

Howard County Retirement Plan

Financial Statements
(With Supplementary Information)
and Independent Auditor's Report

June 30, 2015 and 2014

Howard County Retirement Plan

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Independent Auditor's Report

To the Retirement Plan Committee
Howard County Retirement Plan

Report on the Financial Statements

We have audited the accompanying financial statements of the Howard County Retirement Plan, which comprise the statements of fiduciary net position as of June 30, 2015 and 2014, and the related statements of changes in fiduciary net position for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Plan's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Plan's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the fiduciary net position of the Howard County Retirement Plan as of June 30, 2015 and 2014, and the changes in its fiduciary net position for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in note 2 to the financial statements, the Plan adopted GASB Statement No. 67, "Financial Reporting for Pension Plans" as of the fiscal year ended June 30, 2014. The related financial reporting requirements have been applied to the accompanying financial statements.

Required Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary schedules as of June 30, 2015, listed in the foregoing index, together referred to as "required supplementary information," are presented for the purpose of additional analysis and are not a required part of the financial statements but are supplementary information required by the Governmental Accounting Standards Board. Such information is the responsibility of the Plan's management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements, and, accordingly, we do not express an opinion or provide any assurance on it.



Baltimore, Maryland
November 24, 2015

Howard County Retirement Plan
Statements of Fiduciary Net Position
June 30, 2015 and 2014

	2015	2014
<u>Assets</u>		
Receivables		
Employer contributions	\$ 675,743	\$ 629,143
Member contributions	178,533	154,188
Interest and dividends	479,936	483,390
Due from sale of investments	414,061	4,420
Other	2,189	2,721
Total receivables	1,750,462	1,273,862
Investments, at fair value		
Equities	163,740,944	180,819,372
Alternative investments	69,177,971	41,699,078
Money market funds	5,969,835	6,561,920
Fixed income	98,295,250	96,271,166
Real estate funds	16,055,410	13,820,800
Total investments	353,239,410	339,172,336
Prepaid insurance	18,475	409
Total assets	355,008,347	340,446,607
<u>Liabilities</u>		
Investments purchased	245,988	580,566
Accounts payable	349,529	289,761
Total liabilities	595,517	870,327
Net position held in trust for pension benefits	\$ 354,412,830	\$ 339,576,280

See Notes to Financial Statements.

Howard County Retirement Plan

Statements of Changes in Fiduciary Net Position Years ended June 30, 2015 and 2014

	2015	2014
Additions		
Contributions		
Employer	\$ 13,967,304	\$ 12,778,495
Member	3,573,323	2,979,366
Total contributions	17,540,627	15,757,861
Investment income		
Net appreciation in fair value of investments	1,693,646	38,699,797
Interest	2,207,988	2,154,583
Dividends	7,209,286	6,192,061
Other, net	31,140	27,963
Total investment income	11,142,060	47,074,404
Less investment expense	1,158,785	1,118,661
Net investment income	9,983,275	45,955,743
Total additions	27,523,902	61,713,604
Deductions		
Benefit payments		
Annuities	11,900,255	10,486,109
Death	223,103	407,457
Refunds of contributions	252,397	245,692
Total benefits	12,375,755	11,139,258
Administration expenses	311,597	283,093
Total deductions	12,687,352	11,422,351
Net change	14,836,550	50,291,253
Net position held in trust for pension benefits		
Beginning of year	339,576,280	289,285,027
End of year	\$ 354,412,830	\$ 339,576,280

See Notes to Financial Statements.

Howard County Retirement Plan

Notes to Financial Statements June 30, 2015 and 2014

Note 1 - Plan description

Plan administration

The Howard County Retirement Plan (the "Plan") is a single-employer defined benefit public employee retirement system established and administered by Howard County, Maryland (the "County"), to provide defined pension benefits for those County employees who do not participate in other County and State plans. The Plan was established on July 1, 1995, at which time approximately 73% of the County's employees transferred from the State Retirement and Pension Systems of Maryland to the Plan. The Plan is considered part of the County's financial reporting entity and is included in the County's financial statements as a pension trust fund. The accompanying financial statements present only the operations of the Plan and are not intended to present the financial position and results of operations of the County.

