Merced County Employees' Retirement Association

AGENDA
Retirement Board Education Meeting

Thursday, September 3, 2026, 9:30 A.M. - 12:30 P.M.

Location: Merced County Employees' Retirement Association
690 W 19th Street, Merced, CA
2nd Floor, Training Room

1. **Call to Order- 9:30 A.M.**

The Retirement Board may discuss and take action on the following:

2. **Roll Call**

3. **Public Comment**
Members of the public may comment on any item under the Board's jurisdiction including items on the Board's agenda. Matters presented under this item will not be discussed or acted upon by the Board at this time. Persons addressing the Board will be limited to a maximum of five (5) minutes in total. Please state your name for the record.

4. **Meeting**
Board Education
Discussion on the following presentations:
a. Private Equity Valuation Overview – Cliffwater LLC
b. County Employees Retirement Law of 1937 Disability Retirement – Ted Cabral

5. **Information Sharing**

6. **Adjournment**

The Agenda and supporting documentation, including any material that was submitted to the Merced County Employees' Retirement Association Board after the distribution of the Agenda, are available online at www.mercedcera.com.

All supporting documentation for Agenda items, including any material that was submitted to the retirement board after the distribution of the Agenda, is also available for public inspection Monday through Friday from 8:00 a.m. to 5:00 p.m. at the administrative office for the Merced County Employees' Retirement Association located at 690 W 19th Street, Merced, California 95340.

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Merced County Employees' Retirement Association

Spanish and Hmong interpreters are available.

Interpretes de espanol y hmong estan disponibles.
Peb muaj tug paab txhais lug Mev hab Hmoob.

Presentation to MercedCERA

Private Equity Valuation

September 2026

CLIFFWATER

Agenda

1. Private equity valuation methodology
2. Regulatory framework and quarterly valuation process
3. Buyout and venture capital valuation examples
4. Valuation and performance metrics during different market environments
5. Protections for private fund investors

Relevant Legal & Compliance Background

Prior to 2007, valuing investments at cost basis was prevalent.

ASC 820 (fair value measurement) was initially issued as FAS 157 in 2006 (effective for 2007 financial reporting) and changed to ASC 820 in 2008.

Private equity firms became subject to mandatory SEC registration under Title IV of the Dodd-Frank Act of 2010 known as the Private Fund Investment Advisers Registration Act.

Private managers with at least $150 million of assets AUM were required to register with the SEC and file an ADV form. Venture capital managers are exempt from this rule and file an abbreviated Form ADV.

The SEC began its presence exam initiative in 2012 to ensure compliance of rules regarding fees and expenses.

Private Equity Valuation Process

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Accounting Standards Codification 820 (“ASC 820”) - Fair Value Classification

Fair Value Definition: The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Level 1: Quoted prices (unadjusted) are available in active markets for identical investments as of the reporting date.

Level 2: Pricing inputs are observable for the investments, either directly or indirectly, as of the reporting date, but are not the same as those used in Level 1. Fair value is determined through the use of models or other valuation methodologies.

Level 3: Pricing inputs are unobservable for the investments and include situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require significant judgement or estimation by the General Partner.

Private Equity Valuation Process

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Valuation Methodologies – Level 3 Investments

Market Approach

- Under the market approach, fair value may be determined by reference to a recent transaction involving the portfolio company or by reference to observable valuation measures for companies that are determined to be comparable
- In determining value under this approach, key performance metrics of the portfolio company, such as earnings before interest, taxes, depreciation and amortization, will be multiplied by a relevant valuation multiple observed in the range of comparable companies or transactions – adjusted for differences between the portfolio company and the referenced comparable company

Income Approach

- Under the income approach, fair value is determined by converting future amounts, such as cash flows or earnings, to a single present discounted amount using current market expectations about those future amounts
- In determining value under this approach, the firm will make assumptions regarding unobservable inputs such as revenues, operating income, depreciation and amortization, capital expenditures, income taxes, working capital needs, and the terminal value of the investee company, among others

Cost

- Cost basis may be considered the best indicator of fair value if a recent portfolio company acquisition is performing in line with expectations or if no significant events have occurred subsequent

Private Equity Valuation Process

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- Fair value is primarily determined internally as of the end of each calendar quarter
- Portfolio companies generally provide financial information each quarter that may impact fair value, including financial statements and other key performance metrics
- Deal team professionals perform the valuation analysis for each portfolio company after considering factors such as recent financial performance, future expectations, or significant business or industry developments
- Finance and accounting professionals review the proposed valuations for consistency across quarters, existence of valuation support, and computational accuracy
- The quarterly valuations are subject to approval by the firm's Valuation Committee
- Portfolio company valuations are reviewed during the annual external audit process
- Independent valuation firms, such as Kroll or Houlihan Lokey, may be utilized to review internal valuations or provide an independent range of valuations for comparison

Operational Due Diligence Assessment

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Focus on valuation process during the initial diligence and ongoing monitoring.

