

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, 2020 and 2019

Prepared by:

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

INTRODUCTORY SECTION:

Message from the Board	4
Letter of Transmittal	5
Board of Trustees	8
Public Advisors to the Investment Committee	9
Organizational Chart	10
Professional Services	11
Certificate of Achievement	12
Recognition Award for Administration	13

FINANCIAL SECTION:

Report of Independent Public Accountants	16
Management's Discussion and Analysis	18
Financial Statements:	
Statements of Fiduciary Net Position	24
Statements of Changes in Fiduciary Net Position	25
Notes to the Financial Statements	26
Required Supplementary Information:	
Schedule of Changes in Employers' Net Pension Liability	48
Schedule of Employers' Net Pension Liability and Related Ratios.....	62
Schedule of Employers' Contributions and Related Ratios.....	64
Schedule of Investment Returns	66
Notes to Required Supplementary Information	67
Other Supplementary Information:	
Schedule of Funding Progress	69
Schedule of Contributions from Employers and Other Contributing Entity.....	70
Fund Balance Accounts	70
Schedule of Fund Balances	71
Schedule of Administrative Expenses	72
Schedule of Investment Expenses	73
Schedule of Fiduciary Net Position by System	74
Schedule of Changes in Fiduciary Net Position by System	76

INVESTMENT SECTION:

Chief Investment Officer's Report	80
Investment Portfolio Summary	88
Investment Portfolios by Manager	89
Investment Relationship Listings	90
Terra Maria Program.....	92
Equity Relationship Listing.....	92
Equity Commissions to Brokers	93
Largest Stock & Bond Holdings at Market.....	94
Investment Portfolio Allocation	95
Comparative Investment Returns:	
Domestic Equity	96
Private Equity	96
International Developed Equity	97

Real Estate	97
Rate Sensitive	98
Total Plan	98
Ten-Year History of Time-Weighted Annual Returns	99
Ten-Year Growth of Investment Portfolio	99

ACTUARIAL SECTION:

Independent Actuary's Certification Letter	102
Summary of Valuation Results	106
Summary of Unfunded Actuarial Liabilities/Solvency Test	112
Summary of Retirees and Beneficiaries Added to and Removed from Rolls	112
Accounting Statement Information	114
Summaries of Principal Results	116
Schedule of Active Membership Valuation Data by Plan	122

STATISTICAL SECTION:

Statistical Section Overview	126
Ten-Year History of Changes in Net Positions	127
Schedule of Benefit Expense by Type	127
Schedule of Refund Expense by Type.....	127
Ten-Year History of Average Benefit Payments	128
Ten-Year History of Funding Progress	129
Ten-Year History of Employer Contribution Rates by Plan	129
Schedule of Retired Members by Type of Retirement and Option Selected	130
Ten-Year History of Active Membership by Plan	132
Total System Active Membership	132
Active Membership in Teachers' Plans	132
Active Membership in Employees' Plans	132
Ten-Year History of Retirees and Beneficiaries by Plan	133
Total System Retirees and Beneficiaries	133
Ten-Year History of Revenues by Source and Expenses by Type	134
Ten-Year History of Revenues vs. Expenses	135
Principal Participating Employers	135
Governmental Units Participating in the Systems	136
Withdrawn Governmental Units	136

PLAN SUMMARY SECTION:

Teachers' Retirement System	138
Teachers' Pension System	141
Employees' Retirement System	145
Correctional Officers' Retirement System.....	149
Legislative Pension Plan	152
Employees' Pension System	154
State Police Retirement System	159
Judges' Retirement System	163
Law Enforcement Officers' Pension System	165



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, 2020

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, 2020. This report provides information on the financial status of the Retirement System during a period when the System issued approximately \$351 million in average monthly payments to nearly 168,00 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 2020, earning 3.57 percent for the year, reflecting the ongoing impact of the COVID-19 pandemic on global markets. Although the fiscal year earnings fell short of the System's 7.40% assumed actuarial return rate, it exceeded the policy benchmark of 3.14% by 43 basis points. The policy benchmark is a standard for comparing a portfolio's performance in the market from which the manager selects securities. The fund's performance raised the system's managed assets to \$54.8 billion, an increase of \$562 million over last 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 or match projections made at the time of the reforms. Required employer contributions for the coming fiscal year of 2021 are projected to be 17.50% of payroll, significantly lower than the 19.86% predicted at the time of the 2011 reforms. As of June 30, 2020, the System's funded ratio is 72.9%, close to the 73.0% predicted at the same time, yet higher than 72.2% reported last year. The System remains 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
Chair

PETER FRANCHOT
Vice Chair

BOARD OF TRUSTEES

Nancy K. Kopp, *Chair*
Thomas M. Brandt
David R. Brinkley
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R. Dean Kenderdine, *Secretary to the Board*

Maryland State Retirement and Pension System



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120 East Baltimore Street
Baltimore, MD 21202-6700

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STATE RETIREMENT
and PENSION SYSTEM

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LETTER OF TRANSMITTAL

December 15, 2020

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, 2020. 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 168,000 retirees and beneficiaries and is an essential element of the future financial security for more than 196,000 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 138.

