of investment return potential.

Pursuant to provisions in the 1937 Act, MCERA engages an independent actuarial firm to perform actuarial valuations of the system. As part of the valuation, economic assumptions are reviewed regularly. In addition, every three years a triennial experience study of the MCERA membership is conducted and non-economic assumptions are modified as necessary. The most recent actuarial valuation as of June 30, 2005, found the retirement system's actuarial funding status (the ratio of actuarial assets to actuarial liabilities) to be 72.7%. The funded percentage decreased from 80.8% in 2004. This decrease can be attributed to pension benefit increases, investment losses, and changes to the actuarial assumptions.

Investments

The Board of Retirement has exclusive control of all investments of the retirement system and is responsible for establishing investment objectives, strategies and policies. Pursuant to the California Constitution and the 1937 Act, the Board is authorized to invest in any form or type of investment deemed prudent in the informed judgment of the Board. In making decisions regarding the MCERA investment portfolio, the Board acts in a fiduciary capacity and must discharge its duties in accordance with fiduciary principles. In carrying out its investment responsibilities, the Board receives guidance from a professional investment consultant, Milliman USA.

The Board of Retirement has adopted an Investment Policy, which provides the framework for the management of MCERA's investments. The Investment Policy establishes the investment program goals, asset allocation policies, performance objectives, investment management policies and risk controls. The Investment Policy also defines the principal duties of the Board, MCERA's custodian bank and MCERA's investment managers.

The asset allocation plan adopted by the Board is an integral part of MCERA's investment program. It is designed to provide an optimum mix of asset classes with return expectations to satisfy expected liabilities while minimizing risk exposure. A summary of the asset allocation plan can be found in the Investment Section of this CAFR.

The assets of the MCERA are exclusively managed by external professional investment management firms. A listing of the investment professionals who provide services to MCERA can be found on page 15 of this CAFR.

For the fiscal year ending June 30, 2006, investments provided a 8.3% rate of return. MCERA's annualized rate of return over the last three and five years was 10.4% and 6.2% , respectively.

Service Efforts and Accomplishments

The Merced County Board of Supervisors adopted enhanced retirement benefits for county employees pursuant to Government Code Sections 31676.17 and 31664.1. Prior to the adoption of the benefits, commonly known as 3% at 50 for Tier I & Tier II safety members and 3% @ 60 for general members, the Board of Supervisors reviewed various actuarial studies of the cost and implementation of the new benefit levels. The new benefit levels were adopted on March 15, 2005 for general members, effective July 1, 2005 for safety members, effective for the Superior Court, County of Merced November 4, 2005. Further, with the recommendation of the MCERA Board, the Merced County Board of Supervisors approved an increased death benefit for retirees from $1000 to $3000 effective May 2, 2006.

This past year the MCERA acquired a new auditor. Macias, Gini & O'Connell was retained as the result of a Request for Proposal process. MCERA also initiated a search for a new custodial bank and expects to complete the conversion to the new custodian by November 2006.

In the last year, the Retirement Board, pursuant to its investment policy, increased its allocation by $15 million to its private equity asset class. The Board also adopted new by-laws providing for the addition of an alternate elected safety member to the Board and new provisions to improve the day to day operations of the system. A new member benefits handbook was also issued in January updating information for its members.

Certificate of Achievement

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the MCERA for its CAFR for the fiscal year ended June 30, 2005. The certificate of Achievement is a prestigious national award that recognizes conformance with the highest standards for preparation of state and local government financial reports.

In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report, whose contents conform to program standards. The CAFR must satisfy both generally accepted accounting principals and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. This is MCERA's second Certificate of Achievement for Excellence in Financial Reporting. We believe our current report continues to conform to the Certificate of Achievement program requirements.

Acknowledgements

The compilation of this report reflects the dedicated efforts of the MCERA staff and I would like to express my great appreciation for their hard work. I would also like to thank MCERA's professional consultants – particularly our actuary, our investment consultant and our auditors – for their generous and invaluable assistance. Finally, I would like to acknowledge the Board of Retirement for its leadership and commitment to the highest fiduciary standards.

Respectfully submitted,

Maria L. Arevalo
Plan Administrator

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Merced County

Employees' Retirement Association, California

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2005

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.

President

Executive Director

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

BOARD OF RETIREMENT AT JUNE 30, 2006

TRUSTEES	APPOINTED/ELECTED	TERM EXPIRES
LeRoy Gilsdorf	Elected by Retired Members	January 1, 2009
Karen Rodriguez Human Services Agency (Chairperson)	Elected by General Members	July 1, 2007
Karen Adams	County Treasurer	January 1, 2007
Donald Washburn (Vice-Chairman)	Elected by General Members	July 1, 2006
Kathleen Crookham County Supervisor	Appointed by County Board of Supervisors	July 1, 2007
Janey Cabral	Appointed by County Board of Supervisors	July 1, 2006
Ralph Busby	Appointed by County Board of Supervisor	January 1, 2009
Jim Lindsey	Appointed by County Board of Supervisors	July 1, 2008
David Baker County Sheriff's Department	Elected by Safety Members	January 1, 2009
Dwayne McCoy County Probation Department (Alternate)	Elected by Safety Members	January 1, 2009

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

ORGANIZATION CHART AT JUNE 30, 2006

BOARD OF RETIREMENT

Maria L. Arevalo
PLAN ADMINISTRATOR

Annamarie Griffin
RETIREMENT OFFICER

Gale Garcia
RETIREMENT ACCOUNTING ANALYST

Michelle Latta
RETIREMENT BENEFIT SPECIALIST

Roseann Guthrie
ACCOUNT CLERK

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

LIST OF PROFESSIONAL CONSULTANTS AT JUNE 30, 2006

CONSULTING SERVICES

INVESTMENT CONSULTANT
Milliman USA

ACTUARY
Buck Consultants

AUDITOR
Macias Gini & O'Connell, LLP

CUSTODIAN
The Bank Of New York

DATA PROCESSING
County Information
Management Systems

LEGAL COUNSEL
County Counsel of Merced County
Mason, Robbins, Gnass & Browning

MEDICAL ADVISOR
Dr. Theresa Smith

INVESTMENT SERVICES

FIXED INCOME
Lehman Brothers Asset Management
Aberdeen Asset Management

REAL ESTATE
UBS Global Asset Management
PaineWebber Limited Partnership

DOMESTIC EQUITY
Delta Asset Management
Earnest Partners, LLC
Mellon Capital Management
Wasatch Advisors
Wentworth, Hauser & Violich

INTERNATIONAL EQUITY
Invesco Global Asset Management

PRIVATE EQUITY
Invesco Private Capital
Adams Street Partners, LLC
Pantheon Ventures, Inc.

COMMISSION RECAPTURE BROKERS
Donaldson & Co.
Lynch, Jones & Ryan

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MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

Financial Section

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MACIAS GINI & O'CONNELL LLP
CERTIFIED PUBLIC ACCOUNTANTS & MANAGEMENT CONSULTANTS

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Sacramento, CA 95816
916.928.4600

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515 S. Figueroa Street, Suite 325
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402 West Broadway, Suite 400
San Diego, CA 92101
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INDEPENDENT AUDITOR'S REPORT

To the Board of Retirement of the
Merced County Employees' Retirement System
Merced, California

We have audited the accompanying statement of plan net assets of the Merced County Employees' Retirement Association (the Association), as of June 30, 2006, and the related statements of changes in plan net assets for the year then ended. These financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of Merced County Employees' Retirement Association as of June 30, 2005, were audited by other auditors whose report dated September 1, 2005, expressed an unqualified opinion on those statements

We conducted our 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 we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2006 financial statements referred to above present fairly, in all material respects, the plan net assets of the Merced County Employees' Retirement Association as of June 30, 2006, and the changes in plan net assets for the year then ended in conformity with the accounting principles generally accepted in the United States of America.

As described in Note 2, effective July 1, 2005, the Association adopted the provisions of Governmental Accounting Standards Board Statement No. 44, *Economic Condition Reporting: The Statistical Section – An Amendment of NCGA Statement 1.*

In accordance with *Government Auditing Standards*, we have issued our report dated September 1, 2006, on our consideration of the Association's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations and contracts, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.The Management's Discussion and Analysis on pages 21 through 27, the required supplementary schedules on pages 51 through 53 are not a required part of the basic financial statements, but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements. The other supplementary schedules in the financial section are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has been subjected to auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory, investment, actuarial and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Macias Gini & O'Connell LLP

Certified Public Accountants

Sacramento, California
September 1, 2006

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

MANAGEMENT'S DISCUSSION AND ANALYSIS

We are pleased to provide this overview and analysis of the financial activities of the Merced County Employees' Retirement Association (MCERA) for the fiscal year ended June 30, 2006 and 2005. We encourage readers to consider the information presented here in conjunction with the additional information furnished in the Letter of Transmittal.

Financial Highlights

- At the close of the fiscal year, MCERA's net assets held in trust for the payment of pension benefits totaled $445,896,721. All plan net assets are available to meet MCERA's ongoing obligations to plan participants and their beneficiaries.

- Over the fiscal year, MCERA's total net assets held in trust for pension benefits increased by $26,750,266 (an increase of 6.4%).

- MCERA's funding objective is to meet long-term benefit obligations through contributions and investment income. As of June 30, 2005, the date of MCERA's last actuarial valuation, MCERA's funded ratio was 72.7%. In general, this indicates that for every one dollar of benefits due, MCERA has slightly more than $.72 of assets available for payment.

- Additions to Plan Net Assets for the year were a positive $55,163,563, which includes member and employer contributions of $22,971,691 and a net investment gain of $32,191,872.

- Deductions in Plan Net Assets increased from $25,993,178 in the last fiscal year to $28,413,297 in the current fiscal year (an increase of approximately 9.3%).

Overview of the Financial Statements

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

1. Statement of Plan Net Assets

2. Statement of Changes in Plan Net Assets

3. Notes to the Basic Financial Statements

4. Required Supplementary Schedules

5. Other Supplementary Schedules

The ***Statement of Plan Net Assets*** is a point in time picture of account balances as of the fiscal year end. It indicates the assets available for future payments to retirees and any current liabilities.

The ***Statement of Changes in Plan Net Assets***, on the other hand, provides a view of the current year additions to and deductions from the retirement plan.

Both financial statements are in compliance with the accounting principles and reporting guidelines set forth in Governmental Accounting Standards Board (GASB) Statements 25, 28, 34, 40 and 44. These pronouncements require certain disclosures, and also require that state and local governments report using the full accrual method of accounting. MCERA complies with all material requirements of these pronouncements.

The two financial statements report information about MCERA's financial activities. As previously noted, the 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 revenue and expenses are taken into account regardless of when cash is received or paid. All investment gains or 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.

The information reported in these two financial statements regarding the retirement system's net assets held in trust to pay pension benefits is generally considered to be a good measure of the retirement system's financial position. Over time, increases or decreases in the retirement system's net assets is one indicator of whether the system's financial health is improving or deteriorating. Other factors however, such as investment market conditions, should also be considered in measuring the retirement system's overall health.

The ***Notes to Basic Financial Statements*** are an integral part of the financial report and provide additional information that is essential to a full understanding of the data provided in the financial statements.

In addition to the financial statements and accompanying notes, this report presents certain required supplementary information concerning MCERA's funding status. The ***Required Supplementary Schedules*** include the Schedule of Funding Progress and Schedule of Employer Contributions. The Schedule of Funding Progress provides historical information about the actuarial funding status of the plan and reflects the progress made in accumulating sufficient assets to pay benefits when due. The Schedule of Employer Contributions provides historical information about annual required contributions of the employer and the actual contributions made. Together, these schedules and the supporting ***Notes to Required Supplementary Schedules*** provide information to help promote understanding of the changes in the funding status of the plan over time. Finally, the ***Other Supplementary Schedules*** represent information concerning MCERA's operations on a multi-year basis.

Financial Analysis

As previously noted, net assets may serve over time as a useful indication of MCERA's financial position. At the close of the fiscal year, MCERA's assets exceeded its liabilities by $445,896,721. All of the net assets are available to meet MCERA's ongoing obligations to plan participants and their beneficiaries.

Plan net assets as of June 30, 2006 totaled $445.9 million which is $26.8 million or 6.4% more than the prior year. This result essentially reflects the 6.2% increase in the balance of MCERA's investments during 2006.

The increase in plan net assets is a direct result of strict adherence to MCERA's Investment Guidelines, Policies, and Procedures. The disciplined approach, combined with the asset allocation and rebalancing program adopted by MCERA's Board, have enabled MCERA to maximize any upturns in the Market. Much like the past few years, the investment markets were quite volatile during the year, with investment performance varying from quarter to quarter. Despite these market fluctuations, MCERA's management and actuary concur that MCERA remains in a solid financial position to meet its obligations to the plan participants and beneficiaries. MCERA's sound financial position is a result of a prudently diversified investment program designed to maximize the return on invested assets while minimizing risk exposure. More detailed information is available in the investment section.

MCERA's Net Assets as of June 30, 2006 and 2005

	2006	2005	Increase/ (Decrease) Amount	Increase/ (Decrease) Percent
Current and Other Assets	$ 20,495,905	$ 22,016,476	$ (1,520,571)	-6.9%
Investments at Fair Value	436,105,973	410,750,152	25,355,821	6.2%
Fixed Assets	29,260	28,551	709	2.5%
Total Assets	**456,631,138**	**432,795,179**	**23,835,959**	**5.5%**
Current Liabilities	10,734,417	13,648,724	(2,914,307)	-21.4%
Total Liabilities	**10,734,417**	**13,648,724**	**(2,914,307)**	**-21.4%**
Net Assets	**$ 445,896,721**	**$ 419,146,455**	**$ 26,750,266**	**6.4%**

MCERA's Net Assets as of June 30, 2005, and 2004

	2005	2004	Increase/ (Decrease) Amount	Increase/ (Decrease) Percent
Current and Other Assets	$ 22,016,476	$ 21,750,577	$ 265,899	1.2%
Investments at Fair Value	410,750,152	393,560,050	17,190,102	4.4%
Fixed Assets	28,551	36,434	(7,883)	-21.6%
Total Assets	**432,795,179**	**415,347,061**	17,448,118	4.2%
Current Liabilities	13,648,724	18,563,370	(4,914,646)	-26.5%
Total Liabilities	**13,648,724**	**18,563,370**	**(4,914,646)**	**-26.5%**
Net Assets	**$ 419,146,455**	**$ 396,783,691**	**22,362,764**	**5.6%**

Reserves

MCERA's reserves are established from contributions and the accumulation of investment income after satisfying investment and administrative expenses. MCERA previously implemented GASB Statement 25, which impacted the reserve accounts and the amount of interest credited to reserve accounts. Under GASB Statement 25, investments are stated at fair value instead of at cost, and fair value includes the recognition of unrealized gains and losses in the current period. These unrealized gains and losses are tracked in a reserve account called the Market Value Fluctuation Reserve. As a result of the modest upturn in the investment markets (and the corresponding increase in the fair value of MCERA's investments), the Market Value Fluctuation Reserve increased by $3,592,713 in the current fiscal year, resulting in a positive closing balance of $69,662,223. The investment performance was positive in the current fiscal year (approximately 8.3% before fees).

MCERA's Reserves as of June 30, 2006, 2005, and 2004

	2006	2005	2004
Active Member Reserves	$ 54,825,607	$ 49,161,941	$ 48,707,821
Employer Advance Reserves	66,763,872	73,309,666	86,260,253
Retired Member Reserves	230,191,661	219,322,395	204,267,473
Ad-Hoc COLA Reserve	1,568,795	1,553,241	1,544,447
Interest Fluctuation Reserve	-	-	-
Market Value Fluctuation Reserve	69,662,223	66,069,509	45,993,069
Medical Insurance Trust	-	2,610,752	5,301,792
Contingency Reserve	18,194,769	4,327,952	3,967,837
Internal Revenue Code (IRC) Section 401(h)	4,689,794	2,790,999	740,999
Total Reserves at Fair Value	**$ 445,896,721**	**$ 419,146,455**	**$ 396,783,691**

MCERA's Activities

A modest upturn in the investment markets resulted in a June 30, 2006 fiscal year increase of $26,750,266 in MCERA's net assets (an increase of approximately 6.4% from the previous year). The key elements of this increase is in direct relationship with the following changes in plan net assets.