Valuation Policy and Procedures		Yes	No
	Valuation policy establishes the methods, sources, third parties and procedures used to value each product type that may be invested in by the fund		
	Valuation policy mitigates potential conflicts of interest inherent in valuing investment positions		
	Valuation policy is reviewed at least annually and updated when a new security type is introduced		
	Professionals responsible for valuation are knowledgeable and qualified to implement valuation policies on a day-to-day basis		
	Professionals responsible for valuation frequently review processes and models to ensure effectiveness		
	The manager reviews and approves the guidelines and policies for classifying investments within the ASC 820 structure		
	The manager has policies to ensure the selection and oversight of third-party valuation providers is appropriate for the products traded, if applicable		
	The manager ensures valuation policies are fairly and consistently applied		
Valuation Sources		Yes	No
	Manager uses independent, reliable, and recognized pricing inputs		
	Manager maintains credible supporting documentation for all positions priced by the manager		
	Manager collects and evaluates all information which could impact quarterly valuations on an ongoing basis		
	Upon request the manager discusses and/or provides limited partners with supporting documentation for all positions priced by the manager		
	Manager's reliance on valuation models is reasonable given the nature of the products and strategy		
Advisory Board Review Process		Yes	No
	The Advisory Board has the ability to review portfolio valuations		

MercedCERA Portfolio: Buyout Example

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Quarterly performance summaries by fund on the Cliffwater client portal

Example:

Provider of packaging equipment

- Acquired for a price of 8x EBITDA
- Revenue grows by 20% and EBITDA grows by 10% during the first year
- Investment is valued at 1.2 times cost basis after the first year of ownership
- Comparable companies trade at a premium to 8x EBITDA
- Manager calculates the median value of comparable company transactions and applies a valuation multiple of 8.5x EBITDA.

MercedCERA Portfolio: Venture Example

Quarterly performance summaries by fund on the Cliffwater client portal

Example:

AI-enabled software development platform

- Invested at a pre-money valuation of ~$2 billion.
- Investment was written up to ~1.4 times invested capital after one year reflecting company technical progress, intermediate rounds of financing, and revenue generation of >100% year-over-year.
- Company closed a new round of financing the quarter after at a $10.2 billion post-money valuation, with a new third-party venture fund leading the pricing of the round.
- Investment is valued at a modest discount to last round's post money valuation.

Valuation Process Constraints

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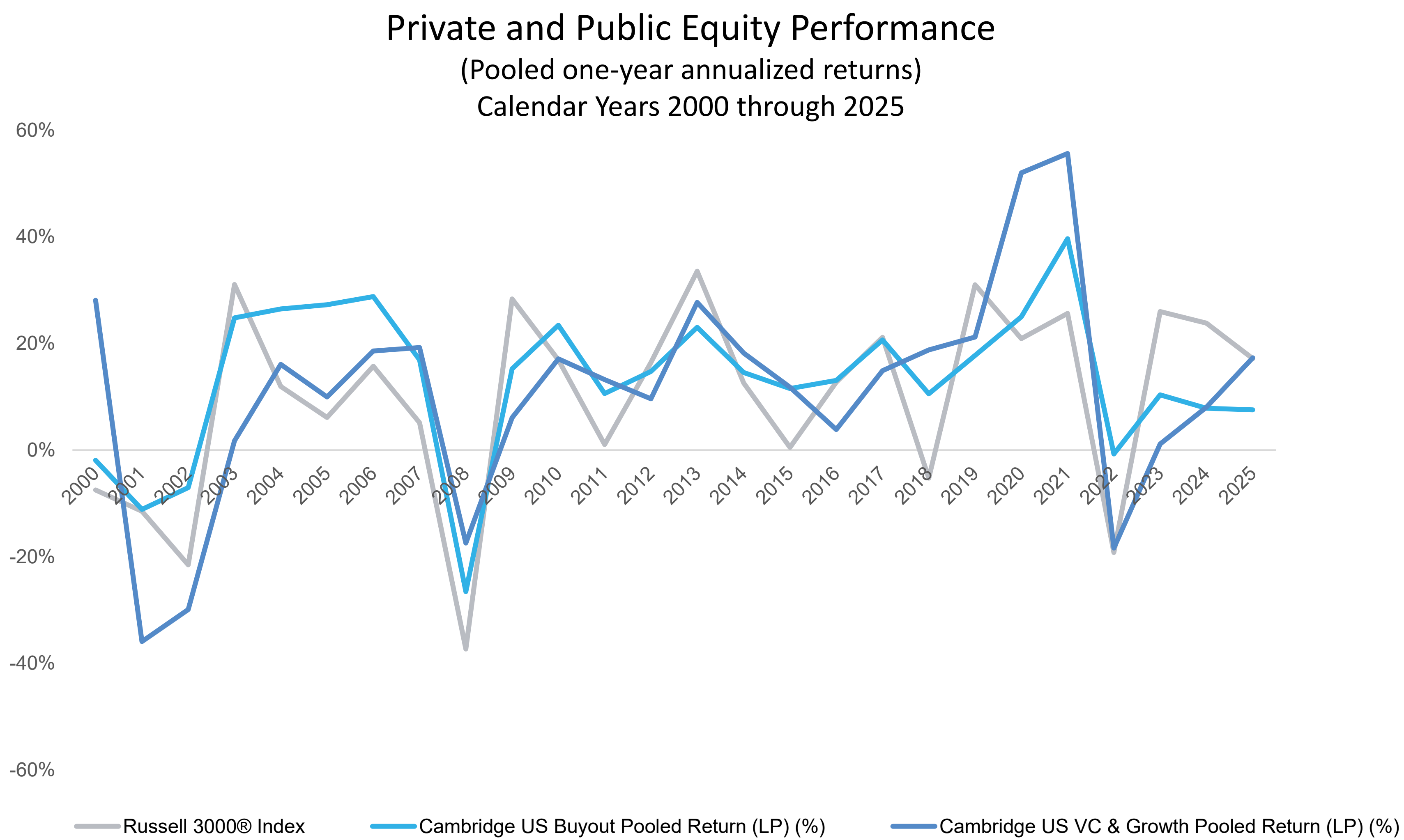
- Weak set of comparable data
- Rapid and unexpected change in company performance
- Significant change in market conditions
- Time lag in private market reporting