Plan membership

At July 1, 2014 and 2013, the Plan's membership consisted of the following:

	<u>2014</u>	<u>2013</u>
Active	1,669	1,596
Retired and beneficiaries	556	506
Disabled	13	11
Terminated vested	191	189
	<u>2,429</u>	<u>2,302</u>

The Plan was established, is operated, and may be amended under the provisions of the Howard County Code, Sections 1.400 and 1.401 to 1.478. Essentially all of the County's full-time benefited and part-time benefited employees (excluding career firefighters and sworn police officers) are eligible to participate in the Plan, except for certain exceptions provided for in Howard County Code Section 1.406. The Retirement Plan Committee established by Howard County Code Section 1.455 has full power and authority to administer and operate the Plan in accordance with its terms and in particular the authority contained in subsection 1.454(a). The Pension Oversight Commission established by Howard County Section 1.482 provides ongoing assessment and evaluation of the Plan's operations.

Benefits provided

Under the Retirement Plan, participants become vested after five years of eligibility service and are entitled to a benefit beginning at age 62. If an employee leaves employment or dies before five years of eligibility service, accumulated employee contributions plus interest are refunded to the employee or designated beneficiary. A participant who becomes totally and permanently disabled may retire prior to normal retirement and receive a benefit. Both disability and death benefits vary if incurred in the line of duty.

Howard County Retirement Plan

Notes to Financial Statements June 30, 2015 and 2014

Participating general employees with thirty years of eligibility service, regardless of age, are entitled to a normal retirement benefit. Also, participants attaining the age of 62 and older who have completed between 2 to 5 years of eligibility service (for a total of 67) may retire and receive unreduced benefits. For creditable service earned prior to June 30, 2012, the benefit is 1.55% of the participant's average compensation times the participant's creditable service; for creditable service after July 1, 2012, the multiplier is 1.66%. The Plan permits early retirement for participants who attain the age of 55 with at least 15 years of Eligibility Service or have 25 years of eligibility service, regardless of age. For early retirement, the benefit is reduced by 0.5% for each month that the benefit begins prior to normal retirement date.

For participating AFSCME Local 3085 the benefit is 1.66% of the participants average compensation times all years of creditable service.

Participating Corrections employees are entitled to receive a normal retirement benefit of 2.5% of average compensation multiplied by years of creditable service (up to 20 years) plus 1.0% of average compensation multiplied by creditable service greater than 20 years but less than 30 years (excluding sick leave, which is always credited at 1.0% of average compensation). Different rules are applied to employees who retired before July 1, 2005.

Annually, the benefits are adjusted for cost of living adjustment ("COLA"). The Plan uses the Consumer Price Index ("CPI-U") for the Washington/Baltimore area as published by the Bureau of Labor Statistics to calculate the change in retiree allowances each July. Maximum annual COLA is 3%.

Contributions

The Plan is authorized to establish or amend the obligation to make contributions under the provisions of Sections 1.423 and 1.465 of the Howard County Code. The Plan's funding policy provides for periodic employer contributions at actuarially determined rates that, expressed as percentages of annual covered payroll, are sufficient to accumulate sufficient assets to pay benefits when due. Participant contributions are 8.5% of base pay for participating Corrections employees with less than 20 years of creditable service, 0% of base pay for participating Correction employees with greater than 20 years of creditable service and effective January 1, 2014, 3% of base pay for other participants. The County funds the remainder of the cost of employees' participation in the Plan which was 13.5% and 13.1% of covered payroll in fiscal years 2015 and 2014, respectively. The County contribution is determined through an actuarial valuation performed by Bolton Partners, Inc. for each fiscal year. Expenses incurred in the administration and operation of the Plan are funded by the Plan.

