

# Comprehensive Annual Financial Report Maryland State Retirement and Pension System



A Pension Trust Fund of the State of Maryland

For the Years Ended June 30, 2019 and 2018

*Prepared by:*

Maryland State Retirement Agency  
120 East Baltimore Street  
Baltimore, Maryland 21202

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**STATE RETIREMENT AGENCY**

120 East Baltimore Street  
Baltimore, MD 21202-6700

MARYLAND  
STATE RETIREMENT  
and PENSION SYSTEM

410-625-5555 • 1-800-492-5909  
TTY Users: call via Maryland Relay  
sra.maryland.gov

December 15, 2019

Dear Members, Retirees and Beneficiaries:

On behalf of the Board of Trustees, we are pleased to present the Comprehensive Annual Financial Report of the Maryland State Retirement and Pension System for the fiscal year ended June 30, 2019. This report provides information on the financial status of the Retirement System during a period when the System issued approximately \$332 million in average monthly payments to nearly 165,000 retirees and beneficiaries.

The Board's fundamental mission is to ensure that retirement benefits are paid in full, and in an accurate and timely manner. The Board oversees the investment of the Maryland State Retirement and Pension System assets in order to ensure the funding necessary to meet those obligations.

The pension fund realized modest gains in fiscal 2019, earning 6.46 percent for the year, falling short of the plan's 7.45 percent assumed actuarial return rate. Even so, the fund's performance raised the assets of the System to \$54.2 billion, an increase of \$2.3 billion over the previous fiscal year.

While the focus will typically be on investment returns, the Board recognizes that the management of risk is equally important in the investment of plan assets. History has shown that returns will vary from year to year, at times by wide margins. The Board has adopted investment policies designed to minimize the downside impact of such volatility on the value of System assets, while still capturing significant value when markets are strong.

Reforms enacted by the Maryland General Assembly in 2011 and in subsequent years continue to show positive results for the System and, in fact, continue to exceed earlier projections. Required employer contributions for the coming fiscal year of 2021 are projected to be 17.75% of payroll, significantly lower than the 19.35% predicted at the time of the 2011 reforms. As of June 30, 2019, the System's funded ratio is 72.9%, higher than the 71.7% predicted at the same time. The System is on track to be 80% funded by 2026; 85% funded by 2030; and 100% funded by 2039.

Your Retirement System remains administratively and financially sound. As a participant in the System, you can remain confident that your pension benefits are secure. As always, your commitment to and involvement in the concerns of the System are greatly appreciated. We value your input—this is your System. If you have any questions, please do not hesitate to contact us.

Sincerely,

NANCY K. KOPP  
*Chairman*

PETER FRANCHOT  
*Vice Chairman*

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**BOARD OF TRUSTEES**

Nancy K. Kopp, *Chairman*  
David R. Brinkley  
Eric D. Brotman  
Jamaal R. A. Craddock

Kenneth B. Haines  
David B. Hamilton

Linda A. Herman  
Sheila Hill

F. Patrick Hughes  
Charles W. Johnson

Peter Franchot, *Vice Chairman*  
Richard E. Norman  
Douglas Prouty  
Michael J. Stafford, Jr.

---

R. Dean Kenderdine, *Secretary to the Board*

Maryland State Retirement and Pension System



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Baltimore, MD 21202-6700

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## LETTER OF TRANSMITTAL

December 15, 2019

We are pleased to submit the Comprehensive Annual Financial Report for the Maryland State Retirement and Pension System for the fiscal year ended June 30, 2019. We believe this report fairly presents the operating results achieved during this 12-month reporting period.

The System is responsible for properly administering retirement, disability, and death benefits. At the same time, it strives to keep employer contribution rates as reasonable as possible by maximizing investment returns while maintaining an acceptable level of risk. Members covered by the plans include state employees, teachers, law enforcement officers, legislators, judges, as well as local government employees and correctional personnel whose employers have elected to participate in the System.

The System currently provides monthly allowances to nearly 165,000 retirees and beneficiaries, and is an essential element of the future financial security for more than 193,000 active participating members. Descriptions of the membership requirements and benefits provided by each plan administered by the System are included in the Plan Summary Section starting on page 136.