Historical Valuation Trends



1. Cambridge Associates data as of 12/31/2025. Data includes buyout, growth equity, and venture capital returns.

Private Fund Economic Terms

- **Management fee (base)** typically decreases post-investment period.
- **Profit sharing** between LPs and GPs is typically 80/20. Certain high performing GPs are able to negotiate a 25% or 30% profit share.
- Partnership agreements dictate the **timing of distributions**.
- Quarterly valuations on active (unrealized) investments **do not affect** management fee payments or carried interest payments to GPs.
- Other LPA protections to LPs include the **"Clawback Obligation"** which requires the GP to return any excess carried interest paid should the fund performance deteriorate in the later years of a fund term.

Limited Partner Protections

- Independent auditor testing
- Governance and rights in the limited partnership agreement
- SEC oversight
- Go-forward business concerns for a GP that maintains poor valuation practices
- Robust Cliffwater process for monitoring each fund and reviewing quarterly valuation changes

Cliffwater Disclosures

Important Notice

This presentation was prepared exclusively for information and discussion purposes, and is not meant to be, nor shall it be construed as, an attempt to define all information that may be material to you. All information including opinions or facts expressed herein are current as of the date appearing in this presentation and is subject to change without notice. All information has been obtained from sources believed to be reliable. No representation, warranty, or undertaking, express or implied, is given as to the accuracy or completeness of the information or opinions contained in this presentation. Past performance does not guarantee future performance.

This presentation may include sample or pro forma performance. Such information is presented for illustrative purposes only and is based on various assumptions, not all of which are described herein. Such assumptions, data, or projections may have a material impact on the returns shown.

References to market or composite indices (such as the S&P 500), benchmarks or other measures of relative market performance over a specified period of time (each, an "index") are provided for information only. Reference to an index does not imply that a portfolio will achieve returns, volatility or other results similar to the index. The composition of an index may not reflect the manner in which a portfolio is constructed in relation to expected or achieved returns, portfolio guidelines, restrictions, sectors, correlations, concentrations, volatility or tracking error targets, all of which are subject to change over time.

The S&P/LSTA U.S. Leveraged Loan Index is a market value weighted index tracking institutional leveraged loans in the United States based upon market weightings, spreads and interest payment, including Term Loan A, Term Loan B and Second Lien tranches.

The Bloomberg Barclays U.S. Corporate High Yield Index (Bloomberg Barclays High Yield) measures the USD-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below. Bonds from issuers with an emerging markets country of risk, based on the indices' EM country definition are excluded.

The Bloomberg Barclays U.S. Aggregate Index represents securities that are SEC-registered, taxable, and dollar denominated. The index covers the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities.

The NCREIF Property Index is a quarterly time series composite total rate of return measure of investment performance of a very large pool of individual commercial real estate properties acquired in the private market for investment purposes only. All properties in the index have been acquired, at least in part, on behalf of tax-exempt institutional investors.

The Cambridge Private Equity Index is based on data compiled from global institutional-quality buyout, growth equity, private equity energy, venture capital and mezzanine funds, including fully liquidated partnerships, formed between 1986 and 2016.