Changes in Net Assets

A. Additions to Plan Net Assets

The reserves needed to finance retirement benefits are normally accumulated through the collection of employer and employee contributions and through earnings on investment income (net of investment expenses). Additions to Plan Net Assets for the current fiscal year totaled a positive $55,163,563, primarily due to investment gains. Overall, revenues for the fiscal year were up $6,807,621 (approximately 14.1%) from the fiscal year ended June 30, 2005, due to investment gains and increased employee and employer contributions. In the 2004-2005 fiscal year, investment gains resulted in a positive $48,355,942 in total revenue, which was a decrease of $8,358,800 from the total revenue in the 2003-2004 fiscal year. Employer and employee contributions increased in the current fiscal year due to the actuarial assumptions and experience of the Association. The increase in the MCERA's employer and employee rates due to the enhanced benefit levels are reflected in the actuarial valuation for June 30, 2005. The Investment Section of this report provides a more detailed review of the investment markets and investment performance for the current fiscal year.

Additions to Plan Net Assets
(For the Years Ended June 30, 2006 and 2005)

	2006	2005	Increase/ (Decrease) Amount	Increase/ (Decrease) Percent
Employer Contributions	$ 14,749,934	$ 8,930,842	$ 5,819,092	65.2%
Member Contributions	8,221,757	4,584,598	3,637,159	79.3%
Net Investment Income/(Loss)	32,191,872	34,840,502	(2,648,630)	-7.6%
Total Additions	**$ 55,163,563**	**$ 48,355,942**	**$ 6,807,621**	**14.1%**

Additions to Plan Net Assets
(For the Years Ended June 30, 2005 and 2004)

	2005	2004	Increase/ (Decrease) Amount	Increase/ (Decrease) Percent
Employer Contributions	$ 8,930,842	$ 7,268,826	$ 1,662,016	22.9%
Member Contributions	4,584,598	3,347,455	1,237,143	37%
Net Investment Income/(Loss)	34,840,502	46,098,461	(11,257,959)	-24.4%
Total Additions	**$ 48,355,942**	**$ 56,714,742**	**$ (8,358,800)**	**(14.7)%**

B. Deductions from Plan Net Assets

MCERA was created to provide lifetime retirement annuities, survivor benefits and permanent disability benefits to qualified members and their beneficiaries. The cost of such programs includes recurring benefit payments, as designated by the plan; refunds of contributions to terminated employees; and the cost of administering the retirement system.

Deductions for the current fiscal year totaled $28,413,297, an increase of 9.3% from the previous year. The increase in expenses in the current fiscal year can be attributed primarily to the retiree payroll, which grew approximately 9.1% due to an increase in the number and average amount of benefits paid to retirees. Deductions for the 2005 fiscal year totaled $25,993,178, an increase of 6.4% from the 2004 fiscal year. Retiree payroll was the largest part of this increase, which grew 12.0%.

Deductions in Plan Net Assets
(For the Years Ended June 30, 2006 and 2005)

	2006	2005	Increase/ (Decrease) Amount	Increase/ (Decrease) Percent
Benefits	$ 26,263,569	$ 24,069,742	$ 2,193,827	9.1%
Administrative Expenses	649,080	602,451	46,629	7.7%
Refunds of Contributions	602,210	409,034	193,176	47.2%
Retiree Health Insurance	850,000	850,000	0.00	0%
Actuarial Expense	48,438	61,951	(13,513)	-21.8%
Total Deductions	**$ 28,413,297**	**$ 25,993,178**	**$ 2,420,119**	**9.3%**

Deductions in Plan Net Assets
(For the Years Ended June 30, 2005 and 2004)

	2005	2004	Increase/ (Decrease) Amount	Increase/ (Decrease) Percent
Retiree Payroll	$ 24,069,742	$ 21,498,606	$ 2,571,136	12%
Administrative Expense	602,451	830,439	(227,988)	(27.5)%
Refunds of Contributions	409,034	349,488	59,546	17%
Retiree Health Insurance	850,000	1,758,550	(908,550)	(51.7)%
Actuarial Expense	61,951	-	61,951	100%
Total Deductions	**$ 25,993,178**	**$ 24,437,083**	**$ 1,556,095**	**6.4%**

MCERA's Fiduciary Responsibilities

MCERA's Board and management staff are fiduciaries of the pension trust fund. Under the California Constitution, the system's assets must be used exclusively for the benefit of plan participants and their beneficiaries.

Requests for Information

This financial report is designed to provide the Retirement Board, the MCERA membership, taxpayers, investment managers and creditors with a general overview of MCERA's financial condition and to demonstrate accountability for the funds MCERA receives and manages. Questions concerning any of the information provided in this report, or requests for additional information should be addressed to:

Merced County Employees' Retirement Association
3199 M Street
Merced, California 95348

Respectfully submitted,

Maria L. Arevalo
Plan Administrator

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

STATEMENTS OF PLAN NET ASSETS

As of June 30, 2006 and 2005

ASSETS	June 30, 2006	June 30, 2005
Cash and short-term investments:		
Cash invested with Merced County Treasurer	$ 8,569,708	$ 4,064,191
Other cash and cash equivalents	7,725,097	11,644,169
Receivables:		
Other		5,175
Bond interest	1,024,623	1,035,337
Stock dividends	163,818	160,823
Contributions	485,794	937,532
Securities sold	2,481,865	4,169,249
Total receivables	4,156,100	6,308,116
Investments at fair value:		
U.S. government and agency obligations	58,210,041	70,123,894
Domestic fixed income	60,497,695	60,072,558
Common stocks (individual equities)	188,036,203	169,817,224
Invesco (international equity fund)	43,947,332	35,024,262
Mellon Capital Mgmt (index fund)	50,564,107	45,973,407
UBS Real Estate Separate Account (RESA)	31,212,368	28,132,565
Alternative investments	3,163,227	1,131,242
Direct real estate investment	475,000	475,000
Total investments	436,105,973	410,750,152
Prepaid expenses	45,000	-
Capital assets: Net of accumulated depreciation of $42,969 and $34,513 respectively	29,260	28,551
Total assets	456,631,138	432,795,179
LIABILITIES		
Accounts payable	1,318,449	1,219,946
Securities purchased	9,373,556	12,386,414
Unclaimed contributions	42,412	42,364
Total liabilities	10,734,417	13,648,724
Net assets held in trust for pension benefits	$ 445,896,721	$ 419,146,455

(A *Schedule of Funding Progress* for pension benefits is presented on page 51)

The accompanying notes are an integral part of these financial statements

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

STATEMENTS OF CHANGES IN PLAN NET ASSETS
For the Years Ended June 30, 2006 and 2005

	June 30, 2006	June 30, 2005
ADDITIONS		
Contributions:		
Employer	14,749,934	$ 8,930,842
Plan members	8,221,757	4,584,598
Total contributions	22,971,691	13,515,440
Net appreciation in fair value of investments	3,592,713	20,076,440
Partnership income	-	4,196
Investment income	31,010,792	16,992,698
Other revenue	51,748	58,442
Less investment expenses	(2,463,381)	(2,291,274)
Net investment income	32,191,872	34,840,502
Total additions	55,163,563	48,355,942
DEDUCTIONS		
Post employment health subsidies	850,000	850,000
Benefits	26,263,569	24,069,742
Refunds of contributions	602,210	409,034
Actuarial expense	48,438	61,951
Administrative expense	649,080	602,451
Total deductions	28,413,297	25,993,178
Net increase	26,750,266	22,362,764
Net assets held in trust for pension benefits at beginning of year	419,146,455	396,783,691
Net assets held in trust for pension benefits at end of year	$ 445,896,721	$ 419,146,455

The accompanying notes are an integral part of these financial statements

NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2006 and 2005

1. PLAN DESCRIPTION

A. General Information

The Merced County Employees' Retirement Association (MCERA or the System) was established July 1, 1950, under and subject to the legislative authority of the State of California as enacted and amended in the County Employees Retirement Act of 1937 (the "1937 Act"). The retirement system was voter approved by a greater than 2/3 majority of the electorate of Merced County (The County). The System was integrated with Social Security on January 1, 1956. Members of the System at that time had a one–time option to convert to the new System or remain in the previous System. MCERA administers a cost sharing, multiple-employer defined benefit pension plan (the Plan). MCERA's annual financial statements are included in the County's financial reports as a pension trust fund.

The management of the retirement system MCERA is vested in a Board of Retirement that consists of nine members and one alternate:

1. County Treasurer
2. Two elected general members
3. One member of the County Board of Supervisors
4. Three members appointed by the County Board of Supervisors who are not affiliated with county government
5. One elected retired member
6. One elected safety member
7. One alternate safety member

Day to day management of MCERA is vested in a Plan Administrator who is appointed by and serves at the pleasure of the Board of Retirement.

MCERA, with its own governing board, is an independent governmental entity separate and distinct from the County and derives its authority from California Government Code Sections 31450 et seq., and the California Constitution.

B. Membership Structure

(1) *General*

Plan members are classified as either General or Safety members. Membership becomes effective on the first day of service. Members include all permanent employees appointed to permanent positions or permanent part-time positions within the Merced County, Superior Court, County of Merced, and the Merced Cemetery District. Newly hired persons age 60 and over and elected officials may waive membership in the retirement system.

(2) *Multi-Tier Benefits*

All employees hired prior to June 13, 1994, and all executive "A" Level management (i.e., appointed and elected unrepresented managers per Amendment to County Board of Supervisors Resolution 94-89, effective July 1, 2000) are members of Tier I. The Tier I retirement benefit is based on the highest one year compensation. The minimum age to retire is 50 or any age with 30 years of service credit (20 years for Safety). General and Safety Tier I members are eligible for post-retirement cost of living adjustments.

The County Board of Supervisors adopted a new retirement tier (Tier II) for both General and Safety members hired after June 13, 1994. Benefits for members under Tier II are based on 3 years final average salary and are not eligible for post-retirement cost of living adjustments.

The structure of the membership on June 30, 2006 was as follows:

	GENERAL		SAFETY		
Active Members	**Tier I**	**Tier II**	**Tier I**	**Tier II**	**TOTAL**
Vested	547	638	96	61	1,342
Non-Vested	21	756	3	156	936
Inactive Members					
Deferred and Inter-System Members	273	128	57	19	477
Unclaimed	9	23	1		33
TOTAL MEMBERS	**850**	**1,545**	**157**	**236**	**2.788**
Retired Members					
Service Retirements	992	15	110	2	1,119
Beneficiaries	130	-	19	-	149
Service Connected Disability	71	1	85	3	160
Non-service Connected Disability	58	5	4	-	67
Survivors	19	2	5	-	26
TOTAL RETIRED MEMBERS	**1,270**	**23**	**223**	**5**	**1,521**

The structure of the membership on June 30, 2005 was as follows:

	GENERAL		SAFETY		
Active Members	**Tier I**	**Tier II**	**Tier I**	**Tier II**	**TOTAL**
Vested	593	555	109	55	1,312
Non-Vested	19	767	2	130	918
Inactive Members					
Deferred and Inter-System Members	283	104	57	16	460
Unclaimed	9	22	1	-	32
TOTAL MEMBERS	**904**	**1,448**	**169**	**201**	**2,722**
Retired Members					
Service Retirements	965	6	102	-	1,073
Beneficiaries	128	-	19	-	147
Service Connected Disability	73	1	86	3	163
Non-service Connected Disability	61	4	4	-	69
Survivors	19	-	5	-	24
TOTAL RETIRED MEMBERS	**1,246**	**11**	**216**	**3**	**1,476**

C. Benefit Provisions

(1) *Service Retirement Benefit*

Members with ten years of service and who have attained the minimum age of 50 (age 55 for General Tier II) are eligible to receive a lifetime monthly retirement benefit. A member with 30 years of service (20 years for Safety), regardless of age is eligible for retirement benefits. Members who are at least 70 years of age are eligible to retire, regardless of years of service. The service retirement benefit is a percentage of monthly final average salary per year of service, depending on age at retirement. For members integrated with Social Security, the benefit is reduced by 1/3 of the percentage multiplied by the first $350 of monthly final average salary, per year of service credited after January 1, 1956. The actual benefit paid will also be affected by the benefit payment option selected by the member.

The County Board of Supervisors adopted Government Code Section 31676.17 of the County Employees Retirement Law of 1937 for all County General members (Tier I and Tier II) on March 15, 2005, Government Code Section 31664.1 for all Safety member (Tier I and Tier II) on July 1, 2005 and Government Code Section 31676.17 for Superior Court of California, County of Merced members on November 4, 2005. The enhanced benefits do not apply to County members who, on March 15, 2005 were deferred, reciprocal or a Merced County Cemetery District employee.

Percentage of Final Average Salary for Each Year of Service (Rounded)

	Tier I		Tier II	
Retirement Age	General	Safety	General	Safety
50	2.00%	3.00%	-	3.00%
55	2.50%	3.00%	2.50%	3.00%
60+	3.00%	3.00%	3.00%	3.00%

(2) ***Retirement Options***

Unmodified

Under the current "Fixed Formula" retirement, a member may elect the "unmodified" allowance, which provides the maximum allowance to the member for life, with a continuance of 60% of the allowance to the spouse or registered domestic partner if the spouse or registered domestic partner is designated as beneficiary. No allowance, however, shall be paid to a surviving spouse or domestic partner unless he or she is married to the member or has been registered as a domestic partner at least one year prior to the date of retirement. In the event of the death of the retiree, spouse or domestic partner, any balance of the retiree's contributions, less retirement allowances received, is payable to an alternate beneficiary.

Option No. 1

The member may elect to receive a slightly reduced monthly retirement allowance, payable throughout his or her life, with the proviso that upon his or her death, his or her accumulated contributions less the actual annuity payments received by the retiree, will be paid to a designated beneficiary. Under this option, beneficiaries may be changed after retirement.

Option No. 2

The member receives a considerably reduced monthly allowance, with the proviso that 100% of the retiree's benefit will continue to be paid after the member's death to a beneficiary named at the time of retirement. All payments stop at the death of both annuitants.

Option No. 3

A reduced allowance is paid to the member with 50% of the member's allowance continuing to the beneficiary after the member's death. As in Option No. 2, all payments stop at the death of both annuitants.

(3) ***Cost of Living Adjustment***

Annual cost-of-living adjustments (COLAs) to retirement allowances may be granted by the Retirement Board in accordance with governing law. The current maximum increase in a retirement allowance is 3% per year. Any increase is based on the change in the Bureau of Labor Statistics' Consumer Price Index for All Urban Consumers (CPI) for the calendar year prior to the April 1 effective date of the COLA. The amount of any actual CPI above the 3% maximum is accumulated. Accumulated COLAs may be used in future years, at the Retirement Board's discretion, when the cost-of-living change is less than the maximum 3%. Tier II members are not eligible for any cost-of-living increases in their retirement allowances.

(4) ***Disability Benefit***

Members with 5 years of service, regardless of age, are eligible for non-service connected disability benefits. Tier I member benefits are 1.5% (1.8% for Safety members) of final average salary for each year of service. If this benefit does not equal 1/3 of final average salary, the benefit is increased by the above percentage of final average salary for the years that would have been credited had the member worked to age 65 (age 55 for Safety members). The total benefit cannot exceed 1/3 of the final average salary.

Tier II non-service connected disability benefits are calculated in the same manner as Tier I.

If the disability is service connected, the member may retire regardless of length of service, and the benefit is 50% of final average salary, unless the member is also eligible for a service retirement, in which case the member receives the greater of the two amounts.

(5) *Death Benefit Before Retirement*

In addition to the return of the member's contributions plus interest, MCERA provides a basic death benefit payable to the member's beneficiary or estate equal to one month's salary for each completed year of service under the System, based on the final year's average salary, but not to exceed six (6) months salary. Depending on length of service, a monthly allowance could be selected by the surviving spouse to be paid the rest of his or her life as an alternate benefit.

If a member dies while eligible for service retirement or non-service connected disability, the spouse may receive 60% of the allowance that the member would have received for retirement on the day of his or her death in lieu of the basic death benefit. If the member was below the qualifying retirement age at the time of death, the surviving spouse may elect to leave the member's accumulated contributions on deposit until such time as the member would have attained the qualifying age had he or she lived, at which time the spouse may exercise the option above. Unmarried minor children of the deceased member may continue to receive this allowance until marriage or attaining age 18 (21 if full-time student in an accredited school), upon the death of the surviving spouse or in place of the spouse if he or she does not survive the death of the member.

If a member dies as a result of service-connected injury or disease arising out of the course of his or her employment, his or her surviving spouse may elect, in lieu of the basic death benefit, to receive a monthly allowance of one-half of the member's final compensation. Unmarried minor children of the member may receive the same monthly allowance prior to their marriage or attaining age 18 (21 if a full-time student in an accredited school) if there is no surviving spouse or upon the death of the spouse.

(6) *Death Benefit After Retirement*

If a member dies after retirement, a lump sum amount of $3,000 (Government Code Section 31789.3 adopted May 2, 2006) is paid to the beneficiary or estate; however, if the member is an inter-retirement system member, this benefit is payable only by the retirement system under which the member last worked.

If the retirement was for service-connected disability, 100% of the amount the member was receiving at the time of death is continued to the surviving spouse for life.

If the retirement was for other than service-connected disability, there are several options available to the member.