Note 2 - Summary of significant accounting policies and plan asset matters

Method used to value investments

The Plan's investments are reported at fair market value. Short-term investments consisting of money market funds are reported at cost, which approximates fair value. Securities traded on a national or international exchange are valued at either the last reported sales price, evaluated bid, broker quoted, or pool-specific pricing. The fair value

Howard County Retirement Plan

Notes to Financial Statements June 30, 2015 and 2014

of real estate investments is approximated by the net asset value of the Plan's share of ownership of the co-mingled real estate investment funds. Fair value of other securities is determined by the mean of the most recent bid and asked prices as obtained from dealers that make markets in such securities.

Basis of accounting

The Plan's financial statements are prepared using the accrual basis of accounting. Employer and employee contributions are recognized as revenue in the period in which employee services are performed and expenses and refunds are recorded when the corresponding liabilities are incurred, regardless of when payment is made. Benefits are recorded when the payments are made.

Use of estimates

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

Income taxes

The Internal Revenue Service issued a determination letter on June 27, 2012, which stated that the Plan and its underlying trust qualify under the applicable provisions of the Internal Revenue Code and therefore are exempt from Federal income taxes. Although the Plan has been amended since receiving the determination letter, in the opinion of the Plan administrator, the Plan and its underlying trust are designed and are being operated in compliance with the applicable provisions of the Internal Revenue Code; therefore, the Plan is qualified and the related trust is tax exempt.

Recently issued accounting pronouncements

In June 2012, the GASB issued Statement No. 67, "Financial Reporting for Pension Plans" ("GASB No. 67") and Statement No. 68, "Accounting and Financial Reporting for Pensions" ("GASB No. 68") to improve financial reporting by state and local governmental pension plans administered through trusts that meet the specified criteria and to improve accounting and financial reporting by state and local governments for pensions, respectively.

GASB No. 67 amends the previous standards (GASB No. 25, "Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans" and GASB No. 50, "Pension Disclosures") for pension plans administered through trusts or equivalent arrangements that meet the specified criteria by revising the financial statements presentation for pension plans, specifying the required approach to measuring the pension liability of employers and non-employer contributing entities for benefits provided through pension plans (the net pension liability) and stipulating incremental note disclosures and RSI in the separately issued financial reports for pension plans. The Plan adopted GASB No. 67 as of fiscal year ended June 30, 2014 and has applied the related changes to the accompanying financial statements.

Howard County Retirement Plan

Notes to Financial Statements June 30, 2015 and 2014

GASB No. 68, which is effective for fiscal years beginning after June 15, 2014, amends the previous standards (GASB No. 27, "Accounting for Pensions by State and Local Governmental Employers," and GASB No. 50, "Pension Disclosures") for employers with defined benefit pension plans by requiring employers to shift from a "funding approach," in which pension liability is not reported if employers make the annual required contribution, to an "earnings approach," where pension liability is reported as employees earn their pension benefits and changes in pension liability are recognized immediately as pension expense or as deferred outflows/inflows of resources to be amortized over future periods by establishing the standards for measuring and recognizing Net Pension Liability, identifying the methods and assumptions that should be used to determine Total Pension Liability and stipulating incremental note disclosures and RSI in the financial reports for employers with defined benefit pension plans.

Subsequent events

Material subsequent events have been considered for disclosure and recognition in these financial statements through November 24, 2015 (the date the financial statements were available to be issued).