The Russell 3000 Index is a capitalization-weighted stock market index that seeks to track the entire U.S stock market. It measures the performance of the 3,000 largest publicly held companies incorporated in the United States based on market capitalization.

Select Topics in CERL Disability Retirement

- Burdens of Proof
- Board's Duty to Investigate
- Use of Medical Opinions
- Factors Affecting Volume of Applications

Presented by Ted M. Cabral
MercedCERA Disability Retirement Counsel
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(209) 491-7000

Overview of Key Substantive Issues:

<u>Permanent Incapacity Defined</u>:

A member is entitled to disability retirement if he/she is physically or mentally substantially and permanently disabled from the performance of his/her usual job duties.

<u>Service Connection Defined</u>:

A member is entitled to service-connected disability retirement if his/her permanent disability:

- Arose out of and occurred in the course of employment and
- The employment contributed substantially to the disability
- No requirement that the employment be the sole or majority cause of the disability
- But there must be a real and measurable connection between the disability and the employment

Burden of Proof

- Burden of Production
- Burden of Persuasion

Burden of Production

The applicant has the initial duty of presenting enough evidence to support a claim for disability retirement. This is the threshold for deeming an application "filed." Typical evidence includes

- The application itself
- A treating physician's statement
- A workers' compensation report
- Medical records

This is a very low threshold which does not involve consideration of opposing evidence.

Burden of Persuasion

This is the duty to persuade or convince the Board that a claim or defense meets the required legal standard. The party asserting the affirmative claim usually has the burden of proof/persuasion. For example,

- The applicant has the burden of proof regarding
  - permanent incapacity
  - service connection
- MercedCERA has the burden of proof on affirmative defenses such as
  - statute of limitations
  - doctrine of avoidable consequences

Effect of Presumptions

- Presumptions work by shifting the burden of proof regarding service connection from the applicant to the retirement association.
- If a presumption applies, a disability is deemed service connected unless the retirement system can prove that it is not service connected.
- Presumptions never affect the burden of proof regarding permanent incapacity.

Standard of Proof

- A "standard of proof" is the level of persuasion required to establish a claim.
- All issues in CERL applications are subject to a <u>"preponderance of the evidence"</u> standard of proof. This means that the probability that a claim is true is greater than 50%.

Board's Duty to Investigate Applications

Board’s Duty to Investigate

The Board has a duty to investigate applications to ensure that it only pays benefits to those members who are eligible to receive them. This means that the Board has a duty to investigate disability retirement applications . . .

- even when the initial application materials do not satisfy the applicant’s burden of proof, and
- even when the initial application materials appear to satisfy the applicant’s burden of proof.
- The extent of the investigation depends on the circumstances of each application

Use of Medical Opinions

Medical Opinions Are Usually Required

Medical opinions are necessary because some of the key issues relating to disability and service connection are beyond the knowledge of non-experts. For example,

- The applicant's medical/psychiatric diagnoses
- The prognoses for those conditions
- Whether the applicant has reached permanent and stationary status
- The applicant's permanent job restrictions
- The resulting disability, if any

When Medical Opinions Are Not Required

If the applicant’s condition, the cause of the condition, and the resulting disability are readily apparent to a non-expert, the Board may grant an application without the cost and delay of obtaining a formal medical opinion. For example,

- A nurse who loses the use of an arm is almost certainly permanently incapacitated.
- An attorney who loses his eyesight is almost certainly permanently incapacitated.
- An applicant undergoing chemotherapy for terminal cancer is almost certainly permanently incapacitated.

Sources of Medical Opinions

Medical opinions can be obtained from various sources. For example,

- Treating physician's statements (Readily available, but are often prepared by non-specialists whose opinions are not authoritative)
- Workers' compensation PQME reports (Usually authoritative and usually address permanent incapacity and service connection, but sometimes unavailable)
- Independent Medical Evaluations (IMEs) (Expensive, but sometimes necessary when other options are unavailable)
- Doctor depositions

Relying on Workers' Compensation Medical Reports

The Board may rely on medical reports prepared in corresponding workers' compensation cases if . . .

- The evaluation is conducted by an appropriately qualified specialist.
- The evaluating doctor has examined the applicant and reviewed all relevant evidence including medical records, test results, MRIs/X-rays, and personnel records when relevant.
- The report is recent. A report from several years ago does not reflect the applicant's current condition.
- The doctor's opinion must not be based on unsupported assumptions, improper legal theories, etc.

Evaluating Contradicting Medical Opinions

When there are contradicting medical opinions, the Board must decide which opinion is the most persuasive. Factors to consider include . . .

- Which opinion is most authoritative – i.e., which doctor is best qualified to opine on the disabling condition?
- Which opinion has the best foundation – i.e., has the doctor reviewed all the relevant records and personally evaluated the member?
- Which opinion is best supported by the evidence? (An "expert opinion is worth no more than the reasons upon which it rests.")

Conclusion and Questions