(7) *Terminated Members*

A member leaving covered employment after completing five years of credited service becomes eligible for a deferred retirement allowance, provided the member lives to the minimum service retirement age and does not withdraw his or her accumulated contributions. A member must elect deferred status within 180 days after termination. Members leaving employment with less than five years of service are not eligible to receive a retirement benefit. Non-vested members (less than five years of service) may leave their contributions on deposit and continue to be credited interest or they can choose to withdraw their contributions. County-paid employee contributions under various Memoranda of Understanding (salary negotiations) are not refundable. A non-vested member that enters a reciprocal retirement system after terminating employment with MCERA may wish to arrange for reciprocal benefits. Under a reciprocal arrangement the member funds are kept on deposit with MCERA.

(8) *Vesting*

Active members of the System receive a 100% vested interest in the Plan after five years of service, but cannot receive a service retirement benefit until they have been a member of the System for ten years and obtained age fifty for Tier I General members, Tier I and Tier II Safety members, and age fifty-five for Tier II General members.

Safety members may receive a service retirement benefit after being a member of the system for 20 years regardless of age.

(9) *Contribution Rates*

The County Employees Retirement Law of 1937 establishes the basic obligations for employer and member contributions to the retirement system. The actual employer and members contribution rates in effect each year are based on recommendations made by an independent actuary and adopted by the Board of Retirement.

Benefits payable by the System are financed through member contributions, employer contributions from the County, Merced Cemetery District, Superior Court, County of Merced and earnings from investments.

A. Member

MCERA members are required to contribute a percentage of their annual covered salary. The rates are set to provide a retirement amount that is equal to a fractional part of the highest year(s) salary, based on membership and tier. Contribution rates that are actuarially determined are based on a formula reflecting the member's age of entry in the System. For members integrated with Social Security, the contributions are reduced by 1/3 of such contribution payable with respect to the first $350 of monthly salary.

B. County

The County and participating employers are required by statute to contribute the amounts necessary to finance the estimated benefits accruing to MCERA members not otherwise funded by employee contributions or investment earnings. Pursuant to provisions of the 1937 Act, the Retirement Board recommends annual contributions rates for adoption by the County Board of Supervisors each year based upon the rates recommended by the System's actuary.

(10) *Post Retirement Health Care*

The County currently provides a health care plan for both active members and eligible retirees. In order to qualify for post-retirement health care coverage under the County program, an individual receiving a regular service retirement benefit or an individual receiving a non-service connected disability retirement benefit must have a minimum of ten years of service under MCERA. There is no minimum service requirement for individuals receiving a service connected disability benefit. Under the County program, retirees pay a percentage of their health insurance premium and 100% of the premium for any dependents. In December 2001, the County implemented a "Service Year Rate Structure Plan" for determining the amount the County would pay toward an eligible retiree's health insurance premium. Under the "Service Year Rate Structure Plan," the individual's years of service are utilized as the basis for determining the level of subsidy to be provided by the County. Retiree health and dental benefits are not vested and the continued availability of such benefits is not guaranteed. The County reserves the right to amend or terminate the program at any time, as permitted by law.

In the 2002-2003 fiscal year, MCERA adopted an Internal Revenue Code (IRC) Section 401(h) Plan to serve as the vehicle for providing financial support from MCERA for retiree health insurance costs. Pursuant to the provisions of the 1937 Act and the IRC, the Retirement Board will make an annual determination of MCERA's ability to provide financial assistance to defray such costs. The decision to provide financial support, or the level of such support, will be in the sole discretion of the Retirement Board, and among other things, will be contingent on the availability of surplus excess investment earnings to offset any employer contributions used to provide funding for the IRC Section 401(h) Plan. Payments from the IRC Section 401(h) Plan began with the 2003-2004 fiscal year.

Retirees have no vested right to receive such financial support from the IRC Section 401(h) Plan or any other MCERA reserve, and the availability of such support is not guaranteed. MCERA reserves the right to alter the level of financial support, to alter the method by which it provides such support, or to terminate such support, as permitted by law.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

While the System is governed by the Board of Retirement and is considered an independent entity, it is a component unit of the County in accordance with GASB Statement No. 14 of the Government Accounting Standards Board.

B. Basis of Accounting

MCERA's financial statements are prepared on an accrual basis of accounting, which recognizes income when earned, and expenses when the obligation is incurred. Employer and employee contributions are recognized when due, pursuant to formal commitments as well as statutory or contractual requirements. Investment income is recognized as revenue when earned. Retirement benefits and refunds are recognized when due and payable in accordance with the terms of the plan. Other expenses are recognized when the corresponding liabilities are incurred. The net appreciation (depreciation) in fair value of investments held by MCERA is recorded as an increase (decrease) to investment income based on the valuation of investments.

C. Methods Used to Value Investments

Investments are reported at fair value in the accompanying Statement of Plan Net Assets based upon the closing sale prices reported on recognized securities exchanges on the last business day of the period. For listed securities having no reported sales and for unlisted securities, fair value is based upon last reported sales price. Cash deposited in the Merced County Treasurer's pool is stated at fair value. The value of the System's pool shares is determined on an amortized cost basis, which may be different than fair value. The fair value of the real estate investment holdings has been determined using industry standard appraisal techniques and assumptions. The real estate portfolio managers use appraisals, which are updated annually, to determine the fair value of these holdings.

D. Management's Estimates

The preparation of basic financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

E. Securities Transactions and Related Investment Income

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.

F. Capital Assets

Capital assets are carried at cost, net of accumulated depreciation. Capital assets with an initial cost of more than $2,500 and an estimated useful life in excess of one year are depreciated. Depreciation is calculated using the straight-line method over the estimated useful lives of the depreciable assets. Equipment and furniture are depreciated over eight years.

G. New Pronouncement

For the fiscal year ended June 30, 2006, MCERA implemented GASB Statement No. 44, *Economic Condition Reporting:* The Statistical Section - An Amendment of NCGA Statement 1. This statement establishes and modifies requirements related to the supplementary information presented in the statistical section that accompanies the basic financial statements.

H. Reclassification of Financial Statement Presentation

Certain reclassifications have been made to the 2005 financial statements to conform with the 2006 financial statement presentation. Such reclassifications had no effect on net increase in net plan assets as previously reported.

3. CASH AND INVESTMENTS

A. Investment Stewardship

The Board of Retirement has exclusive control over all investments of the System and is responsible for establishing investment objectives, strategies and policies. Pursuant to the California Constitution and California Government Code Sections 31594 and 31595, the Retirement Board is authorized to invest in any investment the Board deems prudent.

The Board of Retirement has adopted an Investment Policy, which provides the framework for the management of MCERA's investments. The Investment Policy establishes MCERA's investment objectives and defines the principal duties of the Retirement Board, the custodian bank 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. MCERA currently employs external investment managers to manage its assets subject to the provisions of the Investment Policy.

B. Cash and Short-Term Investments

Cash and cash equivalents consist of short-term investments held by the County Treasurer and MCERA's custodian bank, the Bank of New York. Cash and cash equivalents are highly liquid investments with a short maturity. Cash and cash equivalents are recorded at cost, which approximates fair value.

(1) *County Treasury*

Cash from deposits and the cash needed for daily operational purposes is held in a pooled account with other County funds. The County Treasury Oversight Committee is responsible for regulatory oversight of the pool. 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. The fair value of the System's cash invested with the County Treasurer totaled $8,569,708 and $4,064,191 at June 30, 2006 and 2005 respectively. Cash and investments included within the County Treasurer's pool is described in the County's Comprehensive Annual Financial Report.

(2) *Short-Term Investment Funds*

The short-term investment funds that are in the custody of Bank of New York are liquidity funds. The cash is invested in short-term obligations and deposits, including U.S. treasury and agency obligations, corporate bonds, commercial paper, repurchase agreements, certificates of deposit, banker's acceptances, time deposits and floating-rate notes. All participants in the pool proportionately share earnings and losses. Deposits in the pooled accounts approximate fair value. At June 30, 2006 and 2005, short-term investment balances were $7,725,097 and $11,644,169, respectively, which are held in the System's name and are not insured. The System is not exposed to custodial credit risk with respect to these deposits.

C. Credit Concentration

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. As of June 30, 2006, the System had no single issuer that exceeds 5% of total investments. Investments issued or explicitly guaranteed by the U.S government and investments in mutual fund, external investment pools, and other pooled investments are excluded. MCERA's investment policy does not allow for an investment in any one issuer that is in excess of 5% of the value of a portfolio and no single industry (based on North American Industry Classification System (NAICS) codes) can represent more than 15% of the market value of the account. These single security and single industry restrictions do not apply to U.S. Government issued or guaranteed investments, investments in mutual funds, external investment pools and other pooled investments.

D. Credit Risk

Credit risk is the risk that an issuer or other counterparty to a debt instrument will not fulfill its obligation as described by nationally recognized statistical rating organizations—rating agencies— as of the date of the financial statements. An investment grade security is defined as a security which has been rated investment grade (BBB or higher) by at least one (but preferably two) of the three nationally recognized rating agencies; Fitch Ratings, Moody's Investor Service, and Standard & Poor's. MCERA requires that no more that 5% of an investment's managers fixed income portfolio may be invested in below investment grade rated securities (BB or B rated bonds). No security rated below single B may be purchased at any time. Securities that have at least a single B but subsequently fall below single B ratings, shall be sold in an orderly manner. The County's pool and the short-term investment funds held with fiscal agent are unrated.

E. Custodial Credit Risk

The custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. As of June 30, 2006 and 2005, 100% of the System's investments were held in the system's name, and the System is not exposed to custodial credit risk related to these investments.

MCERA's cash and investments stated at fair value as of June 30, 2006 and 2005 are presented as follows:

Cash Equivalents	Fair Value	
	2006	2005
Funds Pooled with County	$ 8,569,708	$ 4,064,191
Short-Term Investment Funds held with Fiscal Agents	7,725,097	11,644,169
Total Cash Equivalents	16,294,805	15,708,360
Investments		
U.S. Government & Agency Bonds	58,210,041	70,123,894
Domestic Fixed Income	60,497,695	60,072,558
Domestic Stocks	188,036,203	169,817,224
Total	306,743,939	300,013,676
Investments		
Real Estate	31,687,368	28,607,565
Alternative Investments	3,163,227	1,131,242
Domestic Stocks-Commingled Fund	50,564,107	45,973,407
International Stocks-Commingled Fund	43,947,332	35,024,262
Total	129,362,034	110,736,476
TOTAL CASH EQUIVALENTS & INVESTMENTS	$ 452,400,778	$ 426,458,512

F. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. MCERA's Investment Policy Statement does not have a formal policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. However, MCERA's bond portfolios are managed duration neutral to their benchmark, the Lehman Brothers Aggregate Bond Index. As of June 30, 2006 and 2005 the County's pool has a fair value of $560,891,522 and $513,398,733 respectively and a weighted average maturity of 343 days for June 30, 2006 and 340 days for June 30, 2005. The weighted average maturity of the short-term investment funds with fiscal agent were not available as of June 30, 2006.

As of June 30, 2006 and 2005 MCERA had the following fixed income investments:

Investment Type	Fair Value 2006	Weight of Total Fixed Income 2006	Effective Duration 2006	Fair Value 2005	Weight of Total Fixed Income 2005	Effective Duration 2005
U.S. Treasuries	$ 20,720,307	17.45%	5.86	$ 18,817,968	14.45%	5.60
U.S. Agencies	22,101,663	18.62%	4.29	59,205,854	45.47%	5.86
Asset Backed Securities	49,106,347	41.37%	4.27	8,203,325	6.31%	4.77
Corporate Bonds	14,027,679	11.82%	6.44	41,912,654	32.19%	7.03
Municipal Bonds	3,803,982	3.20%	2.94	530,163	.41%	7.08
Other Government-GNMAs	7,709,184	6.49%	2.34	1,526,488	1.17%	4.67
Short-Term Bills/Notes	1,238,574	1.05%	.39	-	-	-
Total Fair Value	$ 118,707,736	100.00%		$ 130,196,452	100.00%	
Portfolio Effective Duration			4.76			6.13

2006

Quality	Percentage of Total Fixed Income
AAA	77.26%
AA	3.06%
A	9.42%
BBB	9.93%
BB	0.33%
	100.0%

2005

Quality	Percentage of Total Fixed Income
AAA	76.7%
AA	4.2%
A	8.6%
BAA	10.2%
BA	0.3%
	100.0%

G. Derivatives

MCERA'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 system does not use derivatives for speculative use or to create leverage. Derivatives permitted by MCERA's investment policy are financial futures (if exchange traded), currency forward contracts and currency options (exchange and OTC traded) and also derivative instruments with allocation limits which include; interest only mortgage collateralized mortgage obligations, principal only mortgage (CMOs), interest rate swaps, options (if exchange traded), caps and floors as they apply to the above stated allowable derivative investments. The investments in futures contracts bear credit risk in that parties to the contracts may fail to perform according to the terms of the contract. Also, the investments may be subject to market risk due to a change in the price of the underlying securities. The investments in CMOs may be subject to credit risks, such as the credit quality rating of the underlying security may be downgraded by rating organizations and the mortgages can be prepaid. CMOs also bear market risk, as the market may be sensitive to interest rate fluctuations. Floating-rate investments are investments with interest payments that float or adjust periodically based upon a predetermined benchmark. While the market value of a floating-rate security is relatively insensitive to changes in interest rates, the income received is highly dependent upon the level of the reference rate over the life of the investment. Total return may be less than anticipated if future interest rate expectations are not met. As with any fixed income investment, there is a risk that the issuer will be unable to meet its payment obligations.

A summary of the various derivative instruments as of June 30, 2006 is as follows:

Schedule of Derivatives
For the Years Ended June 30, 2006 and 2005

Type of Derivatives	Fair Market Value 2006	Fair Market Value 2005
Collateralized Mortgage Obligations	$ 14,458,455	$ 24,078,125
Floating –Rate Notes	$ 4,667,048	$ 7,199,135

H. Foreign Currency

Foreign currency risk is the risk that changes in exchange rate will adversely affect the fair value of an investment or a deposit. The following table represent securities held in a foreign currency as of June 30, 2006.

Local Currency Name	Private Equity
Euro Currency	$ 61,766

4. RESERVES

As required by the County Employees Retirement Law of 1937 or the Board of Retirement's policy, the following reserves for Net Assets in Trust for Pension Benefits and post employment healthcare benefits have been established to account for the members, employers, and retirees' contributions. Reserve balances at June 30, 2006 and 2005 respectively, are as follows:

A. Active Members' Reserves $ 54,825,607

These reserves represent the cumulative contributions made by active employees. Additions include member contributions and related earnings: Deductions include refunds of member contributions and, upon retirement, the member contributions plus interest credited to their account are transferred from this reserve to the Retired Members' Reserves.

B. Employer Advance Reserves $ 66,763,872

These reserves represent the cumulative contributions made by the County for future retirement payments to current active members. Additions include contributions from the employer and related earnings; deductions include transfers to the Retired Member Reserve, and lump sum death benefits.

C. Retired Members' Reserves $ 230,191,661

These reserves are established upon the retirement of an employee. Employee contributions plus interest earnings credited to the employee account are transferred from the Active Member Reserves to the Retired Members' Reserves. In addition, the present value of the actuarially determined pension benefits is also transferred from the Employer Advance Reserves to the Retired Members' Reserves. From these reserves, the System pays the retiree pension benefits in an amount computed in accordance with the 1937 Act.

D. Interest Fluctuation Reserve $ 0.00,

Prior to June 30, 2003, the Interest Fluctuation Reserve served as both the interest crediting account and the contingency reserve. Effective June 30, 2003, a separate Contingency Reserve was created and the Interest Fluctuation Reserve is used for interest crediting purposes and for holding any funds allocated by the Retirement Board as a reserve for future interest earnings deficiencies.

E. Medical Insurance Trust $ 0.00

This account was established in 1984 as a reserve to assist with the System's discretionary financial assistance for retiree health insurance costs. Over time, the account has been funded with surplus/excess investment earnings. In 2003, in accordance with the provisions of the 1937 Act and the Internal Revenue Code (IRC), MCERA established an IRC Section 401(h) Plan which now serves as the vehicle for any MCERA support for retiree health insurance costs. By resolution, in May 2006, the Retirement Board directed that the balance in the Medical Insurance Trust be directed to offset Merced County's contribution in an equal amount into the 401(h) account and that the Medical Insurance Trust be terminated. Retirees have no vested right to financial support for such costs from the IRC Section 401(h) Plan or otherwise, and the availability of such support is not guaranteed. The amount of such support, if any, will be determined annually in the sole discretion of the Retirement Board.

