

**MONTGOMERY COUNTY CONSOLIDATED RETIREE HEALTH BENEFITS TRUST**

**FINANCIAL STATEMENTS AND  
SUPPLEMENTARY INFORMATION  
YEAR ENDED JUNE 30, 2019**

**WITH  
INDEPENDENT AUDITORS' REPORT**





**MONTGOMERY COUNTY CONSOLIDATED RETIREE HEALTH BENEFITS TRUST**

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## INDEPENDENT AUDITORS' REPORT

The Honorable County Council of Montgomery County, Maryland  
Board of Trustees  
Montgomery County Consolidated Retiree Health Benefits Trust  
Rockville, Maryland

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the Montgomery County Consolidated Retiree Health Benefits Trust (Trust), which comprise the statements of fiduciary net position as of June 30, 2019, and the related statements of changes in fiduciary net position for the year then ended and the related notes to the financial statements, as listed in the table of contents.

### ***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.

### ***Auditors' Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audit. 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 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 auditors' 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 entity'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 entity'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 Trust as of June 30, 2019, and the respective changes in fiduciary net position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

## **Other Matters**

### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, and the schedules of changes in the net OPEB liability and related ratios, employer contributions and investment returns and related notes, as listed in the table of contents, be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

## **Other Reporting Required by Government Auditing Standards**

In accordance with *Government Auditing Standards*, we have also issued our report dated October 29, 2019, on our consideration of the Trust's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely 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 Trust's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Trust's internal control over financial reporting and compliance.



**CliftonLarsonAllen LLP**

Baltimore, Maryland  
October 29, 2019

# MONTGOMERY COUNTY CONSOLIDATED RETIREE HEALTH BENEFITS TRUST

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### INTRODUCTION

The following Management's Discussion and Analysis (MD&A) of the Montgomery County Consolidated Retiree Health Benefits Trust (Trust) financial performance provides an introduction to the financial statements of the Trust as of and for the year ended June 30, 2019.

Since the MD&A is designed to focus on current activities, resulting changes and current known facts, it should be read in conjunction with the financial statements, notes to the financial statements and required supplementary information which follow this discussion.

### REQUIRED FINANCIAL STATEMENTS

The financial statements for the Trust have been prepared under the accrual basis of accounting in conformity with U.S. generally accepted accounting principles, promulgated by the Governmental Accounting Standards Board. The Statement of Fiduciary Net Position comprises the Trust's assets and liabilities and provides information about the nature and amount of investments, as well as the liabilities. The Statement of Changes in Fiduciary Net Position reports the changes in the Trust's net position, measured by the additions by major sources and deductions by type.

### FINANCIAL ANALYSIS OF THE CONSOLIDATED RETIREE HEALTH BENEFITS TRUST

Shown below is a condensed presentation of the net position of the Consolidated Retiree Health Benefits Trust at June 30:

	Net Position (Millions)		
	2019	2018	Percentage Change
<b>ASSETS</b>			
Cash and investments	\$ 1,080.2	\$ 978.3	10.4 %
Receivables	12.6	11.9	5.9
Total assets	<u>1,092.8</u>	<u>990.2</u>	10.4
<b>LIABILITIES</b>			
Claims payable	4.3	4.0	7.5
Other liabilities	<u>9.0</u>	<u>7.2</u>	25.0
Total liabilities	<u>13.3</u>	<u>11.2</u>	18.8
<b>NET POSITION</b>	<u>\$ 1,079.5</u>	<u>\$ 979.0</u>	10.3 %

Net position held in the Trust on June 30, 2019 increased 10.3 percent to \$1,079.5 million primarily attributed to contributions made to the Trust and investment returns achieved by the Trust. Other liabilities increased 25.0 percent to \$9.0 million primarily due to pending trades at year end.

Shown below is a condensed presentation of the change in net position of the Consolidated Retiree Health Benefits Trust at June 30:

<b>Change in Net Position</b>			
(Millions)			
	2019	2018	Percentage Change
<b>ADDITIONS</b>			
Contributions and other income	\$ 88.3	\$ 74.2	19.0 %
Net investment income	79.1	78.4	0.9
Purchase of units (\$1 per unit)	27.2	55.7	(51.2)
Total additions	194.6	208.3	(6.6)
<b>DEDUCTIONS</b>			
Claims and claims administration	66.2	60.8	8.9
Redemption of units (\$1 per unit)	27.2	27.2	-
Administrative expenses	0.7	0.5	40.0
Total deductions	94.1	88.5	6.3
<b>CHANGE IN NET POSITION</b>	<b>\$ 100.5</b>	<b>\$ 119.8</b>	(16.1) %

The primary sources of additions to the Trust are contributions and other income, the purchase of units by Montgomery County Public Schools, and net investment income. Contributions and other income comprise employer contributions, rebates from prescription drug programs and receipts from the Medicare Part D program. In fiscal year (FY) 2019, contributions increased 19 percent to \$88.3 million based on the County Council approved budget for FY 2019. The purchase of units decreased by 51.2 percent to \$27.2 million due to the County Council approved funding for FY 2019. Net investment income increased 0.9 percent to \$79.1 million mainly attributed to increase of the Trust investment assets.