This Comprehensive Annual Financial Report contains six sections. The Introductory Section provides information about the administrative structure of the System. The Financial Section provides a comprehensive review of the System's financial position, the results of its operations and its funded status. It also contains the report from the System's independent auditor, the combined financial statements and supplementary financial data. The Investment Section includes a report highlighting the System's investment performance in addition to various summary level portfolio compositions and other investment data. The Actuarial Section contains the independent actuary's report on the results of the System's annual actuarial valuation. The Statistical and Plan Summary Sections provide demographic composition of the System's membership segments affected by each plan and detailed descriptions of the various plans' provisions. In addition to this Letter of Transmittal, additional narrative, overview, and analysis can be found in Management's Discussion and Analysis beginning on page 18.

## INVESTMENTS

The System's investment portfolio returned 6.46 percent (money-weighted net of fees) on investments for the fiscal year 2019—falling short of the 7.45 percent assumed actuarial return rate and the plan's policy benchmark of 7.09 percent. After the payment of benefits, the market value of invested assets increased by roughly \$2.3 billion from \$51.9 billion on June 30, 2018 to \$54.2 billion on June 30, 2019.

The System's long-term target asset allocation is comprised of 37 percent public equities, 19 percent rate sensitive assets, 13 percent private equities, 9 percent credit/debt strategies, 14 percent real assets, and 8 percent absolute return. The System's portfolio is balanced across several asset and sub-asset classes and is globally diversified. This, coupled with a long term investment horizon, provides the System with greater protection during short-term market volatility.

## FINANCIAL INFORMATION

System management has committed the resources necessary to maintain an internal control structure that provides reasonable assurance that assets are adequately safeguarded, financial records are consistently and accurately maintained, and transactions are properly executed to permit preparation of financial statements in accordance with generally accepted accounting principles. The System's internal control structure includes written policies and procedures and an internal audit division that reports to the Board.

### ACCOUNTING SYSTEM AND REPORTS

The System reports its transactions on the accrual basis of accounting. Under this method, revenues are reported in the accounting period they are earned and become measurable, and expenses are reported when the related liability is incurred and measurable. Investments are reported at fair value at fiscal year-end. Investment purchases and sales are reported in the accounting period in which the related trade dates occur.

### REVENUES

The reserves necessary to finance retirement allowances and other benefits are accumulated through investment earnings and the collection of employer and member contributions. During fiscal year 2019, investment earnings were \$3.6 billion, while revenues from employer and member contributions were \$2.05 billion and \$807.3 million, respectively. For fiscal year 2019, member contribution rates on average were 7 percent, while employer rates varied depending on the System.

### EXPENSES

The System's expenses consist of monthly retirement allowances, refunds of contributions to terminated and transferring members, withdrawing employers, and the administrative cost of System operations. Payments to retirees, beneficiaries and transferring or withdrawing members and employers continued to be the System's primary disbursements during FY2019, totaling \$4.0 billion. In addition, the System disbursed \$409.9 million to manage the investment portfolio and to administer the System, of which \$370.1 million was paid for investment management and \$39.8 million was used to fund the System's administrative operations.

## FUNDING

Funds are derived from the excess of additions, which include contributions and investment earnings, over deductions, which are comprised of benefits and administrative expenses. Funds are accumulated to meet future benefit obligations to retirees and beneficiaries. This accumulated balance is referred to as the "net assets held in trust for pension benefits" in the Statement of Plan Net Position in the Financial Section of this report. The Net Pension Liability (NPL) is not disclosed in the basic financial statement but is disclosed in note nine to the basic financial statements. The funded status schedule presented in Other Supplemental Information shows the actuarial value of assets, which is based on a five-year smoothed expected rate of return, wherein the excess or shortfall of investment income over or under the actuarial assumed income of 7.45 percent is recognized over a five-year period. This is the value of assets used by the actuary in determining contribution rates for the Systems as disclosed in note five to the basic financial statements.