F. Market Value Fluctuation Reserve $ 69,662,223

The Board of Retirement established this "designation" account on June 30, 1997 to track the increase (or decrease) in the market value of System assets. The annual change in market value of MCERA's assets is as follows:

Accumulated thru 2003	2004	2005	2006	TOTAL
$ 13,293,506	$32,699,563	$20,076,440	$3,592,713	$69,662,223

G. Ad-Hoc COLA Reserve $ 1,568,795

This reserve was established in 1999 as the source of funds for an ad-hoc COLA granted to certain retirees and beneficiaries pursuant to Section 31874.3(b) of the 1937 Act. Eligibility for the COLA was limited to retirees with accumulated uncredited COLAs totaling 25 percentage points or more as of April 1, 1999.

H. Contingency Reserve $ 18,194,769

Prior to the fiscal year ending June 30, 2003, the Interest Fluctuation Reserve was also used as MCERA's contingency reserve. Effective June 30, 2003 the contingency reserve function will be carried out through a separate account called the Contingency Reserve. The Contingency Reserve is comprised of surplus/excess earnings that are held as a reserve against deficiencies in investment earnings in other years, losses on investments and other contingencies.

I. Internal Revenue Code (IRC) Section 401(h) $4,689,794

MCERA adopted and implemented an Internal Revenue Code (IRC) Section 401(h) Plan to serve as the vehicle for providing financial support for retiree health care costs.

Multi-Year Reserve Balances

	2006	2005	2004	2003	2002	2001
Active Member Reserves	$ 54,825,607	$ 49,161,941	$ 48,707,821	$ 48,378,964	$ 50,940,716	$ 49,481,396
Employer Advance Reserves	$ 66,763,872	$ 73,309,666	$ 86,260,253	$ 91,368,990	$ 108,864,811	$ 109,324,461
Retired Member Reserves	$ 230,191,661	$ 219,322,395	$ 204,267,473	$ 198,758,208	$ 187,694,191	$ 183,519,659
Interest Fluctuation Reserve	$ -	$ -	$ -	$ -	$ -	$ 7,794,732
Medical Insurance Trust	$ -	$ 2,610,752	$ 5,301,792	$ 7,519,329	$ 9,783,076	$ 10,633,788
Market Fluctuation Reserve	$ 69,662,223	$ 66,069,509	$ 45,993,069	$ 13,293,506	$ (2,495,045)	$ 22,300,377
Ad-Hoc Reserve	$ 1,568,795	$ 1,553,240	$ 1,544,447	$ 1,541,975	$ 1,600,748	$ 1,595,651
Contingency Reserve	$ 18,194,769	$ 4,327,952	$ 3,967,837	$ 3,645,060	$ -	$ -
Litigation Reserve	$ -	$ -	$ -	$ -	$ 1,008,577	$ 966,163
IRC Section 401(h)	4,689,794	2,790,999	740,999	-	-	-
Facility/System Reserve	$ -	$ -	$ -	$ -	$ 317,423	$ 304,074

5. INVESTMENT EXPENSES

Investment expenses include fees paid for investment consulting services, fund evaluation services, securities custodian services, and rebate and bank fees incurred during the reporting period. Fees paid are charged against the System's investment earnings pursuant to Sections 31596.1 of the 1937 Act.

6. GENERAL ADMINISTRATIVE EXPENSES

Effective January 1, 2004, Section 31580.3 was added to the 1937 Act to provide more flexibility in establishing the administrative cost limit. Under Section 31580.3 the alternative administrative cost ceiling may not exceed .23% of the total asset value of the retirement system as of the selected valuation date. The MCERA Board of Retirement adopted Section 31580.3 on September 9, 2004 for determining the administrative cost ceiling for the fiscal years ended June 30, 2004 and 2005. Section 31580.3 is set to expire January 2007 and due to an improved investment market, for the current fiscal year, MCERA has calculated its administrative costs pursuant to Government Code Section 31580.2, which provides that the cost ceiling may not exceed .18%. MCERA's administrative expenses in the current fiscal year totaled .14%.

7. LITIGATION

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

8. REQUIRED SUPPLEMENTARY INFORMATION

A schedule of the MCERA's funding progress that reports the actuarial value of assets, the actuarial accrued liability, and the relationship between the two over time and a schedule of employer contributions that provides information about the annual required contributions of the employer's Annual Required Contribution (ARC) and the percentage of the ARC recognized by the plan are presented, where available, on the following pages as Required Supplementary Information.

9. ADMINISTRATIVE BUDGET AND PROFESSIONAL SERVICES BUDGET

MCERA's budget consists of two components, an administrative budget authorized by Government Code §31580.2 and a professional services budget authorized by Government code §31596.1. MCERA's budgets are on a fiscal year basis starting July 1st and ending June 30.

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

REQUIRED SUPPLEMENTARY SCHEDULES

Schedule of Funding Progress

(Dollar amounts in thousands)

Actuarial Valuation Date	Actuarial Value of Assets* (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL As a Percent of Covered Payroll (b-a/c)
7/1/99	$ 354,467	$ 351,252	$ (3,215)	100.9%	$ 62,521	(5.1)%
7/1/01	$ 411,710	$ 404,316	$ (7,394)	101.8%	$ 76,015	(9.7)%
7/1/02	$ 424,613	$ 421,435	$ (3,178)	100.8%	$ 83,001	(3.8)%
7/1/03	$ 428,959	$ 451,181	$ 22,222	95.1%	$ 88,586	25.1%
7/1/04	$ 430,054	$ 531,938	$ 101,884	80.8%	$89,516	113.8%
7/1/05	$ 428,813	$ 589,794	$ 160,981	72.7%	$97,507	165.1%

* Excludes "Other Designated Reserves" and the liabilities associated with these reserves

Note: This information is compiled from MCERA's actuarial report prepared by Buck Consultants dated June 30, 2005. MCERA had no actuarial valuation prepared for the fiscal year ended 07/01/00.

Schedule of Employer Contributions
Pension Benefit Plan

(Dollar amounts in thousands)

Year Ended	Annual Required Contribution	Percentage Contributed
6/30/00	$ 6,259	100%
6/30/01	$ 6,927	100%
6/30/02	$ 7,731	100%
6/30/03	$ 7,201	100%
6/30/04	$ 7,269	100%
6/30/05	$ 8,931	100%

Note: This information is compiled from MCERA's actuarial report prepared by Buck Consultants dated June 30, 2005.

NOTES TO REQUIRED SUPPLEMENTARY SCHEDULES
June 30, 2006

1. GASB STATEMENTS 25

MCERA applied the parameters established by Governmental Accounting Standards Board (GASB) Statement 25 in calculating and presenting the required actuarially determined information in the Schedule of Funding Progress and the Schedule of Employer Contributions.

2. FUNDING STATUS

Viewed in isolation, the dollar amounts of a retirement system's net assets, actuarial accrued liability (AAL) and unfunded actuarial accrued liability (UAAL), as reflected in the Schedule of Funding Progress, can be misleading when assessing the retirement system's funding status. Expressing the plan's net assets as a percentage of the AAL, however, provides one indication of the retirement system's funding status on a going concern basis. Analysis of this percentage (the Funded Ratio) over time will indicate whether the retirement system is becoming financially stronger or weaker. Generally, the higher the Funded Ratio, the stronger the retirement system.

Trends in the UAAL and the annual covered payroll are both affected by inflation. Expressing the UAAL as a percentage of covered payroll adjusted for the effects of inflation will also aid analysis of the retirement system's progress in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the stronger the retirement system.

3. ACTUARIAL ASSUMPTIONS

The information presented in the Schedule of Funding Progress and the Schedule of Employer Contributions was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation is as follows:

Valuation Date	June 30, 2005
Actuarial Cost Method	Entry Age Normal Actuarial Cost Method
Amortization Method	Level percentage - Closed
Remaining Amortization Period	19 years from June 30, 2005
Asset Valuation Method	Five year smoothed market

NOTES TO REQUIRED SUPPLEMENTARY SCHEDULES
June 30, 2006
(Continued)

Actuarial Assumptions

Investment Rate of Return	8.0%
Projected Salary Increases	5.5%
Assumed Inflation Rate	4.5%
Assumed Post-employment Benefit Increase	Up to 3% for Tier I members only

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

OTHER SUPPLEMENTARY SCHEDULES
ADMINISTRATIVE EXPENSES

For the years ended June 30, 2006 and 2005

	2006	2005
Personnel Services:		
Salaries, Wages and Benefits	**$ 414,611**	**$ 309,139**
Office Expenses:		
Communications	2,033	1,816
Requested Maintenance/Utilities/Cost Allocation	18,559	51,260
Office Supplies	9,397	5,310
Postage	4,886	4,286
Total Office Expense	**34,875**	**62,672**
Professional Services:		
Audit Fees	20,322	13,803
Attorney Fees	36,096	31,537
Disability Stenographic Fees/Investigations	2,310	1,860
Publications & Legal Notices	1,025	27,234
Disability Medical Reviews/Services	22,826	27,483
Merced Dept of Information Technology	31,314	25,375
Total Professional Services	**113,893**	**127,292**
Miscellaneous:		
Memberships	2,305	1,926
Fiduciary Meetings	5,500	9,000
Fiduciary and Staff Travel/Training	20,516	16,937
Insurance Liability/Other	48,925	66,988
Software/Other Expense	-	614
Depreciation Expense	8,455	7,883
Total Miscellaneous Expenses	**85,701**	**103,348**
Total Administrative Expenses	**$ 649,080**	**$ 602,451**

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

OTHER SUPPLEMENTARY SCHEDULES

SCHEDULE OF INVESTMENT EXPENSES

For the years ended June 30, 2006 and 2005

INVESTMENT MANAGERS	2006	2005
UBS Real Estate Separate Account (RESA)	$ 340,961	$ 304,270
Delta Asset Mgmt	279,318	265,656
Earnest Partners, LLC	199,024	184,812
Wasatch Advisors	230,131	204,711
Mellon Capital Mgmt	19,813	25,081
Wentworth, Hauser, & Violich	243,861	186,826
Invesco Global Asset Mgmt	272,891	234,479
Aberdeen Asset Mgmt/Deutsche Asset Mgmt	208,052	222,992
Lehman Brothers Asset Mgmt/Lincoln Capital Mgmt	72,837	45,547
Invesco Private Capital	90,000	165,847
Adams Street Partners, LLC	-	2,917
Pantheon Ventures, Inc,	-	20,776
GLOBAL CUSTODIAN		
Bank of New York	140,489	125,357
TOTAL PROFESSIONAL EXPENSE	2,097,377	1,989,271
CONSULTANT EXPENSE	144,896	135,950
BROKERAGE COMMISSIONS & FEES	220,558	163,773
OTHER INVESTMENT EXPENSE	550	2,280
TOTAL INVESTMENT MANAGER FEES, AND OTHER INVESTMENT EXPENSES	$ 2,463,381	$ 2,291,274

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

OTHER SUPPLEMENTARY SCHEDULES

SCHEDULE OF PAYMENTS TO CONSULTANTS

For the years ended June 30, 2006 and 2005

INVESTMENT PROFESSIONAL SERVICE FEES	2006	2005
ACTUARIAL SERVICES		
Buck Consultants/Mellon Human Resources & Investor Solutions	$ 48,438	$ 61,951
INVESTMENT CONSULTANT		
Milliman USA	144,896	135,950
CUSTODIAL SERVICES		
Bank of New York Western Trust Company	140,489	125,357
TOTAL INVESTMENT PROFESSIONAL SERVICE FEES	$ 333,823	$ 323,258

ADMINISTRATIVE PROFESSIONAL SERVICE FEES		
AUDIT SERVICES		
Brown Armstrong Paulden McCown Starbuck & Keeter	$ 20,322	$ 13,803
LEGAL SERVICES		
Mason, Robbins, Gnass & Browning-Disability Attorney	36,096	31,537
DISABILITY STENOGRAPHIC FEES/ INVESTIGATIONS	1,918	1,860
DISABILITY MEDICAL REVIEWS/SERVICES	22,826	27,483
MERCED DEPT. OF INFORMATION TECHNOLOGY	31,314	25,375
OTHER SPECIALIZED SERVICES	1,493	29,514
TOTAL ADMINISTRATIVE PROFESSIONAL SERVICE FEES	$ 113,969	$ 129,572

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

OTHER SUPPLEMENTARY SCHEDULES

Budget Analysis
Budget to Actual Expenditure
For the year ended June 30, 2006

Administrative Services Budget	Budgeted Amounts	Actual Amounts Expended	Percentage of Appropriation Expended
Salaries, Wages and Benefits	$ 473,467	$ 414,611	87.6%
Communications	3,000	2,033	67.8%
Requested Maintenance/Utilities/Cost Allocation	29,120	18,559	63.7%
Office Supplies	13,050	9,397	72.0%
Postage	5,000	4,886	97.7%
Audit Fees	26,500	20,322	76.7%
Attorney Fees	60,000	36,096	60.2%
Disability Stenographic Fees/Investigations	4,000	2,310	57.8%
Publications & Legal Notices	10,300	1,025	10.0%
Disability Medical Reviews/Services	65,000	22,826	35.1%
Merced Dept. of Information and Technology	66,777	31,314	46.9%
Memberships	2,350	2,305	98.1%
Fiduciary Meeting	9,000	5,500	61.1%
Fiduciary and Staff Travel/Training	36,614	20,516	56.0%
Insurance Liability/Other	97,750	93,925	96.1%
Software/Other Expense	75,500	-	0.0%
Capital Expense/Depreciation Expense	12,000	8,455	70.5%
Total Administrative Budget	**989,428**	**694,080**	**70.1%**
Professional Services Budget			
Investment Manager, Custodial Services, and Other Investment Expenses	2,360,000	2,318,485	98.3%
Actuarial Services	183,512	48,438	26.4%
Consultant Fees	160,000	144,896	91.0%
Total Professional Budget	**2,703,512**	**2,511,176**	**92.9%**
Total Budget	**$ 3,692,940**	**$ 3,205,256**	**86.8%**

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Investment section

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September 8, 2006

Ms. Maria Arevalo
Plan Administrator
Merced County Employees' Retirement Association
3199 M Street
Merced, California 95348

Dear Ms. Arevalo:

The Merced County Employees' Retirement Association had a positive investment return of 8.3% for the recently completed fiscal year ending June 30, 2006. Due to the continued rebound of the equity market and strong performance in all the other asset classes, this is the third consecutive year that the Association's fiscal year return has been above the actuarial interest rate assumption. This total fund return was also solidly above the Retirement Association's total fund benchmark return of 7.0%.

The Retirement Association's total fund return over the past five years has averaged 6.2% versus the fund benchmark[1] of 5.4% and the actuarial interest rate assumption of 8.0%. Over the past five years, the Retirement Association has fallen short of the actuarial interest rate assumption by approximately 1.8% per year. This is primarily due to the poor equity markets 4 and 5 years ago. During the last ten years, the total fund return has been 8.9% and easily exceeded the benchmark return of 5.2% and the actuarial interest rate.

Summary of Investment Objectives

The Board holds fiduciary responsibility for the Retirement Association. Given that investment performance is primarily determined by asset allocation decisions, the Board has adopted a diversified asset allocation target. This target is partially based on an analysis of the Retirement Association' liabilities and their cash flow requirements. Other factors considered in the construction of the target are an effort to maximize the return on invested assets, and an attempt to minimize risk exposures.

The primary investment objectives expected to be satisfied by the asset allocation target and investment manager structure, are:

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[1] Prior to the first quarter of 1999 the total fund benchmark was CPI + 4%/year. From 1st quarter of 1999 through 4th quarter of 2001, the benchmark is 42% S&P 500, 8% Russell 2000, 6% EAFE, 38% Lehman Aggregate, 1% 90-day T-Bill, and 5% Wilshire Real Estate Funds. In subsequent periods, the benchmark is 42% S&P 500, 8% Russell 2000, 6% EAFE, 38% Lehman Aggregate, 1% 90-day T-Bill, and 5% NCREIF Property Index. The Board has adopted a revised asset mix that also includes the Private Equity asset class. This asset class is currently being funded, and as of June 30, 2006 had an allocation to three private equity fund of funds that totaled 0.4% of total fund assets. As this commitment increases, the total fund benchmark will incorporate the new asset class.

1) At a minimum, achieve a nominal return equivalent to the Retirement Association's actuarial interest rate. Earn a total return that averages 4% to 6% in excess of the rate of inflation.
2) Exceed the return of the Retirement Association' passive, market-based, investment benchmark.

3) Achieve a total fund return ranking above the median of other public sector retirement funds. Risk-adjusted performance is expected to also be above that of the median pension fund.

In the past fiscal year, the Retirement Association successfully achieved two of these objectives, and missed the third benchmark by a small margin when it ranked in the 53rd percentile.