Deductions from the Trust's net position are primarily comprised of claims and redemption of units by Montgomery County Public Schools, and administrative expenses. Cost related to claims and claims administration increased 8.9 percent to \$66.2 million primarily due to the increase in the volume of claims in FY 2019. Administrative expenses increased 40.0 percent in FY 2019 related to additional professional fees.

For additional information regarding this report, please contact the Montgomery County Employee Retirement Plans at 240-777-8220.

**MONTGOMERY COUNTY CONSOLIDATED RETIREE HEALTH BENEFITS TRUST**  
**STATEMENTS OF FIDUCIARY NET POSITION**  
**JUNE 30, 2019**

	<b>Montgomery County Government and Participating Agencies</b>	<b>Montgomery County Public Schools</b>	<b>Montgomery College</b>	<b>Total Trust</b>
<b>ASSETS</b>				
Equity in pooled cash and investments	\$ 970,110	\$ 818,842	\$ 102,175	\$ 1,891,127
Investments				
Government and agency obligations	85,595,589	72,805,726	9,084,666	167,485,981
Municipal/Provincial obligations	1,403,919	1,194,143	149,005	2,747,067
Asset-backed securities	113,498	96,538	12,046	222,082
Corporate bonds	93,178,164	79,255,297	9,889,440	182,322,901
Common and preferred stock	230,660,356	196,194,628	24,481,078	451,336,062
Mutual and commingled funds	43,888,733	37,330,791	4,658,119	85,877,643
Short-term investments	15,530,141	13,209,596	1,648,287	30,388,024
Cash collateral received under securities lending agreements	3,200,757	2,722,493	339,711	6,262,961
Private real assets	19,892,878	16,920,446	2,111,326	38,924,650
Private equity/debt	57,615,691	49,006,641	6,115,027	112,737,359
Total investments	551,079,726	468,736,299	58,488,705	1,078,304,730
Dividend, interest, and other receivables	2,083,928	1,758,985	219,485	4,062,398
Contributions receivable	8,495,473	-	-	8,495,473
Total assets	562,629,237	471,314,126	58,810,365	1,092,753,728
<b>LIABILITIES</b>				
Payable for collateral received under securities lending agreements	3,200,757	2,722,493	339,711	6,262,961
Accounts payable and other liabilities	1,400,325	1,181,974	147,486	2,729,785
Claims payable	4,272,299	-	-	4,272,299
Total liabilities	8,873,381	3,904,467	487,197	13,265,045
<b>Fiduciary net position held in trust</b>	<b>\$ 553,755,856</b>	<b>\$ 467,409,659</b>	<b>\$ 58,323,168</b>	<b>\$ 1,079,488,683</b>

See accompanying notes to financial statements.

**MONTGOMERY COUNTY CONSOLIDATED RETIREE HEALTH BENEFITS TRUST**  
**STATEMENTS OF CHANGES IN FIDUCIARY NET POSITION**  
**FOR THE YEAR ENDED JUNE 30, 2019**

	Montgomery County Government and Participating Agencies	Montgomery County Public Schools	Montgomery College	Total Trust
<b>ADDITIONS</b>				
Contributions and other income				
Employer contributions	\$ 77,208,188	\$ -	\$ -	\$ 77,208,188
Federal government - Medicare Part D	11,094,679	-	-	11,094,679
Total contributions and other income	88,302,867	-	-	88,302,867
Investment income	42,614,499	37,058,622	4,624,158	84,297,279
Less investment expenses	2,793,303	2,318,983	289,362	5,401,648
Net gain from investment activities	39,821,196	34,739,639	4,334,796	78,895,631
Income from securities lending	156,646	136,223	16,998	309,867
Less securities lending expenses	55,166	45,799	5,715	106,680
Net income from securities lending	101,480	90,424	11,283	203,187
Purchase of units (\$1 per unit)	-	27,200,000	-	27,200,000
Total additions	128,225,543	62,030,063	4,346,079	194,601,685
<b>DEDUCTIONS</b>				
Claims and claims administration	66,208,939	-	-	66,208,939
Redemption of units (\$1 per unit)	-	27,200,000	-	27,200,000
Administrative expenses	339,355	281,734	35,154	656,243
Total deductions	66,548,294	27,481,734	35,154	94,065,182
Net increase	61,677,249	34,548,329	4,310,925	100,536,503
<b>Fiduciary net position held in trust</b>				
Beginning of year	492,078,607	432,861,330	54,012,243	978,952,180
End of year	\$ 553,755,856	\$ 467,409,659	\$ 58,323,168	\$ 1,079,488,683

See accompanying notes to financial statements.

**MONTGOMERY COUNTY CONSOLIDATED RETIREE HEALTH BENEFITS TRUST**

**NOTES TO FINANCIAL STATEMENTS  
Year Ended June 30, 2019**

**INTRODUCTION**

During FY 2008, the Montgomery County Council enacted legislation to establish a trust effective July 1, 2007 to fund certain County retiree health benefit plans. Effective July 1, 2011, the Montgomery County Council enacted legislation to change the name to Consolidated Retiree Health Benefits Trust (Trust) due to the addition of County-funded agency retiree health benefits plans for Montgomery County Public Schools and Montgomery College. The purpose of the Trust is to provide funding for retiree health benefits for retirees and their dependents pursuant to Section 115 of the Internal Revenue Code of 1986, as amended.