Note 3 - Investments

Investment policy

The Plan's policy in regard to the allocation of invested assets is established and administered by the Retirement Plan Committee. Specific investment goals stated in the policy shall be reviewed at least annually and, when appropriate, new goals and standards shall be adopted by the Retirement Plan Committee. The policy is expected to provide diversification of assets in an effort to maximize investment return to the Plan consistent with prudent market and economic risk. All of the Plan's assets are to remain invested at all times in the asset classes as designated by the policy. The following strategic asset allocation policy was adopted by the Plan on March 21, 2002, last amended on February 26, 2015 and remained in effect as of June 30, 2015:

<u>Asset Class</u>	<u>Target Allocation</u>
Equities	40.0%
Alternative investments	22.5%
Fixed income	30.0%
Real estate funds	<u>7.5%</u>
Total	<u><u>100.0%</u></u>

Concentrations

The Plan held investments in the following organizations that represent 5% or more of the pension plan's fiduciary net position: Blackstone (6%), Dimensional (7%), Dodge and Cox (15%), Invesco (7%), LSV (7%), Magnitude (6%), Mondrian (5%), PIMCO (11%), Pyramid (8%) and Westfield (7%).

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Notes to Financial Statements June 30, 2015 and 2014

Concentration of credit risk

The Plan's investment policy does not establish any limitation on the percentage that the Plan may have with any one issuer, other than to state that the Plan's assets are to be diversified in accordance with Modern Portfolio Theory. At June 30, 2015, the Plan had 7% of its investments in corporate bonds.

Rate of return

For the year ended June 30, 2015, the annual money-weighted rate of return on pension plan investments, net of pension plan investment expense, was 2.95%. The money-weighted rate of return expresses investment performance, net of investment expense, adjusted for the changing amount actually invested.

Investments purchased and due from sales of investments

Investment transactions are recorded on a trade plus three days or less timetable resulting in an amount due to and due from State Street Bank (the "Plan's Trustee") at year end.

Risks and uncertainties

The Plan invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect participants' account balances and the amounts reported in the statements of fiduciary net position.

Note 4 - Net pension liability of the County

The components of the net pension liability of the County at June 30, 2015, were as follows:

Total pension liability	\$ 394,134,559
Plan fiduciary net position	354,412,830
County's net pension liability	<u>\$ 39,721,729</u>
Plan fiduciary net position as a percentage of the total pension liability	89.92%

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Notes to Financial Statements June 30, 2015 and 2014

Actuarial assumptions

The total pension liability in the July 1, 2014 actuarial valuation rolled forward to June 30, 2015 was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	2.75 percent
Salary increases	Varies by service, 4.00 to 6.75 percent, including inflation
Investment rate of return	7.50 percent, net of pension plan investment expense, including inflation
Mortality	RP-2000 Combined Healthy tables with generational projection by Scale AA

The actuarial assumptions used in this valuation, for GASB 67 purposes, were generally based on the 2014 Experience Study covering the period from July 1, 2009 through June 30, 2013. Other economic assumptions and the demographic assumptions were updated to reflect the 2009-2013 experience study.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation.

Best estimates of geometric real rates of return for each major asset class, included in the Plan's target allocation as of June 30, 2015 (see note 3), are summarized in the following table:

<u>Asset Class</u>	<u>Long-Term Expected Real Rate of Return</u>
Equities	4.89%
Alternative investments	5.33%
Fixed income	2.63%
Real estate funds	5.67%

Discount rate

The discount rate used to measure the total pension liability was 7.50%. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current contribution rate and that the County contributions will be made at rates equal to the difference between actuarially determined contribution rates and the employee rate. Based on those assumptions, the Plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension

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**Notes to Financial Statements
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liability. The discount rate was reduced from 7.75% to 7.50% for fiscal year ended June 30, 2015.