The actuarial accrued liability of the Systems is also determined by the actuary. It is a measure of the present value of actuarial accrued liabilities estimated to be payable in the future to current retirees, beneficiaries and employees for service earned to date. The percentage computed by dividing the actuarial value of net assets available for benefits by the actuarial accrued liability is generally referred to as the "funded ratio." This ratio provides an indication of the funded status of the System on a going-concern basis and generally, the greater this percentage, the stronger the System. The System's funded ratio increased from 72.5 percent at June 30, 2018 to 72.9 percent at June 30, 2019.

At June 30, 2019, the System's actuarial accrued assets and liability were \$54.4 billion and \$74.5 billion, respectively. The unfunded actuarial accrued liability totaled \$20.1 billion, resulting in a funded status ratio of 72.9 percent. The unfunded actuarial accrued liability is being amortized over a closed 25-year period.

### PROFESSIONAL SERVICES

The System contracts for the services of various independent consulting, investment advisory and financial professionals to assist the Board of Trustees in carrying out its fiduciary responsibility to efficiently and effectively manage the System. Actuarial services were provided by Gabriel Roeder Smith & Company and independent financial statement audit services were provided by SB & Company, LLC. The System's asset custody and portfolio accounting services were provided by the State Street Bank & Trust Company under a multi-year, master custody arrangement. Meketa Investment Group, Inc. served as the System's general investment consultant. Specialty

consulting services were provided by Mercer Investments, LLC for private equity and Townsend Holdings, LLC for real estate. Aksia, LLC advises staff on the retirement System's Absolute Return portfolio. A complete listing of the System's professional consultants and external investment advisors is presented on page 11.

#### AWARDS

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the Maryland State Retirement and Pension System for its Comprehensive Annual Financial Report for the fiscal year ended June 30, 2018. This was the thirtieth consecutive year (1989 through 2018) that it has received this prestigious award. In order to be awarded a Certificate of Achievement, a governmental unit must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current comprehensive annual financial report continues to meet the Certificate of Achievement Program's requirements, and we are submitting it to the GFOA to determine its eligibility for another certificate.

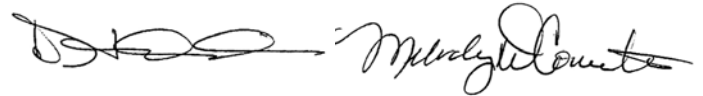
Additionally, the Maryland State Retirement and Pension System received the Public Pension Coordinating Council's (PPCC) 2019 Recognition Award for meeting professional standards for plan funding and administration, as set forth in the Public Pension Standards.

The PPCC is a coalition of associations that represent public pension funds that cover the vast majority of public employees in the U.S., including the National Association of State Retirement Administrators (NASRA), the National Council on Teacher Retirement (NCTR), and the National Conference on Public Employee Retirement Systems (NCPERS).

The Public Pension Standards are intended to reflect expectations for public retirement Systems management and administration, and serve as a benchmark by which all defined benefit public plans should be measured. The Maryland State Retirement and Pension System is proud to be a recipient of this award.

#### ACKNOWLEDGMENTS

This annual report reflects the dedicated efforts of the System's staff under the steady direction of the Board of Trustees. We extend our sincere gratitude to each member of the Board, the System's staff, the Board's advisors and the many people who worked with diligence and dedication throughout fiscal year 2019. Special thanks go to the members of the Maryland State Retirement Agency's senior executive team and the agency's staff of professional and para-professionals who helped to gather and prepare the information for this report.



R. Dean Kenderdine  
*Executive Director  
Secretary to the Board*

Melody Countess, CPA, CGMA  
*Chief Operating Officer*

## BOARD OF TRUSTEES



NANCY K. KOPP, *Chairman*  
State Treasurer  
Ex Officio since February 14, 2002  
Member, Administrative Committee  
Member, Corporate Governance Committee  
Member, Investment Committee



PETER FRANCHOT, *Vice Chairman*  
State Comptroller  
Ex Officio since January 22, 2007  
Member, Investment Committee



DAVID R. BRINKLEY  
Ex Officio since January 21, 2015  
Member, Administrative Committee  
Member, Corporate Governance Committee  
Member, Investment Committee