The Trust is considered part of the County’s financial reporting entity and is included in the County’s basic financial statements. The accompanying financial statements present only the operations of the Trust in conformity with accounting principles generally accepted in the United States of America (GAAP) applicable to the Trust. They are not intended to present fairly the financial position and results of operations of the entire County. The accompanying notes summarize the significant accounting policies and plan provisions established under the Montgomery County Code.

**A. Plan Description and Contribution Information**

*Plan Membership.* At June 30, 2019, the most recent actuarial valuation, plan membership consisted of the following:

Retirees and beneficiaries receiving benefits	7,179
Active plan members	<u>10,439</u>
Total	<u><u>17,618</u></u>

*Plan Administration.* Montgomery County Government and the participating agencies and political subdivisions have elected to participate in the Montgomery County Group Insurance Plan (Plan). The Plan is a cost-sharing multiple-employer defined benefit healthcare plan. The benefits available under the Plan are delivered through various providers, each with its own separate rules governing coverage and administration.

*Benefits Provided.* Substantially all retirees of Montgomery County Government (includes Circuit Court and District Court), Montgomery County Revenue Authority, Housing Opportunities Commission of Montgomery County, Washington Suburban Transit Commission, Strathmore Hall Foundation, Village of Friendship Heights, SkyPoint Federal Credit Union and certain retirees of the State Department of Assessments and Taxation, are provided postemployment benefits such as medical, life, dental, vision, and prescription coverage under the Plan. Retirees may also elect coverage for their eligible dependents. A member of the Employees’ Retirement System of Montgomery County, who retires under a normal, early, disability or discontinued service retirement, is eligible for group insurance benefits under the Plan. However, the member is not eligible for group insurance benefits if the member leaves County service prior to retirement eligibility with a deferred vested benefit payable upon the member’s future retirement date. A member of the Retirement Savings Plan or the Guaranteed Retirement Income Plan is eligible for group insurance upon separation from service based upon the member’s age and credited service at the time of separation. Postemployment benefit provisions and eligibility requirements for retirees are described in the Montgomery County Group Insurance Summary Plan Description.

*Plan Contributions.* The County Council has the authority to establish and amend contribution requirements of the plan members and the County. The Plan is a contributory plan in which the County and the retired members and beneficiaries contribute, based on an actuarial valuation, certain amounts toward the current cost of healthcare benefits. During FY 2019, the County and other contributing entities contributed \$77,208,188 for current premiums and claims as well as toward prefunding future benefits.

*Unit Purchases.* This amount represents the County Council’s action to fund the retiree health care benefits on behalf of Montgomery County Public Schools \$27,200,000 during FY 2019.

**B. Summary of Significant Accounting Policies**

*Basis of Accounting.* The Trust’s financial statements have been prepared under the accrual basis of accounting. Contributions are recognized in the period in which the contributions are required to be made as specified under the County Code. Expenses and claims are recognized when due in accordance with the terms of the Plan.

*Method Used to Value Investments.* Investments are stated at fair value. The fair value for public securities is generally based on quoted market prices at June 30, 2019. Fair value for private investment funds, including private equity and private real assets, is determined using net asset values supplied by the fund managers, which are based upon the fund managers’ valuations of the funds’ underlying holdings. Such values involve subjective judgment and may differ from amounts which would be realized if such holdings were actually sold. The fair value of limited partnership investments are based on valuations of the underlying assets of the limited partnerships as reported by the general partner. Cash received as collateral on securities lending transactions and investments made with such cash are reported at fair value along with a related liability for collateral received.

*Equity in County’s Pooled Cash and Investments.* The Trust maintains its short-term cash with the County, which invests cash and allocates interest earned, on a quarterly basis to the Trust based on the Trust’s average daily balance of its equity in pooled cash. The County’s policy is to fully collateralize the cash maintained in the pool.

*Accounting Changes.* There were no new pronouncements adopted during the year ended June 30, 2019.

**C. Net OPEB Liability**

The components of the Plan’s net OPEB liability as of June 30, 2019, were as follows:

Total OPEB Liability (a)	Plan Fiduciary Net Position (b)	Net OPEB Liability (a-b)	Plan Fiduciary Net Position as a % of Total OPEB Liability (b/a)
\$1,407,188,030	\$553,755,856	\$853,432,174	39.35%

*Actuarial assumptions.* The total OPEB liability was determined by an actuarial valuation as of July 1, 2019, using the following actuarial assumptions, applied to all periods included in the measurement, unless otherwise specified:

Valuation Date	July 1, 2019
Measurement Date	June 30, 2019
Actuarial cost method	Entry Age Normal
Discount Rate	6.10%
20 Yr. Municipal Bond Rate	3.13%
Municipal Bond Rate Basis	Fidelity General Obligation 20 year Municipal Bond Index
Expected Return on Assets	7.50%
Salary Increases	4.25% to 8.25%
General Inflation	3.00%

Mortality

Healthy Retirees	Group A, H, J, GRIP – Pub-2010 Healthy Mortality, Headcount weighted, General Employees, Sex Distinct, Fully Generational projected from 2010 using scale MP-2018  Group E, F, G – Pub-2010 Healthy Mortality, Headcount weighted, Public Safety Employees, Sex Distinct, Fully Generational projected from 2010 using scale MP-2018
Disabled Retirees	Group A, H, J, GRIP – Pub-2010 Disabled Mortality, Headcount weighted, General Employees, Sex Distinct, Fully Generational projected from 2010 using scale MP-2018  Group E, F, G – Pub-2010 Disabled Mortality, Headcount weighted, Public Safety Employees, Sex Distinct, Fully Generational projected from 2010 using scale MP-2018
Health care cost trend rates	The medical trend assumption was developed using the Society of Actuaries (SOA) Long-Run Medical Cost Trend Model, version 2019_b. The model was adjusted to include the effects of the Cadillac tax set to take effect in 2022. The initial rate is 5.40% and the ultimate rate is 3.68%.