Market Overview

The past fiscal year had reasonably strong equity market results, except for the quarter ending June 30th, 2006. The domestic equity markets began the fiscal year with a gain of 3.6%, as measured by the S&P 500. During this third calendar quarter of 2005, eight of the ten S&P 500 sectors recorded gains and was led by Energy and Utilities. The Energy sector was up 18.6% in the quarter. In the fourth quarter of 2005, stocks continued to appreciate with a 2.1% return. Seven of the ten sectors were positive, but Energy was the worst performing sector with a -7.4% return. During the first calendar quarter of 2006, domestic equities continued their gains with a strong return of 4.2%, as based on the S&P 500. Nine of the economic sectors had positive returns and were led by Telecommunication Services and Energy (14.5% and 9.0%, respectively). Reversing the trend of the three prior quarters, the equity markets closed out the fiscal year with a loss. For the calendar quarter ending June 30, 2006, the S&P 500 fell 1.4%. Five sectors had increases, with the Utility and Energy sectors achieving the highest returns (+5.7% and +4.3%, respectively).

In line with the large cap portion of the equity markets, small cap stocks registered three consecutive quarterly gains and then a decline in the final fiscal quarter. In the third quarter of 2005, the Russell 2000 gained 4.7%. International equity also had a strong gain of 10.4%. However, domestic bond performance was weak, with the Lehman Aggregate Index down 0.7%. Real estate had a good return, with a gain of 4.4%, as measured by the NCREIF Property Index.

During the fourth quarter of 2005, all of the capital markets had gains. As stated previously, the S&P 500 returned 2.1%, the Russell 2000 1.1% and international equities returned 4.1%. Domestic bond returns were up 0.6% for the quarter, and the NCREIF Property Index returned a strong 5.4%.

The equity markets generated large gains in the fiscal year's third quarter. The S&P 500 was up 4.2% and the Russell 2000 rose 13.9%. International stocks were up 9.5%. The domestic bond market recorded another decline, with a -0.6% return, based on the Lehman Aggregate Bond Index. Real estate was up significantly during the quarter, with a return of 5.4%, based on the NCREIF Property Index.

Finally, in the second calendar quarter of 2006 (or the fourth quarter of the fiscal year) domestic equity results declined. The S&P 500 lost 1.4% and small cap stocks lost 5.0%, as represented by the Russell 2000. International stocks had a gain of 0.9%, due to foreign currency conversion into a weak dollar. Domestic bond performance continued weak with a return of -0.1%. And, finally, the real estate market achieved a strong 4.0% return.

Style Overview

As had been the case for most of the past six years, value-oriented stocks continued to strongly outperform growth-oriented securities. The Russell 1000 Value Index returned 12.1%, whereas the Russell 1000 Growth Index returned only 6.1%. Small capitalization stocks continued their out-performance of large cap stocks. The Russell 2000 returned 14.6%, versus 8.6% for the S&P 500. International stocks had much higher returns, with the MSCI EAFE Index returning 27.1%. Conversely, this was a poor year for bonds versus all stock categories, as the Lehman Aggregate had a loss of 0.8%. Real estate returns were 18.7% (based on the NCREIF Property Index) and trailed only international stocks.

Fund Overview

The total fund performance followed the overall equity market results. In the third quarter of 2005, the total Fund rose 3.5%, out-performing the total Fund benchmark of 2.5%. This gain ranked the Fund in the second quartile (37th percentile) of pension funds. With modest gains in the fourth quarter of 2005, the total Fund returned 1.5%, modestly trailing the total Fund benchmark (1.7%), and ranked in the third quartile of pension funds (67th percentile). In the calendar first quarter of 2006, the total Fund had a significant gain of 4.4%, which was better than the benchmark return of 3.5%, ranking it in the second quartile of pension funds (39th percentile). During the calendar second quarter of 2006, the total Fund loss was -1.3%, below the benchmark (-0.8%) and ranked in the third quartile of pension funds (70th percentile).

As mentioned earlier, the Retirement Association' total fund gain for fiscal year 2006 was 8.3%. This was better than the total fund benchmark return of 7.0%, ranking it in the 53rd percentile of pension funds.

Investment Results

This investment information is presented in compliance with the Performance Presentation Standards of the CFA Institute.

The Association's total domestic equity segment recorded a gain of 10.6% in fiscal year 2006, which compares favorably to the equity markets. The median domestic equity manager posted a gain of 10.3%. Within the Retirement Association's manager structure, both of the two large cap core equity managers, Earnest Partners and Delta Asset Management, trailed the median large cap core manager, primarily due to weak results in the last quarter of the fiscal year. Earnest's equity only portfolio return of 7.5%, ranked in the 80th percentile of the large cap core group, and Delta's equity only return of 8.5% ranked in the 68th percentile of the same equity style group. With a return of 12.2% and ranking in the 50th percentile of large cap value managers, the Russell 1000 Value index product managed by Mellon Capital matched the median large cap value manager and exceeded the index. Mellon Capital's Russell 1000 Growth Index product matched the median large cap growth manager and exceeded the index, ranking in the 51st percentile of large cap growth managers with an equity only gain of 6.2%.

Within the small capitalization arena, Wentworth Hauser, a small cap core portfolio manager, posted an equity only return of 23.5%, ranking in the 8th percentile. This result was materially better than the 14.6% return of the Russell 2000 Index and the 14.1% return of the median small cap core equity manager. Wentworth generated this out-performance primarily through sector selection and secondarily through stock selection. Wasatch Advisors, the Association's small cap growth manager, had an equity only return of 4.3%, ranking in the 91st percentile of small cap growth managers. Wasatch significantly under-performed the Russell 2000 Growth Index return of 14.6% and the 14.6% return of the median small cap growth equity manager. Stock selection and sector allocation decisions were both responsible for under-performance of the benchmarks. This manager has been placed on the watch list for possible removal.

The international equity segment of the Retirement Association's total Fund had a gain of 25.5% for fiscal year 2006, less than the 27.1% return of the MSCI EAFE Index. Invesco Global Asset Management ranked in the 68th percentile of international equity managers. Under-performance of the benchmark is due to a lower risk profile and no exposure to small capitalization securities. Improved results are expected and were demonstrated in the quarter ending June 30, 2006.

The domestic fixed income segment return of -0.6% out-performed the Lehman Aggregate Bond Index return of -0.8% for the past fiscal year. Fiscal year performance for the Aberdeen Asset Management portfolio was -0.3%, better than the Lehman Aggregate benchmark. This portfolio ranked in the 68th percentile of fixed income managers. The Lehman Asset Management account marginally trailed the benchmark return, ranking in the 88th percentile, with a return of –0.9%.

The UBS Brinson real estate account returned 15.7%, under-performing the benchmark NCREIF Property Index return of 18.7%. The UBS Brinson real estate fund ranked in the 73rd percentile of real estate managers during the past fiscal year.

Similar to last year, trading costs associated with the Retirement Association' domestic equity managers were reviewed to ensure that commission costs were reasonable and execution costs appropriate. Overall commission and price penalty costs were stable, which indicates that effective trading is being practiced. Additionally, the commission recapture program is being implemented through a number of brokerage firms. A significant percentage of equity trading is being executed through the program at a low cost, resulting in meaningful cost recapture.

Asset Allocation

The Retirement Association's total fund ended the fiscal year with all asset segments within their allocation target ranges. As mentioned above, the allocation to private equity is growing and there will be further commitments. The domestic equity, international equity, real estate and cash asset classes are marginally above target levels. Conversely, domestic fixed income and private equity are below target levels.

Performance Comparison

The last page of our letter provides a table comparing the Retirement Association's total fund returns to all pension funds. The vertical bands represent the range of fund performance with the blue band representing the 25th percentile at the top and 75th percentile at bottom. The solid black line represents the median fund's performance. As the graph illustrates, the fund ranked above the benchmark in every period during the past ten years, except last quarter. Additionally, the Retirement Association out-performed the median fund return in every time frame except for the past quarter and one-year periods. In these periods, the Association ranked in the 70th and 53rd percentiles.

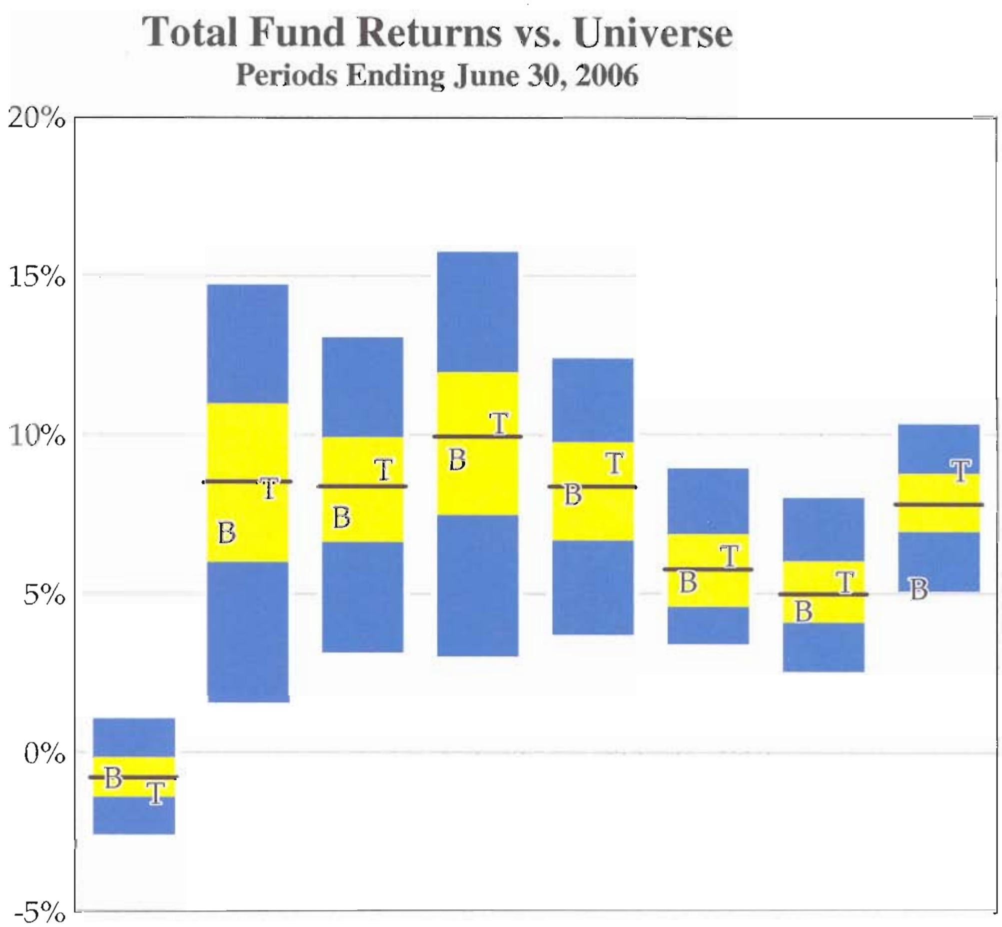
Summary

In conclusion, the fund experienced another good fiscal year with a gain of 8.3%. This was better than the custom benchmark return of 7.0% and above the Retirement Association's actuarial interest rate assumption. The combination of the Retirement Association's domestic equity investment managers produced a return above their benchmarks. The fixed income managers in total exceeded their benchmarks. However, the real estate and international equity managers under-performed their benchmarks, and the domestic small cap growth manager under-performed its benchmark. These situations continue to be closely monitored. Therefore, with a few exceptions, the managers are producing returns in line with or above their benchmarks. At all times, the Fund was managed in accordance with the Retirement Association's policies.

Sincerely,

William R. Cottle

William R. Cottle, CFA



	Last Quarter	Last 1 Yr	Last 2 Yrs	Last 3 Yrs	Last 4 Yrs	Last 5 Yrs	Last 7 Yrs	Last 10 Yrs
Total Fund Universe								
5th Percentile	1.1	14.7	13.1	15.8	12.4	8.9	8.0	10.3
25th Percentile	-0.2	11.0	9.9	12.0	9.8	6.8	6.0	8.8
Median	-0.8	8.5	8.4	9.9	8.4	5.7	5.0	7.8
75th Percentile	-1.4	6.0	6.6	7.5	6.7	4.6	4.1	6.9
95th Percentile	-2.6	1.6	3.2	3.0	3.7	3.4	2.5	5.1
Total Fund (T)	-1.3	8.3	8.9	10.4	9.1	6.2	5.4	8.9
Rank	*70*	*53*	*40*	*44*	*37*	*38*	*39*	*22*
Fund Benchmark (B)	-0.8	7.0	7.4	9.3	8.2	5.4	4.5	5.2
Rank	*49*	*67*	*63*	*57*	*53*	*59*	*62*	*94*

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

OUTLINE OF INVESTMENT POLICIES AND SUMMARY OF PROXY VOTING GUIDELINES AND PROCEDURES

For the Year Ended June 30, 2006

Outline of Investment Policies

The Board of Retirement has exclusive control of all investments of the retirement system and is responsible for establishing investment objectives, strategies and policies.

Pursuant to the California Constitution and the 1937 Act, the Board is authorized to invest in any form or type of investment deemed prudent in the informed judgment of the Board. In making decisions regarding the MCERA investment portfolio, the Board acts in a fiduciary capacity and must discharge its duties in accordance with fiduciary principles. In this regard, investment decisions are to be made in the sole interest and for the exclusive purpose of providing benefits, minimizing employer contributions and defraying the reasonable expenses of the retirement system.

The Board of Retirement has adopted an Investment Policy, which provides the framework for the management of MCERA's investments. The Investment Policy establishes the investment program goals, asset allocation policies, performance objectives, investment management policies and risk controls. The Investment Policy also defines the principal duties of the Board, MCERA's custodian bank and MCERA's investment managers. The Board makes revisions to the Investment Policy as necessary.

Pursuant to the Investment Policy, the basic goal of MCERA's investment program is to obtain a fully funded plan status, while assuming a risk posture consistent with the Board's risk tolerance. In pursuing this goal, the Board has adopted a long-term investment horizon in which the chances and duration of investment losses are carefully weighed against the long-term potential for appreciation of assets. The primary investment objective is to exceed the actuarial assumption for return on assets. The risk assumed in the pursuit of this investment objective must be appropriate for the return anticipated and consistent with the total diversification of the fund.

The asset allocation plan adopted by the Board is an integral part of MCERA's investment program. It is designed to provide an optimum, diversified mix of asset classes with return expectations to satisfy expected liabilities, while minimizing risk exposure.

Summary of Proxy Voting Guidelines and Procedures

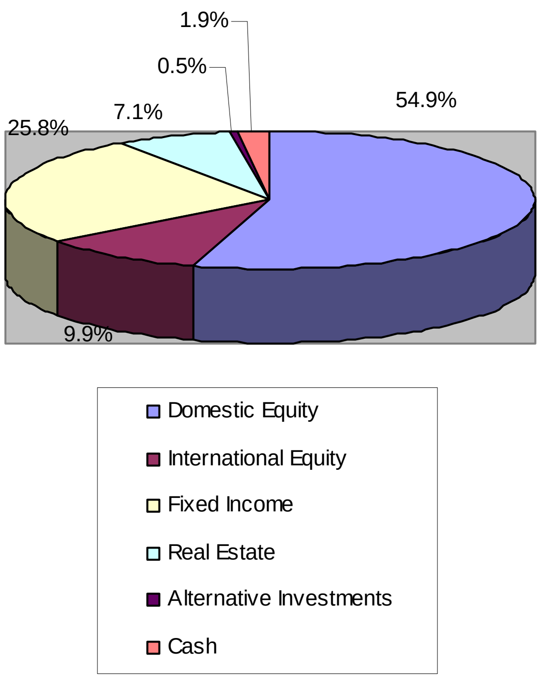
Voting of MCERA's proxy voting ballots shall be in accordance with MCERA's proxy voting guidelines as set forth in the Investment Policy. The basic directive of the proxy voting guidelines is that when voting proxy ballots on behalf of MCERA, investment managers shall vote according to the best interests of the MCERA membership. On a quarterly basis, the investment managers are required to provide a report to MCERA detailing their proxy votes.