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 3.57 percent on investments, net of fees, for the fiscal year 2020—falling short of the 7.40 percent assumed actuarial return rate but exceeding the plan's policy benchmark of 3.14 percent by 43 basis points. After the payment of benefits, the market value of managed assets increased by \$563 million from \$54.2 billion on June 30, 2019 to \$54.8 billion on June 30, 2020.

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 2020, investment earnings were \$2.2 billion, while revenues from employer and member contributions were \$2.14 billion and \$850.3 million, respectively. For fiscal year 2020, member contribution rates on average were seven 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 FY 2020, totaling \$4.2 billion. In addition, the System disbursed \$403.1 million to manage the investment portfolio and to administer the System, of which \$361.8 million was paid for investment management and \$41.3 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 "Fiduciary Net position restricted for pension" in the Statement of Fiduciary 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 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 7.40 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 72.9 percent at June 30, 2019 to 73.6 percent at June 30, 2020.

At June 30, 2020 the System's actuarial accrued assets and liability were \$56.2 billion and \$76.5 billion, respectively. The unfunded actuarial accrued liability totaled \$20.2 billion, resulting in a funded status ratio of 73.6 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 Clifton Larson Allen, LLP. 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 Hamilton Lane Advisors, LLC, for private equity services 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, 2019. This was the thirty-first consecutive year (1989 through 2020) 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.

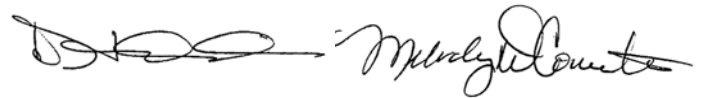
Additionally, the Maryland State Retirement and Pension System received the Public Pension Coordinating Council's (PPCC) 2020 Recognition Award for meeting professional standards for plan funding and administration, as set forth in the Public Pension Standards.

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 2020. Special acknowledgment and thanks is also extended to the members of the Maryland State Retirement Agency's senior executive team and the agency's staff of professional and paraprofessionals 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, *Chair*
State Treasurer
Ex Officio since February 14, 2002
Member, Administrative Committee
Member, Corporate Governance Committee
Member, Investment Committee



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



THOMAS M. BRANDT, JR.
May 7, 2020 - July 31, 2023
Member, Administrative Committee
Member, Audit and Securities Litigation 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
Chairman, Investment Committee



JAMAAL R. A. CRADDOCK
June 19, 2018 - July 31, 2021
Member, Administrative Committee
Member, Investment Committee



JAMES P. DALY, JR.
September 11, 2020 - June 30, 2021



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

BOARD OF TRUSTEES



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August 5, 2016 - July 31, 2024
Chairman, Audit and Securities Litigation Committee
Member, Corporate Governance Committee



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



SHEILA HILL
August 1, 2015 - July 31, 2023
Chairman, Corporate Governance Committee
Member, Investment Committee



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



DOUGLAS PROUTY
August 1, 2017 - July 31, 2021
Vice Chairman, Corporate Governance Committee
Member, Investment Committee



MICHAEL J. STAFFORD, JR.
October 26, 2017 - July 31, 2023
Vice Chairman, Investment Committee