ERIC D. BROTMAN  
January 19, 2016 - June 30, 2023  
Member, Investment Committee



JAMAAL R. A. CRADDOCK  
June 19, 2018 - July 31, 2021  
Member, Audit and Securities Litigation Committee  
Member, Investment Committee



KENNETH B. HAINES  
August 1, 2019 - July 31, 2023  
Vice Chairman, Administrative Committee  
Member, Investment Committee



DAVID B. HAMILTON  
August 5, 2016 - July 31, 2020  
Chairman, Audit and Securities Litigation Committee  
Member, Investment Committee



LINDA A. HERMAN  
August 1, 2013 - June 30, 2023  
Vice Chairman, Investment Committee



## BOARD OF TRUSTEES



**SHEILA HILL**  
August 1, 2015 – July 31, 2023  
Chairman, Corporate Governance Committee  
Member, Administrative Committee  
Member, Investment Committee



**F. PATRICK HUGHES**  
April 20, 2004 – June 30, 2021  
Chairman, Investment Committee  
Member, Audit and Securities Litigation Committee



**CHARLES W. JOHNSON**  
January 14, 2016 – Present  
Vice Chairman, Corporate Governance Committee  
Member, Investment Committee



**RICHARD E. NORMAN**  
August 1, 2014 – July 31, 2022  
Chairman, Administrative Committee  
Vice Chairman, Audit and Securities Litigation Committee  
Member, Investment Committee



**DOUGLAS PROUTY**  
August 1, 2017 – July 31, 2021  
Member, Administrative Committee  
Member, Corporate Governance Committee  
Member, Investment Committee



**MICHAEL J. STAFFORD, JR.**  
October 26, 2017 – Present  
Member, Audit and Securities Litigation Committee  
Member, Investment Committee

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## ADVISORS TO THE INVESTMENT COMMITTEE