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

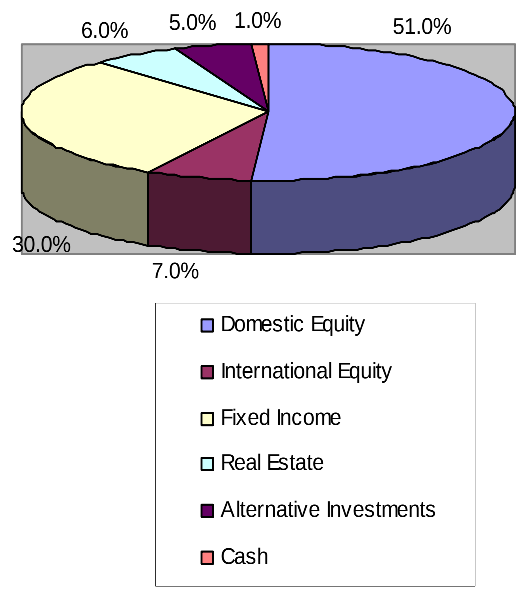
ASSET ALLOCATION INFORMATION

For the Year Ending June 30, 2006

JUNE 30, 2005 ALLOCATION



TARGET ALLOCATION



	June 30, 2006 Asset Allocation	Target Allocation Adopted August 18, 2003	Allocation Range	
Domestic Equity	54.9%	51.0%	+ / -	10%
International Equity	9.9%	7.0%	+ / -	4%
Fixed Income	25.8%	30.0%	+ / -	6%
Real Estate	7.1%	6.0%	+ / -	4%
Alternative Investments	0.5%	5.0%	+ / -	2.5%
Cash	1.9%	1.0%	+ / -	1%
	100.0%	100.0%		

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

INVESTMENT SUMMARY

For the Year Ending June 30, 2006

	MARKET VALUE	% OF TOTAL
DOMESTIC EQUITY:		
Large Cap Growth	$ 101,056,958	22.3%
Large Cap Value	85,446,287	18.9%
Small Cap Growth	21,027,926	4.6%
Small Cap Value	31,069,139	6.9%
TOTAL DOMESTIC EQUITY	238,600,310	52.7%
INTERNATIONAL EQUITY	43,947,332	9.7%
FIXED INCOME	118,707,736	26.2%
ALTERNATIVE INVESTMENTS	3,163,227	.7%
REAL ESTATE	31,687,368	7.%
TOTAL INVESTMENTS	$ 197,505,663	43.7%
CASH AND CASH EQUIVALENTS	16,294,805	3.6%
TOTAL INVESTMENTS, CASH AND CASH EQUIVALENTS	$ 452,400,778	100.0%

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

SCHEDULE OF INVESTMENT RESULTS

For the Years Ending June 30

		CURRENT	ANNUALIZED					
		YEAR	2YR	3YR	4YR	5YR	7YR	10YR
DOMESTIC EQUITY								
Large Cap Growth								
Delta Asset Mgmt.		8.3%	6.8%	11.0%	8.0%	3.1%	1.5%	9.4%
Index: S&P 500		8.6%	7.5%	11.2%	8.4%	2.5%	0.5%	8.3%
Large Cap Value								
Earnest Partners, LLC		7.4%	9.9%	13.1%	10.4%	3.8%	-	-
Index: Russell 1000		9.1%	8.5%	12.0%	9.2%	3.1%	1.2%	8.6%
Large Cap Index								
Mellon Capital Mgmt. Large Cap Growth		6.2%	3.9%	8.4%	-	-	-	-
Index: Russell 1000 Growth		6.1%	3.9%	8.4%	7.0%	-.8%	-3.6%	5.4%
Mellon Capital Mgmt. Large Cap Value		12.2%	13.1%	15.8%	-	-	-	-
Index: Russell 1000 Value		12.1%	13.1%	15.7%	11.3%	6.9%	5.0%	10.8%
Small Cap Growth								
Wasatch Advisors		4.4%	3.2%	9.5%	-	-	-	-
Index: Russell 2000 Growth		14.6%	9.3%	16.3%	12.2%	3.5%	2.2%	4.1%
Small Cap Value								
Wentworth, Hauser & Violich		22.5%	22.0%	27.5%	19.1%	16.1%	18.4%	-
Index: Russell 2000		14.6%	12.0%	18.7%	13.2%	8.5%	8.1%	9.1%
TOTAL DOMESTIC EQUITY		**10.6%**	**9.8%**	**13.7%**	**10.6%**	**4.6%**	**2.8%**	**8.6%**
INDEX: RUSSELL 3000		9.6%	8.8%	12.6%	9.5%	3.5%	1.7%	8.5%
INTERNATIONAL EQUITY								
Invesco Global Asset Mgmt		25.5%	18.8%	22.5%	13.8%	10.2%	7.3%	-
Index: MSCI EAFE		27.1%	20.4%	24.4%	16.0%	10.4%	5.8%	6.8%
FIXED INCOME								
Lehman Brothers Asset Mgmt.		-.9%	2.9%	2.0%	-	-	-	-
Aberdeen Asset Mgmt.		-.3%	3.7%	2.7%	4.9%	5.9%	-	-
TOTAL FIXED INCOME		**-.6%**	**3.3%**	**2.4%**	**4.4%**	**5.1%**	**6.1%**	**6.4%**
INDEX: LEHMAN AGGREGATE		-.8%	2.9%	2.1%	4.1%	5.0%	5.8%	6.2%
REAL ESTATE								
UBS Realty Investors LLC		15.7%	18.2%	15.8%	14.2%	11.8%	12.3%	-
Index: NCRIEF Property Index		18.7%	18.4%	15.8%	13.7%	12.0%	11.3%	11.9%
ALTERNATIVE INVESTMENTS**	**3 Mo**							
Invesco Private Capital	**0.7%**	-	-	-	-	-	-	-
Adams Street Partners, LLC	**2.5%**	-	-	-	-	-	-	-
Pantheon Ventures, Inc.	**-11.8%**	-	-	-	-	-	-	-
Total Private Equity	**-2.0%**							
TOTAL FUND*		**8.3%**	**8.9%**	**10.4%**	**9.1%**	**6.2%**	**5.4%**	**8.9%**
TOTAL FUND CUSTOM INDEX*		**7.0%**	**7.4%**	**9.3%**	**8.2%**	**5.4%**	**4.5%**	**5.2%**

*Using time-weighted rate of return based on market rate of return.
**Performance results lags by two quarters due to financial reporting constraints.

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

TOP 10 LARGEST HOLDINGS BY FAIR VALUE

For the Year ending June 30, 2006

PAR	BONDS	FAIR VALUE
3,853,000	U.S. Treasury Note 4.500% Due 02/28/2011 Cusip #912828EX4	$ 3,756,983
2,469,000	U.S. Treasury Note 4.000% Due 11/15/2012 Cusip #912828AP5	2,320,622
1,660,000	U.S Treasury Bond 6.000% Due 02/15/2026 Cusip #912810EW4	1,798,112
1,370,000	U.S. Treasury Note 3.125% Due 9/15/2008 Cusip #912828BK5	1,312,734
865,000	U.S. Treasury Bond 8.125% Due 08/15/2021 Cusip #912810EKO	1,115,106
1,030,000	U.S. Treasury Note 3.250% Due 01/15/2009 Cusip #912828BV1	984,217
1,017,000	U.S. Treasury Note 4.250% Due 11/15/2013 Cusip #912828BRO	962,418
975,000	GNMA 5.000% Due 12/16/32 Cusip #38374RFM8	900,090
855,000	GNMA 6.000% Due 06/20/2018 Cusip #38373XSN7	854,732
845,000	FNMA 30 YR 6.0000% Due 7/01/2036 Cusip #01F060675	831,533
		$ 14,836,547

SHARES	STOCKS	FAIR VALUE
94,600	GENERAL ELECTRIC CO.	$ 3,118,016
64,200	CITIGROUP, INC.	3,097,008
60,954	BANK OF AMERICA CORP.	2,931,887
46,758	EXXON MOBIL CORP.	2,868,603
95,000	MICROSOFT CORP.	2,213,500
30,100	MERRILL LYNCH & CO., INC.	2,093,756
47,644	JPMORGAN CHASE & CO.	2,001,048
78,900	CORNING INC., COM	1,908,591
31,000	DEVON ENERGY CORP. NEW	1,872,710
12,400	GOLDMAN SACHS GROUP, INC.	1,865,332
		$ 23,970,451

A complete list of the portfolio holdings is available upon request

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

SCHEDULE OF INVESTMENT FEES AND SERVICES AND OTHER PROFESSIONAL INVESTMENT SERVICE PROVIDERS

For the Years Ended June 30, 2006 and 2005

INVESTMENT MANAGERS' FEES	**2006**	**2005**
Equity Managers		
Domestic	$ 972,147	$ 867,088
International	272,891	234,479
Total equity managers' fees	1,245,038	1,101,567
Bond Managers	280,889	268,538
Alternative Investments	90,000	189,540
Real Estate	340,961	304,269
Total Other Investment Management Fees	711,850	762,347
TOTAL INVESTMENT MANAGEMENT FEES	$ 1,956,888	$ 1,863,914
OTHER INVESTMENT SERVICE FEES		
Investment Consultant Fees	$ 144,896	$ 135,950
Investment Custodial Fees	140,489	125,357
Brokerage Commissions and Fees	220,558	163,773
Other Investment Service Fees	550	2,280
Total Other Investment Service Fees	506,493	427,360
TOTAL INVESTMENT MANAGER AND OTHER SERVICE FEES	$ 2,463,381	$ 2,291,274

* Certain reclassifications have been made to the 2005 financial statements to conform with the 2006 financial statement presentations. Such reclassifications had no effect on net increase in net plan assets as previously reported.

Actuarial section

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buckconsultants
an ACS company ACS

March 27, 2006

Board of Retirement
Merced County
Employees' Retirement Association
3199 M Street
Merced, California 95348

Re: *Actuarial Certification of the Merced County Employees' Retirement Association*

Members of the Board:

Buck Consultants, LLC is the Consulting Actuary for the Merced County Employees' Retirement Association. Actuarial valuations are completed annually as of June 30 of each year. The date of the most recent actuarial valuation was June 30, 2005. In each actuarial study, we conduct an examination of all participant data for reasonableness.

Actuarial funding is based on the Entry Age Normal Cost Method. Under this method, the employer contribution rate provides for current cost (normal cost) plus a level percentage of payroll to amortize the unfunded actuarial accrued liability (UAAL). As of June 30, 2005, the remaining amortization period for the UAAL was 19 years. The funding objective of the Association is to establish contribution rates which, over time, will remain as a level percentage of payroll unless Association benefit provisions are changed and which are designed to fully fund the Association's liabilities.

For actuarial valuation purposes, Association assets are valued at Actuarial Value. Under this method, the assets used to determine employer contribution rates take into account market value by spreading all gains and losses (returns above or below expected returns) over five years. The Association's financial statements are audited by an outside auditor.

Our firm has prepared all of the schedules presented in the actuarial report. The actuarial assumptions shown in the schedules were selected by us as being appropriate for the valuation. An analysis of the Association's noneconomic experience was performed as of June 30, 2004 to establish the validity of these assumptions. The assumptions used in the most recent valuation produce results which, in the aggregate, reasonably approximate the anticipated future experience of the Association. The next experience analysis is due to be performed as of June 30, 2007.

We certify that the valuation was performed in accordance with generally accepted actuarial principles and practices. In particular, the assumptions and methods used for funding purposes meet the parameters of the Governmental Accounting Standards Board Statement No. 25.

Respectfully submitted,

Mike Moehle

Michael Moehle, F.S.A., E.A., M.A.A.A.
Principal and Consulting Actuary

Eva Yum, F.S.A., E.A.
Director and Consulting Actuary

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

SUMMARY OF ASSUMPTIONS AND FUNDING METHODS

A. Economic Assumptions

The following economic assumptions and non-economic assumptions were recommended by the actuary and adopted by the Board of Retirement as of the most recent actuarial valuation (dated June 30, 2005):

Investment Rate of Return	8.00% per annum (equates 8.16% effective rate) 3.50% real, 4.50% inflation.
Inflation	4.50% per annum.
Cost of Living Adjustments	Up to 3% per annum for Tier 1
Asset Valuation Method	Five year smoothed market
Interest Credited to Active Members Reserves	Pursuant to the MCERA Interest Crediting Policy, adopted March 13, 2003, interest will fall within a range from 0-2% below the valuation interest rate.
Average Annual Salary Increases	5.50% (4.50% inflation, 1.00% average merit and longevity increase

B. Non-Economic Assumptions

The date of the last study of the Plan's actual experience was June 30, 2005. There have been no changes in actuarial assumptions or methods since that valuation.

Post-Retirement Mortality Tables Used:

1. Service

General Member Males	1994 Group Annuity Mortality Table for Males (unadjusted)
General Member Females	1994 Group Annuity Mortality Table for Females (unadjusted)

Note: Information compiled from Actuarial Report prepared by Buck Consultants dated June 30, 2005.

Safety Member	1994 Group Annuity Mortality Table for Males (1 year setback)

2. Disability

General Males	1981 Disability Mortality Table for General Members, (no setback)
General Females	1981 Disability Mortality Table for General Members (5 year setback)
Safety Member	1981 Disability Mortality Table for Safety Members, (1 year setback)

3. For Employee Contribution Rate Purposes

General Member	1994 Group Annuity Mortality Table for Males (set back 3 years)
Safety Member	1994 Group Annuity Mortality Table for Males (unadjusted)

Pre-Retirement Mortality	Based upon the Experience Analysis as of 6/30/05 (See Schedule of Probabilities of Separation from Active Service)
Withdrawal Rates	Based upon the Experience Analysis as of 6/30/05 (See Schedule of Probabilities of Separation from Active Service)
Disability Rates	Based upon the Experience Analysis as of 6/30/05 (See Schedule of Probabilities of Separation from Active Service)
Service Retirement Rates	Based upon the Experience Analysis as of 6/30/05 (See Schedule of Probabilities of Separation from Active Service)
Salary Growth	Total increases of 5.5% per year, reflecting 4.5% for inflation and an average of 1% per year for merit and longevity

Note: Information compiled from Actuarial Report prepared by Buck Consultants dated June 30, 2005.

SUMMARY OF ASSUMPTIONS AND FUNDING METHODS
(Continued)

C. Funding Method

Employer contributions are actuarially determined level percentage rates that are expressed as percentages of annual payroll. The liability is presently being funded on the Entry Age Normal Actuarial Cost Method. Any unfunded actuarial accrued liability (UAAL) is amortized as a level percentage of projected future payroll cost over a 19-year period from June 30, 2005.

D. Plan Description

A summary of plan provisions can be found in Note 1 of the **NOTES TO BASIC FINANCIAL STATEMENTS**.

Note: Information compiled from Actuarial Report prepared by Buck Consultants dated June 30, 2005.

PROBABILITIES OF SEPARATION FROM ACTIVE SERVICE

GENERAL MEMBERS – MALES

Age	Withdrawal	Ordinary Death	Ordinary Disability	Service	Death While Eligible	Duty Death	Duty Disability	Terminated Vested
20	0.20900	0.00030	0.00000	0.00000	0.00000	0.00000	0.00008	0.00000
30	0.14850	0.00040	0.00080	0.00000	0.00010	0.00000	0.00040	0.01850
40	0.08030	0.00060	0.00130	0.00000	0.00030	0.00000	0.00096	0.02270
50	0.04180	0.00100	0.00240	0.09000	0.00110	0.00000	0.00192	0.02320
60	0.01320	0.00170	0.00420	0.16000	0.00310	0.00000	0.00336	0.01480
70	0.00000	0.00000	0.00000	1.00000	0.00000	0.00000	0.00000	0.00000

PROBABILITIES OF SEPARATION FROM ACTIVE SERVICE

GENERAL MEMBERS – FEMALES

Age	Withdrawal	Ordinary Death	Ordinary Disability	Service	Death While Eligible	Duty Death	Duty Disability	Terminated Vested
20	0.17200	0.00015	0.00000	0.00000	0.00000	0.00000	0.00008	0.00000
30	0.12720	0.00023	0.00020	0.00000	0.00008	0.00000	0.00023	0.01930
40	0.06480	0.00045	0.00040	0.00000	0.00015	0.00000	0.00038	0.02290
50	0.03320	0.00060	0.00180	0.09000	0.00060	0.00000	0.00120	0.01980
60	0.01040	0.00083	0.00460	0.16000	0.00210	0.00000	0.00315	0.01430
70	0.00000	0.00000	0.00000	1.00000	0.00000	0.00000	0.00000	0.00000

PROBABILITIES OF SEPARATION FROM ACTIVE SERVICE

SAFETY MEMBERS

Age	Withdrawal	Ordinary Death	Ordinary Disability	Service	Death While Eligible	Duty Death	Duty Disability	Terminated Vested
20	0.13000	0.00030	0.00000	0.00000	0.00000	0.00030	0.00650	0.00000
30	0.07800	0.00050	0.00030	0.00000	0.00010	0.00060	0.00840	0.02280
40	0.02500	0.00160	0.00060	0.00000	0.00020	0.00170	0.01280	0.01660
50	0.00900	0.00260	0.00120	0.04500	0.00100	0.00270	0.01990	0.00700
60	0.00000	0.00000	0.00000	1.00000	0.00000	0.00000	0.00000	0.00000

Note: Information compiled from Actuarial Report prepared by Buck Consultants dated June 30, 2005.