ADVISORS TO THE INVESTMENT COMMITTEE



MICHAEL K. BARRY



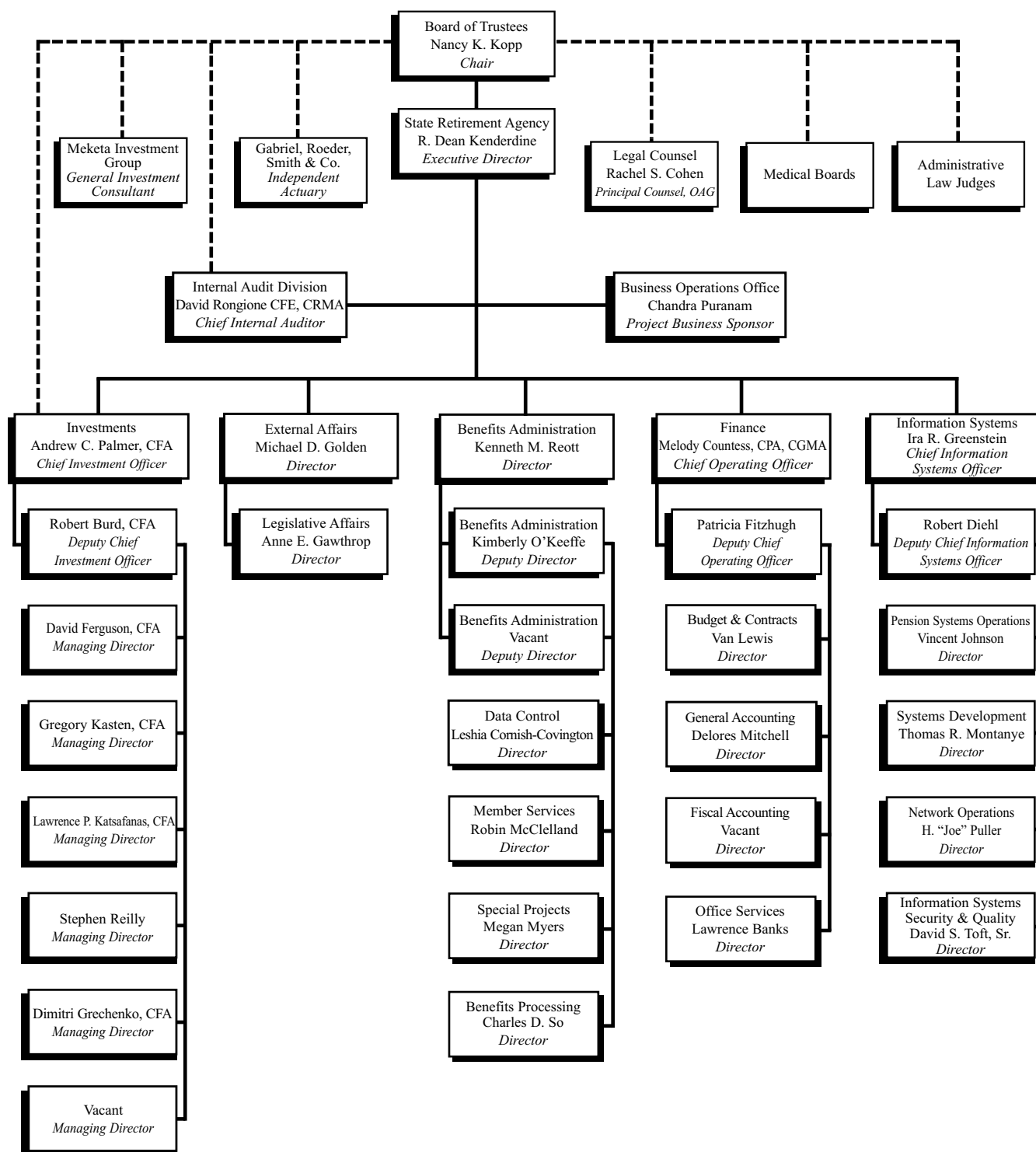
ANNE L. SHELTON



MONTE TARBOX

ORGANIZATIONAL CHART

(November 2020)



*Additional information regarding investment professionals who provide services to the System can be found on pages 11, and 89-92.

PROFESSIONAL SERVICES

Global Custodial Bank and Security Lending

State Street Bank & Trust Company
Boston, Massachusetts

Deutsche Bank
New York, New York

Hearing Officers

Office of Administrative Hearings
Baltimore, Maryland

Independent Actuary

Gabriel Roeder Smith & Co.
Southfield, Michigan

Independent Public Accountant

Clifton Larson Allen
Timonium, Maryland

Independent Investment Consultants

Hamilton Lane Advisors, LLC
Bala Cynwyd, Pennsylvania

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
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Presented to

**Maryland State
Retirement and Pension System**

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended

June 30, 2019

Christopher P. Morrell

Executive Director/CEO



Public Pension Coordinating Council

***Public Pension Standards Award
For Funding and Administration
2020***

Presented to

Maryland State Retirement and Pension System

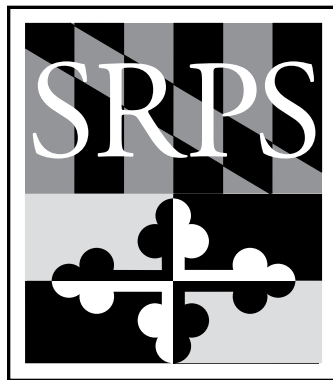
In recognition of meeting professional standards for
plan funding and administration as
set forth in the Public Pension Standards.

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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