The actuarial assumptions used in the June 30, 2019 valuation, with the exception of the mortality assumptions, were based on the results of an actuarial experience study conducted by the County in September 2019 for the period July 1, 2014 to July 1, 2018.

The long-term expected rate of return on OPEB 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 OPEB 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 OPEB plan’s target asset allocation as of June 30, 2019 are summarized in the following table:

<b>Asset Class</b>	<b>Long-Term Expected Real Rate of Return</b>
Domestic Equities	5.30 %
International Equities	5.80
Emerging Market Equities	5.80
Global Equities	5.75
Private Equity	7.63
Credit Opportunities	6.05
High Yield Bonds	4.20
Directional Hedge Funds	5.02
Long Duration Fixed Income	2.55
Cash	0.95
Diversifying Hedge Funds	3.90
Global ILs	2.85
Private Real Assets	7.06
Public Real Assets	5.02

*Discount Rate.* A single discount rate of 6.10% was used to measure the total OPEB liability as of June 30, 2019. This single discount rate was blended based on the expected long-term rate of return on OPEB plan investments of 7.5% and the municipal long term high quality bond index yield (at the measurement date) of 3.13% as described under the terms of the GASB standard. The projection of cash flows used to determine the single discount rate assumes that employer contributions will be made based on the current funding policy (contributions equal to the employer normal cost plus a 30-year open level percent of pay amortization of the unfunded employer liability). Based on these assumptions, the OPEB plan’s fiduciary net position was projected to not be sufficient to make all projected future benefit payments on behalf of current plan members. Therefore, the long-term expected rate of return on plan investments was applied only to those payments prior to the depletion of the fiduciary net position and the bond yield index rate was applied to those benefit payments subsequent to the projected depletion of the fiduciary net position. For this valuation, the bond rate used as of June 30, 2019 was 3.13%. Therefore, the blended discount rate used as of June 30, 2019 was 6.10 %.

*Sensitivity of the Net OPEB Liability to Changes in the Discount Rate.* The following presents the net OPEB liability calculated using the discount rate of 6.10%, as well as what the net OPEB liability would be if it were calculated using a discount rate that is 1-percentage-point lower (5.10%) or 1-percentage-point higher (7.10%) than the current rate:

	<b>1% Decrease</b>	<b>Discount Rate</b>	<b>1% Increase</b>
	5.10%	6.10%	7.10%
Net OPEB Liability	\$1,053,029,364	\$853,432,174	\$690,126,834

*Sensitivity of the Net OPEB Liability to Changes in the Healthcare Cost Trend Rate.* The following presents the net OPEB liability of the Plan using the healthcare cost trend rate of 3.68%, as well as what the Plan’s net OPEB liability would be if it were calculated using healthcare cost trend rates that are 1-percentage-point lower (2.68%) or 1-percentage-point higher (4.68%) than the current healthcare cost trend rate:

	<b>1% Decrease</b>	<b>Trend Rate</b>	<b>1% Increase</b>
	2.68%	3.68%	4.68%
Net OPEB Liability	\$681,840,413	\$853,432,174	\$1,067,812,153

**D. Trustees of the Plan**

The County established a Board of Trustees (Board) for the Trust to be responsible for the investment management of the Trust’s assets for the exclusive benefit of the members. The Board consists of nineteen members appointed by the County Executive and confirmed by the County Council.

**E. Investments**

Section 33-163 of the Code, authorizes the Board to act with the care, skill, prudence and diligence under the circumstances that a prudent person acting in a similar capacity and familiar with the same matters would use to conduct a similar enterprise with similar purposes. The Code also requires that such investments be diversified so as to minimize the risk of large losses unless it is clearly not prudent to diversify under the circumstances. The Board has adopted an investment policy that works to control the extent of downside risk to which the Trust is exposed while maximizing the potential for long term increases in the value of assets. The overall investment policies do not address specific levels of credit risk, interest rate risk or foreign currency risk. The Board believes that risks can be managed, but not eliminated, by establishing constraints on the investment portfolios and by monitoring the financial markets, the Trust’s asset allocation and the investment managers hired by the Trust. Each investment manager has a specific benchmark and investment guidelines appropriate for the type of investments they are managing.