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

SCHEDULE OF ACTIVE MEMBER VALUATION DATA

Valuation Date	Plan Type	Number	Annual Salary	Average Annual Salary	% Increase in Average Salary
7/1/99	General	1,710	$54,639,000	$31,953	-1.59%
	Safety	221	$ 7,882,000	$35,665	-0.12%
	Total	1,931	$62,521,000	$32,378	-9.69%
7/1/01	General	1,850	$67,021,000	$36,228	13.38%
	Safety	234	$ 8,994,000	$38,436	7.77%
	Total	2,084	$76,015,000	$36,476	12.66%
7/1/02	General	1,934	$72,601,000	$37,539	3.62%
	Safety	249	$10,400,000	$41,767	8.67%
	Total	2,183	$83,001,000	$38,022	4.24%
7/1/03	General	1930	$76,971,000	$39,882	6.24%
	Safety	262	$11,615,000	$44,332	6.14%
	Total	2192	$88,586,000	$40,413	6.28%
7/1/04	General	1,824	$77,023,000	$42,228	5.88%
	Safety	268	$12,493,000	$46,616	5.15%
	Total	2,092	$89,516,000	$42,790	5.88%
7/1/05	General	1,892	$83,166,000	$43,957	4.09%
	Safety	295	$14,341,000	$48,614	4.29%
	Total	2,187	$97,507,000	$44,585	4.19%

Note: Information compiled from Actuarial Report prepared by Buck Consultants dated June 30, 2005.

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

RETIRANTS AND BENEFICIARIES ADDED TO AND REMOVED FROM RETIREE PAYROLL

Year	Beginning of Year	Added During Year	Allowances Added ($ 000)	Removed During Year	Allowances Removed ($ 000)	End of Year	Retiree Payroll ($ 000)	% Increase In Retiree Payroll	Average Annual Allowance
7/1/99	1,144	N/A	N/A	N/A	N/A	1,179	$14,398	10.49%	$12,212
7/1/01	1,179	N/A	N/A	N/A	N/A	1,259	$16,548	14.93%	$13,144
7/1/02	1,259	N/A	N/A	N/A	N/A	1,295	$17,673	6.80%	$13,647
7/1/03	1,295	N/A	N/A	N/A	N/A	1,348	$20,369	15.25%	$15,110
7/1/04	1,348	124	2,807	31	396	1,441	$22,780	11.84%	$15,808
7/1/05	1,441	109	2,445	49	450	1,477	$24,867	9.16%	$16,836

SOLVENCY TEST

(Dollar Amounts in Thousands)

	Actuarial Accrued Liabilities (AAL) For					Portion of Accrued Liabilities Covered by Reported Assets		
Valuation Date	1 Active Member Contributions	2 Retirants and Beneficiaries	3 Active Members Employer Portion	Actuarial Accrued Liabilities	Valuation Assets	1	2	3
6/30/99	$43,736	$187,535	$119,981	$351,252	$354,467	100%	100%	100%
6/30/01	$49,481	$211,439	$143,396	$404,316	$411,710	100%	100%	100%
6/30/02	$50,941	$212,359	$158,135	$421,435	$424,613	100%	100%	100%
6/30/03	$48,379	$238,727	$164,075	$451,181	$428,959	100%	100%	86%
6/30/04	$48,708	$265,193	$218,037	$531,938	$430,054	100%	100%	53%
6/30/05	$49,162	$281,246	$259,386	$589,794	$428,813	100%	100%	38%

ACTUARIAL ANALYSIS OF FINANCIAL EXPERIENCE
For Years Ended June 30

	Actuarial (Gains)/Losses					
Plan Year Ending	Asset Sources ($ 000)	Liability Sources ($ 000)	Total ($ 000)	Changes in Plan Provisions ($ 000)	Changes in Assumptions/Methods ($ 000)	Total (Gain)/Loss ($ 000)
6/30/00	N/A	N/A	14,316	N/A	N/A	14,316
6/30/01	N/A	N/A	(804)	N/A	N/A	(804)
6/30/02	N/A	N/A	(7,565)	N/A	N/A	(7,565)
6/30/03	15,639	11,232	26,871	N/A	N/A	26,871
6/30/04	18,204	5,320	23,524	51,722	3,646	78,892
6/30/05	23,825	9,230	33,055	2,435	14,012	49,502

Information compiled from Actuarial Report prepared by Buck Consultants. MCERA had no actuarial valuation for the year ending 06/30/2000.

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Statistical Section

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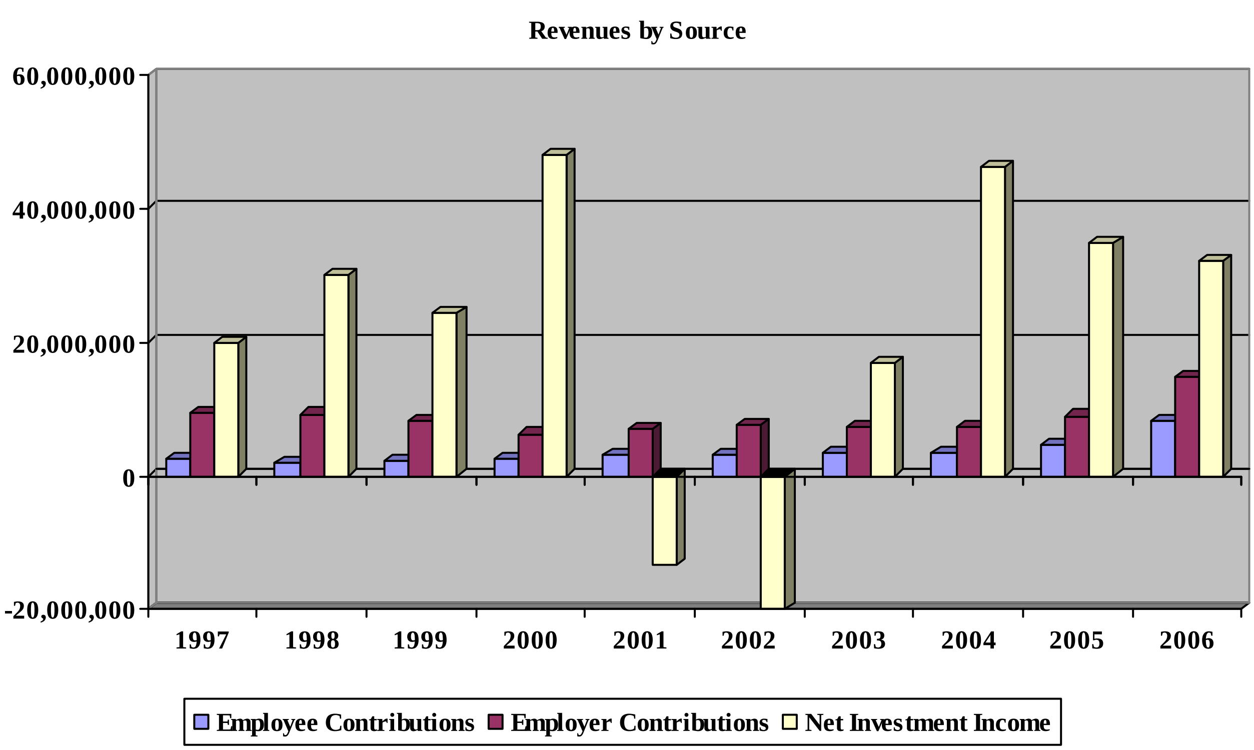
MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

REVENUES BY SOURCE

Fiscal Year Ending	Employee Contributions	Employer Contributions		Employer % of Covered Payroll	Net Investment Income		Total
6/30/97	$ 2,632,852	$ 9,494,988		16.20%	$ 19,851,280		$ 31,979,121
6/30/98	$ 2,039,856	$ 9,253,420		17.38%	$ 29,982,575		$ 41,275,851
6/30/99	$ 2,273,270	$ 8,223,833	**	13.65%	$ 24,394,230		$ 34,891,333
6/30/00	$ 2,435,360	$ 6,259,387	**	9.37%	$ 47,987,209		$ 56,681,956
6/30/01	$ 3,042,813	$ 6,926,949	**	9.66%	$(13,342,217)	*	$ (3,372,455)
6/30/02	$ 3,186,740	$ 7,731,363	**	9.64%	$(19,789,912)	*	$ (8,871,809)
6/30/03	$ 3,298,317	$ 7,200,728	**	8.21%	$ 16,957,409	*	$ 27,456,454
6/30/04	$ 3,347,455	$ 7,268,826	**	7.95%	$ 46,098,461	*	$ 56,714,742
6/30/05	$ 4,584,598	$ 8,930,842	**	9.57%	$ 34,840,502	*	$ 48,355,942
6/30/06	$ 8,221,757	$ 14,749,934	**	15.02%	$ 32,191,872		$ 55,163,563

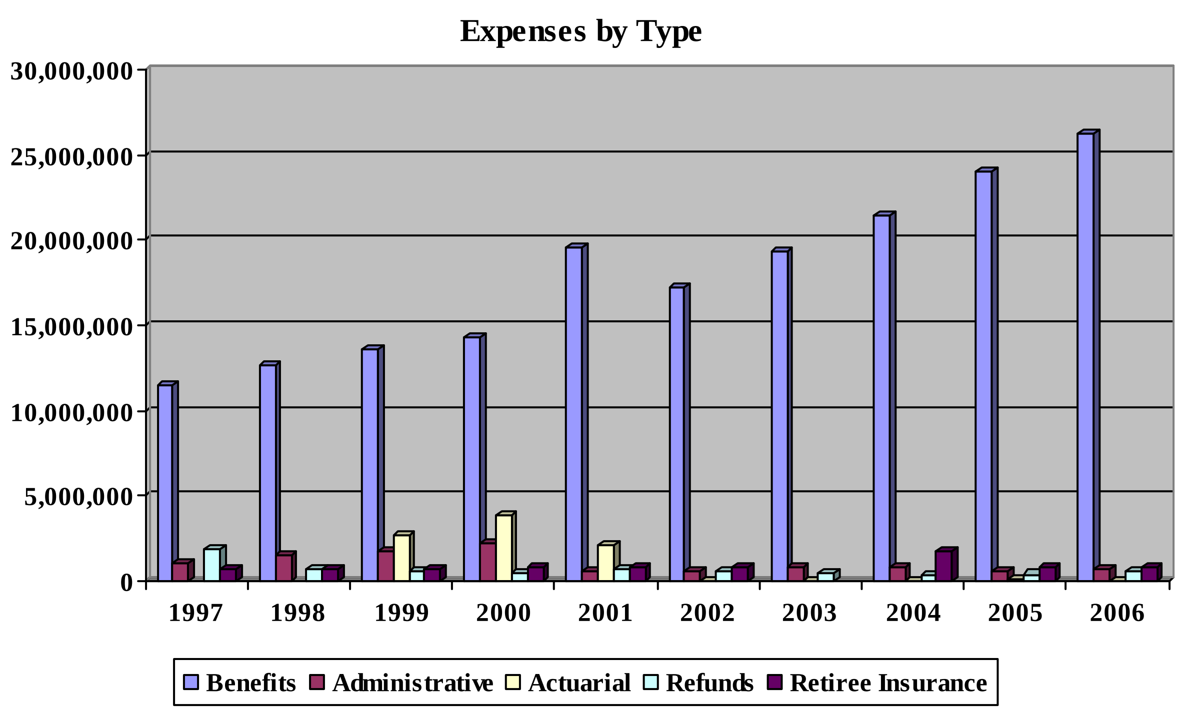


MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

EXPENSES BY TYPE

Fiscal Year Ending		Benefits	Administrative Expenses	Actuarial Expense	Refunds	Retiree Insurance Premium	Total
06/30/97		$ 11,494,535	$ 1,089,118	-	$ 1,842,437	$ 669,118	$ 15,095,208
06/30/98		$ 12,601,445	$ 1,479,445	-	$ 646,853	$ 690,702	$ 15,418,654
6/30/99		$ 13,604,448	$ 1,772,025	$ 2,676,827	$ 624,867	$ 690,702	$ 19,368,871
6/30/00		$ 14,251,035	$ 2,206,015	$ 3,833,565	$ 466,009	$ 823,642	$ 21,580,266
6/30/01	*	$ 19,520,377	$ 528,918	$ 2,078,546	$ 681,371	$ 850,702	$ 23,659,914
6/30/02	*	$ 17,264,575	$ 586,146	$ 7,403	$ 625,159	$ 850,702	$ 19,333,985
6/30/03	*	$ 19,345,829	$ 820,341	-	$ 498,749	-	$ 20,664,919
6/30/04	*	$ 21,498,606	$ 830,439	-	$ 349,488	$ 1,758,550	$ 24,437,083
6/30/05	*	$ 24,069,742	$ 602,451	$ 61,951	$ 409,034	$ 850,000	$ 25,993,178
6/30/06	*	$ 26,263,569	$ 649,080	$ 48,438	$ 602,210	$ 850,000	$ 28,413,297

*Beginning with June 30, 2001 the amounts listed under Administrative, Investment, Depreciation and Other Expenses have been reclassified to conform to the 2006 presentation.



MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

SCHEDULE OF BENEFIT EXPENSES BY TYPE

(Dollar Amounts in Thousands)

	2005	2004	2003	2002	2001	1999	1998	1997	1996	1994
Service Retirement										
Payroll:										
General	$16,378	$14,977	$13,197	$11,238	$11,158	$9,237	$8,274	$7,777	$6,352	$5,622
Safety	3,030	2,506	2,349	1,908	1,810	1,547	1,320	1,219	1,129	1,042
Total	$19,408	$17,483	$15,546	$13,146	$12,968	$10,784	$9,594	$8,996	$7,481	$6,704
Disability Retiree										
Payroll										
General	$1,478	$1,443	$1,388	$1,384	$1,339	$1,154	$1,061	$989	$906	$736
Safety	1,816	1,769	1,572	1,483	1,362	1,122	1,054	1,002	952	741
Total	$3,294	$3,212	$2,960	$2,867	$2,701	$2,276	$2,115	$1,991	$1,858	$1,477
Beneficiary										
Payroll										
General	$1,613	$1,511	$1,347	$1,211	$1,130	$908	$891	$836	$706	$560
Safety	551	575	515	449	439	430	431	407	369	302
Total	$2,164	$2,086	$1,862	$1,660	$1,569	$1,338	$1,322	$1,243	$1,075	$862
Total Benefit Expense										
Payroll										
General	$19,470	$17,931	$15,932	$13,833	$13,627	$11,299	$10,227	$9,603	$7,964	$6,819
Safety	5,397	4,849	4,437	3,840	3,609	3,099	2,804	2,629	2,450	$2,085
Total	$24,867	$22,780	$20,369	$17,673	$17,236	$14,398	$13,031	$12, 232	$10,414	$8,904

SCHEDULE OF RETIRED MEMBERS BY TYPE OF BENEFIT

(Summary of Monthly Allowances Being Paid—As of June 30, 2005)

	GENERAL MEMBERS		SAFETY MEMBERS		TOTAL	
	Number	Monthly Allowance	Number	Monthly Allowance	Number	Monthly Allowance
Service Retirement	981	$ 1,364,843	105	$ 252,515	1,086	$ 1,617,358
Disability	105	$ 123,190	78	$ 151,356	183	$ 274,546
Beneficiaries	174	$ 134,443	34	$ 45,897	208	$ 180,340
Total Retired Members	1,260	$ 1,622,476	217	$ 449,768	1,477	$ 2,072,244

Note: Information compiled from Actuarial Report prepared by Buck Consultants. Information for the fiscal year ending June 30, 2006 was not available for this report. MCERA had no actuarial valuation in 2000 and 1995.