**MICHAEL K. BARRY**



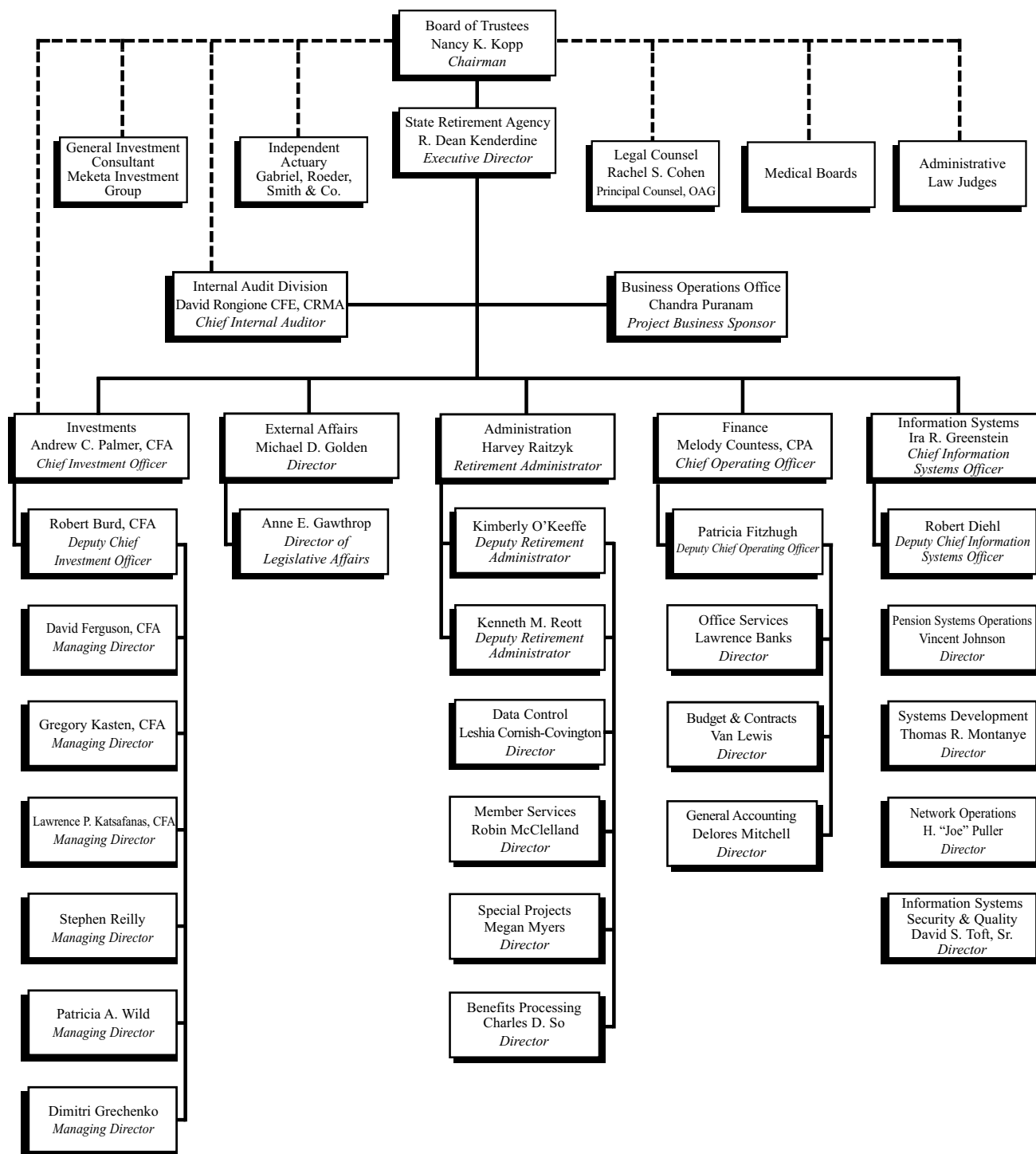
**STEPHEN M. KITSOULIS**



**MONTE TARBOX**

## ORGANIZATIONAL CHART

(November 2019)



\*Additional information regarding investment professionals who provide services to the System can be found on pages 11, and 88-89.

PROFESSIONAL SERVICES

**Global Custodial Bank and Security Lending**

State Street Bank & Trust Company  
Boston, Massachusetts

**Hearing Officers**

Office of Administrative Hearings  
Baltimore, Maryland

**Independent Actuary**

GRS Retirement Consulting  
Southfield, Michigan

**Independent Public Accountant**

SB & Company, LLC  
Owings Mills, Maryland

**Independent Investment Consultants**

Mercer Investments, LLC  
Boston, Massachusetts

Meketa Investment Group, Inc.  
Westwood, Massachusetts

Townsend Holdings, LLC  
Cleveland, Ohio

Aksia, LLC  
New York, New York

**Operational Banking Services**

M & T Bank  
Baltimore, Maryland

The Harbor Bank of Maryland  
Baltimore, Maryland



Government Finance Officers Association

**Certificate of  
Achievement  
for Excellence  
in Financial  
Reporting**

Presented to

**Maryland State  
Retirement and Pension System**

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended

**June 30, 2018**

*Christopher P. Morrell*

Executive Director/CEO



Public Pension Coordinating Council

***Public Pension Standards Award  
For Funding and Administration  
2019***

Presented to

**Maryland State Retirement and Pension System**

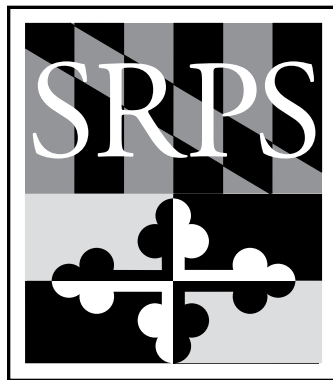
In recognition of meeting professional standards for  
plan funding and administration as  
set forth in the Public Pension Standards.

*Presented by the Public Pension Coordinating Council, a confederation of*

National Association of State Retirement Administrators (NASRA)  
National Conference on Public Employee Retirement Systems (NCPERS)  
National Council on Teacher Retirement (NCTR)

A handwritten signature in black ink, reading 'Alan H. Winkle'. The signature is fluid and cursive, with the first name 'Alan' and last name 'Winkle' clearly distinguishable.

Alan H. Winkle  
Program Administrator



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