The table on the next page shows the Board’s adopted asset allocation policy as of June 30, 2019:

<b>Asset Class</b>	<b>Target Allocation</b>	
Domestic Equities	16.80	%
International Equities	13.50	
Emerging Market Equities	3.40	
Global Equities	3.80	
Private Equity	8.00	
Credit Opportunities	2.00	
High Yield Bonds	8.50	
Directional Hedge Funds	2.50	
<b>Total Growth</b>	<b>58.50</b>	
Long Duration Fixed Income	13.50	
Cash	1.00	
Diversifying Hedge Funds	2.50	
<b>Total Risk Mitigation</b>	<b>17.00</b>	
Global ILs	12.00	
Private Real Assets	5.00	
Public Real Assets	7.50	
<b>Total Real Assets/Inflation Protection</b>	<b>24.50</b>	
<b>Total</b>	<b>100.00</b>	%

*Rate of Return.* The annual money-weighted rate of return on the Trust investments, net of investment expenses, for FY 2019 was 8.26%. The money-weighted rate of return expresses investment performance, net of investment expense, adjusted for the changing amounts actually invested.

*Fair Value Measurement.* The Trust categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset and gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level I measurements) and the lowest priority to unobservable inputs (level III measurements).

Level I – Unadjusted quoted prices for identical assets or liabilities in active markets.

Level II – Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets are not active; and model-derived valuations in which all significant inputs are observable.

Level III – Valuations derived from valuation techniques in which significant inputs are unobservable.

Investments that are measured at fair value using the net asset value per share (or its equivalent) as a practical expedient are not classified in the fair value hierarchy. In instances where inputs used to measure fair value fall into different levels in the fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Trust's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset or liability.

The table on the next page shows the fair value leveling of the Trust's investments.

	6/30/19	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets	Significant Other Observable Inputs	Significant Unobservable Inputs
		Level I	Level II	Level III
<b>Investments by fair value level</b>				
Debt securities				
Government and agency obligations	\$ 77,299,294	\$ -	\$ 77,299,294	\$ -
Asset backed Securities	222,082	-	222,082	-
Municipal/Provincial obligations	2,747,067	-	2,747,067	-
Corporate bonds	182,322,901	-	182,068,755	254,146
<b>Total debt securities</b>	<b>262,591,344</b>	<b>-</b>	<b>262,337,198</b>	<b>254,146</b>
Equity securities				
Consumer goods	37,068,138	36,532,828	535,310	-
Communication Services	13,073,538	13,073,538	-	-
Energy	15,651,687	15,592,610	59,077	-
Financials	23,882,636	23,882,636	-	-
Health Care	28,342,305	28,342,305	-	-
Industrials	33,867,660	33,867,660	-	-
Information Technology	34,039,883	34,039,883	-	-
Materials	8,494,058	8,494,058	-	-
Real Estate	33,483,743	33,483,743	-	-
Utilities	10,960,726	10,960,726	-	-
<b>Total equity securities</b>	<b>238,864,374</b>	<b>238,269,987</b>	<b>594,387</b>	<b>-</b>
Securities lending collateral fund	6,262,961	-	6,262,961	-
<b>Total investments by fair value level</b>	<b>\$ 507,718,679</b>	<b>\$ 238,269,987</b>	<b>\$ 269,194,546</b>	<b>\$ 254,146</b>
<b>Investments measured at the net asset value (NAV)</b>				
Commingled equity funds	212,471,688			
Commingled bond funds	90,186,687			
Commingled real asset funds	27,811,590			
Hedge fund	39,244,623			
Fund-of-hedge funds	18,821,430			
Private real assets	38,924,650			
Private equity/debt	112,737,359			
<b>Total investments measured at the NAV</b>	<b>540,198,027</b>			
<b>Investments measured at amortized cost</b>				
Short-term investments	30,388,024			
<b>Total investments measured at amortized cost</b>	<b>30,388,024</b>			
<b>Total investments</b>	<b>\$ 1,078,304,730</b>			
<b>Investment derivative instruments:</b>				
Foreign exchange contracts	4,595	-	4,595	
<b>Total investment derivative instruments</b>	<b>\$ 4,595</b>	<b>\$ -</b>	<b>\$ 4,595</b>	

Equity securities classified in Level I are valued using prices quoted in active markets for those securities.

Debt securities classified in Level II and Level III are valued using either a bid evaluation, or matrix pricing technique. Bid evaluations may include market quotations, yields, maturities, call features and ratings. Matrix pricing is used to value securities based on the securities relationship to benchmark quoted prices. Level II debt securities have non-proprietary information that was readily available to market participants, from multiple independent sources, which are known to be actively involved in the market. Level III debt securities use proprietary information or single source pricing. Equity securities classified in Level II are securities whose values are derived daily from associated traded securities. Short-term investments are cash or cash equivalents and generally include investments in money market-type securities reported at cost plus accrued interest, which approximates market or fair value.

The valuation method for investments measured at the net asset value (NAV) per share, or equivalent, is presented in the table on the next page.

**Investments Measured at the NAV**

	<b>Fair Value</b>	<b>Unfunded Commitments</b>	<b>Redemption Frequency</b>	<b>Redemption Notice Period</b>
Commingled equity funds	\$ 212,471,688	\$ -	Daily, Monthly	0-15 days
Commingled bond funds	90,186,687	-	Daily	1 day
Commingled real asset funds	27,811,590	-	Daily, Bi-weekly	0-5 days
Hedge fund	39,244,623	-	Monthly	5 days
Fund-of-hedge funds	18,821,430	-	Quarterly	95 days
Private real assets	38,924,650	19,111,610	Not eligible	N/A
Private equity/debt	112,737,359	49,156,578	Not eligible	N/A
<b>Total investments measured at the NAV</b>	<b>\$ 540,198,027</b>	<b>\$ 68,268,188</b>		

*Commingled Bond Funds, Equity Funds and Real Asset Funds.* One bond fund, ten equity funds, and two real asset funds are considered to be commingled in nature. The fair value of the investments in these types of funds have been determined using the NAV per share of the investments.