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

SUMMARY OF ACTIVE MEMBER
For Years Ended June 30
(Annual Payroll Dollars in Millions)

	2005	2004	2003	2002	2001	1999	1998	1997	1996	1994
GENERAL TIER I										
Number	607	660	726	784	830	952	1,003	1,072	1,604	1,957
Annual Payroll**	$32,249	$32,594	$34,233	$35,222	$35,125	$34,553	$35,763	$35,157	$52,467	$61,079
Average Monthly Salary	$4,427	$4,115	$3,929	$3,744	$3,527	$3,025	$2,971	$2,733	$2,726	$2,601
Average Age	51.81	50.94	50.94	50.58	49.78	48.21	47.39	46.68	45.51	43.63
Average Service	18.80	17.29	17.29	16.48	15.72	14.11	13.30	12.34	10.87	8.88
GENERAL TIER II										
Number	1,285	1,164	1,204	1,150	1,020	758	549	392	401	-
Annual Payroll**	$50,917	$44,429	$42,738	$37,379	$31,896	$20,086	$14,628	$9,624	$9,986	-
Average Monthly Salary	$3,302	$3,181	$2,958	$2,709	$2,606	$2,208	$2,220	$2,046	2,075	-
Average Age	41.84	40.78	40.78	40.01	39.56	38.73	39.04	38.62	38.02	-
Average Service	4.81	3.71	3.71	3.09	2.79	2.27	2.15	1.87	1.17	-
SAFETY TIER I										
Number	110	118	128	136	144	173	178	190	195	196
Annual Payroll**	$6,421	$6,326	$6,426	$6,384	$6,130	$6,584	$6,617	$6,560	$6,702	$6,728
Average Monthly Salary	$4,864	$4,468	$4,184	$3,912	$3,547	$3,170	$3,098	$2,877	$2,864	$2,860
Average Age	45.63	45.03	45.03	44.60	43.68	41.48	41.34	40.20	39.72	39.50
Average Service	16.95	15.78	15.78	15.08	14.08	11.66	11.17	10.28	9.84	9.75
SAFETY TIER II										
Number	185	150	134	113	90	48	31	14	12	-
Annual Payroll**	$7,920	$6,167	$5,189	$4,016	$2,864	$1,301	$846	$351	$266	-
Average Monthly Salary	$3,568	$3,426	$3,227	$2,962	$2,652	$2,259	$2,274	$2.089	$1,847	-
Average Age	32.28	33.31	33.31	32.54	31.51	32.34	30.84	31.07	34.00	-
Average Service	3.30	2.83	2.83	2.36	2.17	1.52	1.64	1.64	1.00	-
TOTAL										
Number	2,187	2,092	2,192	2,183	2,084	1,931	1,761	1,668	2,212	2,153
Annual Payroll**	$97,507	$89,516	$88,586	$83,001	$76,015	$62,521	$57,854	$51,692	$69,421	$67,807
Average Monthly Salary	$3,715	$3,566	$3,368	$3,168	$3,040	$2,698	$2,738	$2,583	$2,615	$2,731
Average Age	43.99	43.69	43.94	43.71	43.57	43.49	43.88	43.92	43.58	41.57
Average Service	9.18	8.61	8.86	8.61	8.69	8.93	9.40	9.55	8.97	9.32

** Represents the annualization of active members' pay rates on June 30.

Note: Information compiled from Actuarial Report prepared by Buck Consultants. Information for the fiscal year ending June 30, 2006 was not available for this report. MCERA had no actuarial valuation for the fiscal years ending 2000 and 1995. Tier II was adopted in June 1994.

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

SUMMARY OF RETIRED MEMBERSHIP
For Years Ended June 30
(Basic and Total Annual Allowance Dollars in Millions)

	2005	2004	2003	2002	2001	1999	1998	1997	1996	1994
GENERAL										
Number	1,260	1,228	1,147	1,108	1,079	1,008	981	947	834	784
Basic Annual Allowance	$ 15,000	$ 13,786	$ 12,119	$ 10,298	$ 10,383	$ 8,731	$7,924	$7,554	$6,119	$5,357
Average Basic Monthly Allowance	$ 992	$ 936	$ 880	$ 775	$ 802	$ 722	$673	$665	$611	$569
Total Annual Allowance	$19,470	$17,931	$ 15,932	$ 13,833	$ 13,627	$ 11,299	$10,227	$9,603	$7,964	$6,718
Average Total Monthly Allowance	$1,288	$1,217	$ 1,158	$ 1,040	$ 1,052	$ 934	$869	$845	$796	$735
SAFETY										
Number	217	213	201	187	180	171	163	158	148	130
Basic Annual Allowance	$4,038	$3,597	$ 3,300	$ 2,818	$ 2,671	$ 2,373	$2,156	$2,071	$1,941	$1,682
Average Basic Monthly Allowance	$1,551	$1,407	$ 1,368	$ 1,256	$ 1,237	$ 1,156	$1,102	$1,092	$1,093	$1,078
Total Annual Allowance	$5,397	$4,849	$ 4,437	$ 3,840	$ 3,609	$ 3,099	$2,804	$2,628	$2,450	$2,085
Average Total Monthly Allowance	$2,073	$1,897	$ 1,840	$ 1,711	$ 1,671	$ 1,510	$1,434	$1,386	$1,380	$1,337
TOTAL										
Number	1,477	1,441	1,348	1,295	1,259	1,179	1,144	1,105	982	914
Basic Annual Allowance	$19,038	$17,383	$ 15,419	$ 13,116	$ 13,054	$ 11,104	$10,080	$9,625	$8,060	$7,040
Average Basic Monthly Allowance	$1,074	$1,005	$ 953	$ 844	$ 864	$ 785	$734	$726	$684	$642
Total Annual Allowance	$24,867	$22,780	$ 20,369	$ 17,673	$ 17,236	$ 14,398	$13,031	$12,231	$10,414	$9,003
Average Total Monthly Allowance	$1,403	$1,317	$ 1,259	$ 1,137	$ 1,141	$ 1,018	$949	$922	$884	$821

SUMMARY OF INACTIVE MEMBERSHIP*

	2005	2004	2003	2002	2001	1999	1998	1997	1996	1994
GENERAL										
Number	453	438	449	454	437	429	401	406	212	-
SAFETY										
Number	81	70	74	75	76	68	66	65	69	-
TOTAL										
Number	534	508	523	529	513	497	467	471	281	-

Note: Information compiled from Actuarial Report prepared by Buck Consultants. Information for the fiscal year ending June 30, 2006 was not available for this report. *Includes unclaimed accounts. 1994 Inactive membership information was not available

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

RETIRED MEMBERS BY TYPE OF RETIREMENT
As of June 30, 2006

		Type of Retirement*							Option Selected**			
Amount of Monthly Benefit	Number of Members	1	2	3	4	5	6	7	Unmodified	Opt 1	Opt 2	Opt 3
1 - 250	107	28	51	19	0	7	2	0	81	5	17	4
251 - 500	172	22	82	36	7	11	14	0	140	8	22	2
501 - 750	200	55	93	31	5	2	14	0	174	11	12	3
751 - 1,000	216	75	84	24	6	12	15	0	193	6	15	2
1,001 - 1,250	162	67	59	11	4	9	12	0	148	4	7	3
1,251 - 1,500	133	59	39	10	4	18	2	1	123	1	8	1
1,501 - 1,750	94	39	18	4	0	30	3	0	84	2	8	0
1,751 - 2,000	88	41	23	4	0	17	3	0	81	1	6	0
Over 2000	350	217	67	10	4	50	1	0	333	4	9	4
Total	1552	603	516	149	30	156	66	1	1357	42	104	19

Notes:

*Type of Retirement:
- 1—Normal Retirement for age and service
- 2—Early retirement
- 3—Beneficiary payment, normal or early retirement
- 4—Beneficiary payment, death in service
- 5—Duty disability retirement
- 6—Nonduty disability retirement
- 7—Beneficiary payment, disability retirement

**Option Selected

Unmodified Plan: beneficiary receives 60 % continuance.

The following options reduce the retired member’s monthly benefit:
- Option 1—Beneficiary receives lump sum or member’s unused contributions
- Option 2—Beneficiary receives 100% of member’s reduced allowance
- Option 3—Beneficiary receives 50% of member’s reduced allowance

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

RETIRED MEMBERS AVERAGE BENEFIT PAYMENTS

Last ten years

Retirement Effective Dates	Years of Credited Service						
Period 07/01/05 to 06/30/06	0-5	05-10	10-15	15-20	20-25	25-30	30+
Average monthly benefit	$ 699	$ 1,000	$ 1,185	$ 2,176	$ 2,730	$ 3,290	$ 5,095
Average final average salary	$ 4,382	$ 3,499	$ 4,104	$ 4,726	$ 4,250	$ 4,542	$ 5,509
Number of retired members	5	13	16	13	8	13	10
Period 07/01/04 to 06/30/05							
Average monthly benefit	$ 657	$ 539	$ 1,212	$ 1,643	$ 1,620	$ 4,003	$ 5,101
Average final average salary	$ 6,041	$ 3,802	$ 4,476	$ 4,160	$ 3,190	$ 5,913	$ 6,591
Number of retired members	3	11	18	9	3	6	12
Period 07/01/03 to 06/30/04							
Average monthly benefit	$ 414	$ 510	$ 977	$ 1,332	$ 1,658	$ 2,870	$ 3,577
Average final average salary	$ 5,485	$ 3,238	$ 3,443	$ 3,789	$ 3,606	$ 4,768	$ 4,632
Number of retired members	5	14	19	30	16	11	23
Period 07/01/02 to 06/30/03							
Average monthly benefit	$ 953	$ 1,541	$ 1,236	$ 1,469	$ 2,080	$ 2,559	$ 5,693
Average final average salary	$ 4,854	$ 4,657	$ 4,018	$ 3,784	$ 4,669	$ 4,648	$ 7,125
Number of retired members	6	13	28	14	11	6	16
Period 07/01/01 to 06/30/02							
Average monthly benefit	$ 438	$ 780	$ 1,005	$ 1,130	$ 1,398	$ 1,485	$ 4,310
Average final average salary	$ 4,229	$ 4,216	$ 3,877	$ 3,383	$ 3,604	$ 3,217	$ 5,437
Number of retired members	5	11	17	16	9	4	8
Period 07/01/00 to 06/30/01							
Average monthly benefit	$ 161	$ 638	$ 927	$ 1,511	$ 1,580	$ 1,516	$ 4,113
Average final average salary	$ 4,292	$ 3,688	$ 3,660	$ 3,878	$ 3,823	$ 2,976	$ 5,146
Number of retired members	8	7	18	13	16	5	4
Period 07/01/99 to 06/30/00							
Average monthly benefit	$ 64	$ 510	$ 762	$ 1,017	$ 1,556	$ 2,060	$ 1,776
Average final average salary	$ 4,116	$ 3,069	$ 3,208	$ 3,120	$ 3,358	$ 3,303	$ 2,975
Number of retired members	4	10	17	9	5	8	3
Period 07/01/98 to 06/30/99							
Average monthly benefit	$ 127	$ 493	$ 840	$ 1,115	$ 1,493	$ 2,026	$ 2,204
Average final average salary	$ 3,572	$ 3,327	$ 3,451	$ 3,090	$ 3,224	$ 3,662	$ 3,112
Number of retired members	4	9	21	4	8	5	5
Period 07/01/97 to 06/30/98							
Average monthly benefit	$ 124	$ 780	$ 552	$ 989	$ 1,354	$ 2,184	$ 2,878
Average final average salary	$ 3,793	$ 3,894	$ 2,509	$ 2,815	$ 3,072	$ 2,997	$ 3,180
Number of retired members	2	4	22	6	7	2	8
Period 07/01/96 to 06/30/97							
Average monthly benefit	$ 551	$ 551	$ 613	$ 910	$ 1,169	$ 2,137	$ 2,596
Average final average salary	$ 4,725	$ 2,701	$ 2,773	$ 3,001	$ 2,619	$ 3,577	$ 3,250
Number of retired members	4	7	44	40	15	6	9

ACTUARIAL BALANCE SHEET

For the Year Ending June 30

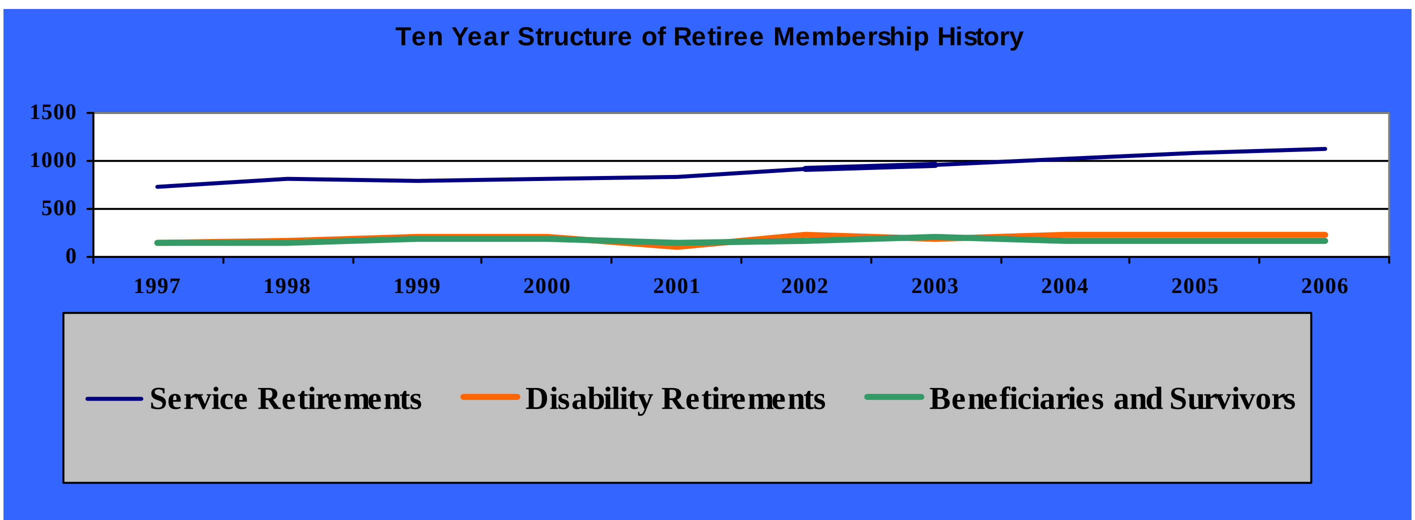
		2005	2004
	ASSETS		
1.	Total actuarial value of assets	$ 428,813,477	$ 430,053,925
2.	Present value of future contributions by members	46,403,626	42,218,183
3.	Present value of future employer contributions for normal cost	48,660,586	42,437,607
4.	Present value of other future employer contributions (UAAL)	160,980,930	101,884,508
5.	Total Actuarial Assets	$ 684,858,619	$ 616,594,223
	LIABILITIES		
6.	Present value of retirement allowances payable to retired members and their survivors	$ 274,772,830	$ 258,185,204
7.	Present value of service retirement allowances payable to presently active member and their survivors	288,296,652	247,605,621
8.	Present value of allowances payable to current and future vested terminated members and their survivors	67,239,410	60,451,246
9.	Present value of disability retirement allowances payable to presently active members and their survivors	26,848,431	24,077,021
10.	Present value of death benefits payable on behalf of presently active members	5,022,347	4,478,901
11.	Present value of members' contributions to be returned upon withdrawal	16,205,719	14,788,673
12.	Special Reserves	6,473,230	7,007,557
13.	Total Actuarial Liabilities	$ 684,858,619	$ 616,594,223
	FUNDED RATIO		
14.	Present value of future benefits (items 6 to 12)	$ 684,858,619	$ 616,594,223
15.	Present value of future contributions by members and employers (items 2 and 3)	95,064,212	84,655,790
16.	Actuarial accrued liability (item 14 minus item 15)	589,794,407	531,938,433
17.	Actuarial value of assets	428,813,477	430,053,925
18.	Unfunded actuarial accrued liability (UAAL) (item 16 minus item 17)	$ 160,980,930	$ 101,884,508
19.	Funded Ratio	72.7%	80.8%

MERCED COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

PARTICIPATING EMPLOYERS AND ACTIVE MEMBERS

Current Year and Nine Years Ago
(Information Compiled from Plan's Data Base)

County of Merced	**2006**	**2005**	**2004**	**2003**	**2002**	**2001**	**2000**	**1999**	**1998**	**1997**
General Members	1,853	1,931	1,882	1,928	2,060	1,874	1,821	1,745	1,608	1,488
Safety Members	316	296	274	262	253	234	233	221	215	204
Total County of Merced	2,169	2,227	2,156	2,190	2,313	2,108	2,054	1,966	1,823	1,692
Percentage of Membership	95.22%	99.87%	99.91%	99.91%	99.87%	99.86%	99.86%	99.85%	99.84%	99.83%
Participating Agencies										
Merced Cemetery District	3	3	2	2	3	3	3	3	3	3
Percentage of Membership	.13%	.13%	.09%	.09%	.13%	.14%	.14%	.15%	.16%	.17%
Superior Court of California	106	-	-	-	-	-	-	-	-	-
Percentage of Membership	4.65%	-	-	-	-	-	-	-	-	-
Total Participating Agencies	109	3	2	2	3	3	3	3	3	3
Total Active Membership										
General	1,962	1,934	1,884	1,930	2,063	1,877	1,824	1,748	1,611	1,491
Safety	316	296	274	262	253	234	233	221	215	204
Total	**2,278**	**2,230**	**2,158**	**2,192**	**2,316**	**2,111**	**2,057**	**1,969**	**1,826**	**1,695**



	1997	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**
Service Retirements	733	818	783	809	826	911	966	1,012	1,073	1,119
Disability Retirements	152	162	212	207	108	225	180	233	232	227
Beneficiaries and Survivors	155	156	180	184	145	158	202	171	171	175
Total	1,040	1,136	1,175	1,200	1,079	1,294	1,348	1,416	1,476	1,521

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