Sensitivity of the net pension liability to changes in the discount rate

The following presents the net pension liability of the County, calculated using the discount rate of 7.50%, as well as what the County's net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (6.50%) or 1 percentage point higher (8.50%) than the current rate:

	<u>1% Decrease (6.50%)</u>	<u>Current Discount Rate (7.50%)</u>	<u>1% Increase (8.50%)</u>
County's net pension liability	<u>\$ 91,929,317</u>	<u>\$ 39,721,729</u>	<u>\$ (3,923,181)</u>

Required Supplementary Information

Howard County Retirement Plan

Required Supplementary Information

Schedule of Changes in the County's Net Pension Liability and Related Ratios (Dollar amounts in thousands) June 30, 2015 and 2014

	FY 2015	FY 2014*
Total pension liability		
Service cost	\$ 14,073	\$ 12,727
Interest	27,198	24,974
Change of benefit terms	-	3,534
Difference between expected and actual experience	(2,741)	-
Changes of assumptions	(851)	10,918
Benefit payments - including refunds of member contributions	(12,375)	(11,139)
Net change in total pension liability	25,304	41,014
Total pension liability - beginning	368,831	327,817
Total pension liability - ending	\$ 394,135	\$ 368,831
Plan fiduciary net position		
Contributions - employer	\$ 13,967	\$ 12,778
Contributions - member	3,573	2,979
Net investment income	9,983	45,956
Benefit payments - including refunds of member contributions	(12,375)	(11,139)
Administrative expenses	(311)	(283)
Other	-	-
Net change in plan fiduciary net position	14,837	50,291
Plan fiduciary net position - beginning	339,576	289,285
Plan fiduciary net position - ending	\$ 354,413	\$ 339,576
County's net pension liability - ending	\$ 39,722	\$ 29,255
Plan fiduciary net position as a percentage of the total pension liability	89.92%	92.07%
Total covered employee payroll (FY 2015)	\$ 108,049	\$ 100,883
County's net pension liability as a percentage of covered employee payroll	36.76%	29.00%
Expected average remaining service years of all participants	7	7

Notes to Schedule

Benefit Changes: For General employees not in AFSCME Local 3085 Employees, the multiplier was changed from 1.55% to 1.66% for service earned after June 30, 2012. The Employee contribution percentage was raised from 2.0% to 3.0% effective January 1, 2014.

* Information for FY 2013 and earlier is not available

See Independent Auditor's Report.

Howard County Retirement Plan
Required Supplementary Information

Schedule of County Contributions
(Dollar amounts in thousands)
June 30, 2015 and 2014

	FY 2015	FY 2014
Actuarially determined contribution	\$ 13,967	\$ 12,778
Contributions in relation to the actuarially determined contribution	13,967	12,778
Contribution deficiency (excess)	\$ -	\$ -
Covered-employee payroll ¹	\$ 108,049	\$ 100,883
Contributions as a percentage of covered-employee payroll ¹	12.93%	12.67%

¹Amounts shown are based on total compensation and not just pensionable earnings only.

Notes to Schedule

Valuation Date:

The actuarial valuation date is the beginning of the fiscal year (July 1, 2014).

Methods and assumptions used to determine contribution rates for fiscal year 2015:

Actuarial cost method	Projected Unit Credit (Entry Age used for GASB 67 purposes)
Amortization method	Level percent of pay increasing 2.75% per year
Remaining amortization period	From 8 to 25 years
Asset valuation method	5-year smoothed market
Inflation	2.75%
Salary increases	4.00% to 6.75%, including inflation
Investment rate of return	7.50%, net of pension plan investment expense, including inflation
Retirement age	Rates vary by participant age and service
Mortality	RP-2000 Combined Healthy tables with generational projection by Scale AA
Cost of Living Adjustment	2.75%

Howard County Retirement Plan
Required Supplementary Information
Schedule of Investment Returns
June 30, 2015 and 2014

<u>Fiscal Year Ended</u>	<u>Annual money-weighted rate of return, net of investment expenses</u>
June 30, 2015	2.95%
June 30, 2014	15.62%
June 30, 2013	11.33%
June 30, 2012	-1.21%
June 30, 2011	20.56%
June 30, 2010	15.42%
June 30, 2009	-16.21%
June 30, 2008	-14.44%
June 30, 2007	17.62%
June 30, 2006	12.19%