*Hedge Fund.* One fund is categorized in this category. The fair value of the investments have been determined using the NAV per share of the fund.

*Fund-of-Hedge Funds.* The fair value of this fund is based upon information provided by underlying hedge fund investments using the NAV per share of the funds. Fund-of-hedge funds provide additional opportunities in terms of manager access, investment structuring, and fees. These funds also could be subject to varying degrees of redemption restrictions based on market conditions that may impact their underlying portfolios.

*Private Real Assets.* The portfolio consists of twenty-three private real asset limited partnerships. Private real asset funds include U.S. real estate, oil and gas, timber, agriculture and other real asset investments. The fair value of these funds has been determined using the net asset values as of June 30, 2019. Net asset values one quarter in arrears plus current quarter cash flows are used when the most recent information is not available. These funds are not eligible for redemption. Distributions are received as underlying investments within the funds are liquidated, which on average can occur over a span of 5 to 10 years.

*Private Equity/Debt.* The portfolio consists of forty private equity/debt limited partnerships. Private equity funds include buyout, turnaround, and fund-of-funds investments. Private debt funds include distressed and structured equity investments. The fair value of these funds has been determined using the net asset values as of June 30, 2019. Net asset values one quarter in arrears plus current quarter cash flows are used when the most recent information is not available. These funds are not eligible for redemption. Distributions are received as underlying investments within the funds are liquidated, which on average can occur over a span of 3 to 10 years.

*Interest Rate Risk.* Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of the investment. The Board's investment policies and guidelines manage interest rate risk by establishing duration constraints on each fixed income manager's portfolio based on the duration of each manager's respective benchmark. Duration is a measure of interest rate risk based on a bond price's sensitivity to a 100-basis point change in interest rates. The greater the duration of a bond, or a portfolio of bonds, the greater its price volatility will be in response to a change in interest rates and vice-versa. Duration of eight would mean that, given a 100-basis point change up/down in rates, a bond's price would move down/up by 8 percent. As of June 30, 2019, the Trust's fixed income portfolio had the following sensitivity to changes in interest rates:

<b>Type of Investment</b>	<b>Effective Duration in Years</b>	<b>Fair Value</b>	<b>Percentage of Portfolio</b>
U.S. Government Obligations	16.99	\$ 76,847,295	20.05 %
Foreign Government Obligations	1.27	451,999	0.12
Municipal/Provincial Obligations	14.40	2,747,067	0.72
Corporate Bonds	8.34	182,322,901	47.58
Asset-Backed Securities	7.84	222,082	0.06
Fixed Income Pooled Funds	N/A	90,186,687	23.54
Short-term Investments and Others *	N/A	30,388,024	7.93
<b>Total Fixed Income Securities</b>		<b>\$ 383,166,055</b>	<b>100.00 %</b>

\*Short-term investments consist of U.S. Treasury and government sponsored securities, money market funds, commercial paper, certificates of deposit, repurchase agreements, asset backed securities, notes and bonds issued by U.S. corporations, and other allowable instruments that meet short-term maturity or average life, diversification, and credit quality restrictions.

*Credit Risk/Concentration of Credit Risk.* Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Board's investment policies and guidelines limit the percentage of the total fund and individual manager's account which can be invested in fixed income securities rated below investment grade. In addition, the Board's investment policies and guidelines, for the majority of public fund managers, limit the percentage of each investment manager's account that may be allocated to any one security, position, issuer or affiliated issuer, to less than 5 percent of the fair value of the investment manager's account. The Trust does not have investments (other than those issued or explicitly guaranteed by the U.S. Government or pooled investments) in any one company that represents 5 percent or more of net assets.

The quality ratings of investments in fixed income securities as described by nationally recognized rating organizations as of June 30, 2019 are as follows:

<b>Type of Investment</b>	<b>Quality Rating</b>	<b>Fair Value</b>	<b>Percentage of Portfolio</b>
U.S. Government Obligations*	AAA	\$ 76,678,140	20.01 %
	BBB	169,155	0.04
Foreign Government Obligations	A	123,396	0.03
	Unrated	328,603	0.09
Municipal/Provincial Bonds	AAA	405,709	0.10
	AA	1,833,425	0.48
	BBB	147,431	0.04
	B	337,549	0.09
	Unrated	22,953	0.01
Corporate Bonds	AAA	1,801,551	0.47
	AA	9,308,317	2.43
	A	36,497,908	9.53
	BBB	47,828,429	12.48
	BB	43,998,072	11.48
	B	30,038,567	7.84
	CCC	6,671,820	1.74
	CC	27,155	0.01
	C	44,875	0.01
	D	619,032	0.16
	Unrated	5,487,175	1.43
	Asset-Backed Securities	AAA	222,082
Fixed Income Pooled Funds	Unrated	90,186,687	23.54
Short-term Investments and others	Unrated	30,388,024	7.93
<b>Total Fixed Income Securities</b>		<b>\$ 383,166,055</b>	<b>100.00 %</b>

\*Obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not have purchase limitations.

*Foreign Currency Risk.* Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The Board's International Investing Policy's objective is to achieve long-term capital appreciation and current income by investing in diversified portfolios of non-U.S. equities and bonds. The Trust has indirect exposure to foreign currency risk as shown in the table below:

<b>International Securities</b>	<b>Equity</b>	<b>Fixed Income</b>	<b>Short-Term and Other</b>	<b>Total Non-U.S. Dollar</b>
Euro	\$ 36,117,915	\$ -	\$ 4,217	\$ 36,122,132
Japanese yen	19,586,482	-	4,517	19,590,999
British pound sterling	11,430,845	234,311	(155,516)	11,509,640
Hong Kong dollar	11,398,011	-	4,863	11,402,874
Swiss franc	5,714,208	-	1,662	5,715,870
Canadian dollar	4,896,584	-	14,650	4,911,234
Australian dollar	4,667,655	-	30	4,667,685
Swedish krona	4,183,283	-	-	4,183,283
Singapore dollar	2,946,201	-	-	2,946,201
Mexican peso	1,530,165	-	-	1,530,165
Other Currencies	1,992,513	678,401	20,090	2,691,004
Total International Securities	<u>\$ 104,463,862</u>	<u>\$ 912,712</u>	<u>\$ (105,487)</u>	<u>\$ 105,271,087</u>

*Derivatives.* In accordance with the Board's Statement of Investment Policy and Objectives, the Trust regularly invests in derivative financial instruments in the normal course of its investing activities to manage exposure to certain risks within the fund. During FY 2019, the Trust invested directly in various derivatives including exchange-traded futures contracts, forward currency contracts, and swaps. Investment managers are prohibited from purchasing securities on margin or using leverage unless specifically permitted within the investment manager's guidelines. These investments generally contain market risk resulting from fluctuations in interest and currency rates. The credit risk of these investments is associated with the creditworthiness of the related parties to the contracts. The Trust could be exposed to risk if the counterparties to the contracts are unable to meet the terms of the contracts. The Board's Statement of Investment Policy and Objectives seeks to control this risk through counterparty credit evaluations and approvals, counterparty credit limits, and exposure monitoring procedures. In addition, the Trust has indirect exposure to market and credit risk through its ownership interests in certain mutual and commingled funds which may hold derivative financial instruments. The Trust is not a dealer, but an end-user of these instruments.

The notional or contractual amounts of derivatives indicate the extent of the Trust's involvement in the various types of derivative financial instruments and do not measure the Trust's exposure to credit or market risk and do not necessarily represent amounts exchanged by the parties. The amounts exchanged are determined by reference to the notional amounts and the other terms of the derivatives.

As permitted by the Board's policies, the Trust holds off-financial statement derivatives in the form of exchange-traded financial futures.

Futures contracts are contracts in which the buyer agrees to purchase and the seller agrees to make delivery of a specified financial instrument at a predetermined date and price. Gains and losses on futures contracts are settled daily. Futures contracts are standardized and are traded on exchanges. The exchange assumes the risk that a counterparty will not pay. As of June 30, 2019, the Trust held 404 long US Treasury futures contracts with a fair value of \$ 78,006,218 and 283 short US Treasury futures contracts with a fair value of (\$36,246,031).

Foreign exchange contracts involve an agreement to exchange the currency of one country for the currency of another country at an agreed-upon price and settlement date. Foreign exchange contracts contain market risk resulting from fluctuations in currency rates. The credit risk is associated with the creditworthiness of the related parties to the contracts. As of June 30, 2019, the Trust held \$325,648 buy foreign exchange contracts and (\$321,053) sell foreign exchange contracts. The unrealized gain on the Trust's contracts was \$4,595.

*Securities Lending.* Board policy permits the Trust to lend its securities to broker-dealers and other entities (borrowers) for collateral that will be returned for the same securities in the future. The Trust's custodian is the agent in lending

the Trust's securities for collateral of 102 percent for domestic and 105 percent for international securities. The custodian receives cash, securities or irrevocable bank letters of credit as collateral. All securities loans can be terminated on demand by either the Trust or the borrower. Cash collateral received from the borrower is invested by the lending agent, as an agent for the Trust, in a short-term investment pool in the name of the Trust, with guidelines approved by the Board. Such investments are considered a collateralized investment pool. The relationship between the maturities of the investment pool and the Trust's loans are affected by the maturities of securities loans made by other plan entities that invest cash collateral in the investment pool, which the Trust cannot determine. The Trust records a liability for the return of the cash collateral shown as collateral held for securities lending in the statement of fiduciary net position. The agent indemnifies the Trust by agreeing to purchase replacement securities, or return the cash collateral thereof, in the event a borrower fails to return loaned securities or pay distributions thereon. There were no such failures by any borrower during the FY, nor were there any losses during the period resulting from a default of the borrower or lending agent.

As of June 30, 2019, the fair value of securities on loan was \$77,723,408. Cash received as collateral and the related liability of \$6,262,961 as of June 30, 2019, is shown on the Statement of Fiduciary Net Position. Securities received as collateral are not reported as assets since the Trust does not have the ability to pledge or sell the collateral securities absent borrower default. Securities lending revenues and expenses amounting to \$309,687 and \$106,680, respectively, have been classified with investment income and investment expenses, respectively, in the accompanying financial statements.

The following represents the balances relating to the securities lending transactions at June 30, 2019:

<b>Securities Lent</b>	<b>Underlying Securities</b>	<b>Non-Cash Collateral Value</b>	<b>Cash Collateral Investment Value</b>
Lent for Cash Collateral:			
Government Obligations	\$ -	\$ -	\$ -
Corporate Bonds	4,244,601	-	4,325,388
Equities	1,875,617	-	1,937,573
Lent for Non-Cash Collateral:			
Government Obligations	21,488,354	23,054,058	-
Corporate Bonds	2,204,362	2,294,167	-
Equities	47,910,474	51,159,294	-
Total	<u>\$ 77,723,408</u>	<u>\$ 76,507,519</u>	<u>\$ 6,262,961</u>

At year-end, the Trust has no credit risk exposure to borrowers because the amounts the Trust owes the borrowers exceeded the amounts the borrowers owe the Trust. The Trust is fully indemnified by its custodial bank against any losses incurred as a result of borrower default.

*Custodial Credit Risk.* Custodial credit risk is the risk that, in the event of the failure of the counterparty, the Trust will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. At June 30, 2019, there were no funds held by a counterparty that was acting as the Trust's agent in securities lending transactions.

## REQUIRED SUPPLEMENTARY INFORMATION

The following required supplementary information is intended to help users assess the Trust's net position as a percentage of total OPEB liability, assess progress made in accumulating assets to pay benefits when due, and make comparisons among employers.

### SCHEDULE OF CHANGES IN THE NET OPEB LIABILITY AND RELATED RATIOS

Fiscal Year Ending	June 30, 2019	June 30, 2018	June 30, 2017
<b>Total OPEB Liability</b>			
Service Cost	\$ 70,518,206	\$ 65,155,686	\$ 73,126,875
Interest Cost	111,580,719	117,685,710	116,270,504
Differences between Expected and Actual Experiences	(351,021,508)	(1,877,264)	(22,113,781)
Changes of Assumptions	(191,917,617)	(268,604,422)	(261,363,550)
Medicare Part D Reimbursement	11,094,679	10,453,719	6,345,721
Benefit Payments	(66,208,939)	(60,773,387)	(63,284,352)
Net Change in Total OPEB Liability	(415,954,460)	(137,959,958)	(151,018,583)
Total OPEB Liability – Beginning	1,823,142,490	1,961,102,448	2,112,121,031
Total OPEB Liability – Ending (a)	<u>\$ 1,407,188,030</u>	<u>\$ 1,823,142,490</u>	<u>\$ 1,961,102,448</u>
<b>Plan Fiduciary Net Position</b>			
Contributions - Employer	\$ 77,208,188	\$ 63,725,810	\$ 122,466,187
Net Investment Income	39,922,676	40,066,004	42,759,085
Medicare Part D Reimbursement	11,094,679	10,453,719	6,345,721
Benefit Payments	(66,208,939)	(60,773,387)	(63,284,352)
Administrative Expense	(339,355)	(276,553)	(4,292,538)
Net Change in Plan Fiduciary Net Position	61,677,249	53,195,593	103,994,103
Plan Fiduciary Net Position – Beginning	492,078,607	438,883,014	334,888,911
Plan Fiduciary Net Position – Ending (b)	<u>\$ 553,755,856</u>	<u>\$ 492,078,607</u>	<u>\$ 438,883,014</u>
Net OPEB Liability – Ending (a-b)	\$ 853,432,174	\$ 1,331,063,883	\$ 1,522,219,434
Plan Fiduciary Net Position as a Percentage of Total OPEB Liability	39.35%	26.99%	22.38%
Covered Payroll	\$ 785,379,904	\$ 766,111,522	\$ 750,986,381
Net OPEB Liability as a Percentage of Covered Payroll	108.66%	173.74%	202.70%

*Note: Schedule is intended to show information for 10 years. Additional years will be displayed as they become available.*

### SCHEDULE OF EMPLOYER CONTRIBUTIONS

FY Ended June 30	Actuarially Determined Contribution	Actual Contribution	Contribution Deficiency (Excess)	Covered Payroll	Actual Contribution as a % of Covered Payroll
2017	\$112,702,000	\$122,466,187	(\$9,764,187)	\$750,986,381	16.31%
2018	117,474,000	63,725,810	53,748,190	766,111,522	8.32
2019	116,737,000	77,208,188	39,528,812	785,379,904	9.83

*Note: Schedule is intended to show information for 10 years. Additional years will be displayed as they become available.*





**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

The Honorable County Council of Montgomery County, Maryland  
Board of Trustees  
Montgomery County Consolidated Retiree Health Benefits Trust

We have audited, in accordance with the 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, the financial statements of the Montgomery County Consolidated Retiree Health Benefits Trust (Trust), as of and for the year ended June 30, 2019, and the related notes to the financial statements, and have issued our report thereon dated October 29, 2019.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Trust's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control. Accordingly, we do not express an opinion on the effectiveness of the Trust's internal control.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Trust's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

### **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the Trust's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Trust's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in cursive script that reads "CliftonLarsonAllen LLP".

**CliftonLarsonAllen LLP**

Baltimore, Maryland  
October 29, 2019