

**HARFORD COUNTY, MARYLAND
SHERIFF'S OFFICE PENSION SYSTEM**

**Financial Statements and Supplementary Schedules
Together with Report of Independent Public Accountants**

For the Year Ended June 30, 2012



SB & COMPANY, LLC
EXPERIENCE • QUALITY • CLIENT SERVICE

JUNE 30, 2012

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REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Board of Directors
Harford County, Maryland
Sheriff's Office Pension System

We have audited the accompanying statement of plan net assets of Harford County, Maryland Sheriff's Office Pension System (the Plan), a pension trust fund of Harford County, Maryland, as of June 30, 2012, and the related statement of changes in plan net assets for the year then ended. These financial statements and supplemental schedules are the responsibility of the Plan's management. 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of the Harford County, Maryland Sheriff's Office Pension System as of June 30, 2012, and the changes in its plan net assets for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the statement of plan net assets. The accompanying schedules of funding progress and employer contributions are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The accompanying schedules of funding progress and employer contributions have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion or provide any assurance on them.

Hunt Valley, Maryland
October 1, 2012

SB & Company, LLC

HARFORD COUNTY, MARYLAND SHERIFF'S OFFICE PENSION SYSTEM

Statement of Plan Net Assets As of June 30, 2012

Assets

| | |
|---------------------------------------|-------------------|
| Equity in pooled cash and investments | \$ 309,171 |
| Investments, at fair value: | |
| Cash equivalents | 331,040 |
| Fixed income fund | 10,832,556 |
| Equities and equivalents | <u>25,082,981</u> |
| Total investments | <u>36,246,577</u> |
| Total Assets | 36,555,748 |

Liabilities

| | |
|------------------|---------------|
| Accounts payable | <u>13,677</u> |
|------------------|---------------|

| | |
|--|------------------------------------|
| Net Assets Held In Trust for Pension Benefits | <u><u>\$ 36,542,071</u></u> |
|--|------------------------------------|

The accompanying notes are an integral part of this financial statement.

HARFORD COUNTY, MARYLAND SHERIFF'S OFFICE PENSION SYSTEM

Statement of Plan Net Assets For the Year Ended June 30, 2012

Additions

Contributions:

| | |
|---------------------|------------------|
| Employer | \$ 2,258,322 |
| Employee | 478,499 |
| Total Contributions | <u>2,736,821</u> |

Investment earnings:

| | |
|---------------------------------------|-------------------------|
| Net loss in fair value of investments | (844,279) |
| Interest and dividends | 708,612 |
| Less: investments expense | 153,599 |
| Net investment earnings | <u>(289,266)</u> |
| Total Additions | <u>2,447,555</u> |

Deductions

| | |
|-------------------------|-------------------------|
| Administrative expenses | 34,890 |
| Benefits | 2,200,319 |
| Total Deductions | <u>2,235,209</u> |

| | |
|--------------------------------|------------------------------------|
| Changes in net position | 212,346 |
| Net assets, beginning of year | 36,329,725 |
| Net Assets, End of Year | <u><u>\$ 36,542,071</u></u> |

The accompanying notes are an integral part of this financial statement.

HARFORD COUNTY, MARYLAND SHERIFF'S OFFICE PENSION SYSTEM

Notes to the Financial Statements

June 30, 2012

1. PLAN DESCRIPTION

The Sheriff's Office Pension System (the SOPS or the Plan) is a single employer defined benefit pension plan, established by Harford County, Maryland (the County) effective July 1, 1997, for certain law enforcement and correctional employees of the Office of the Sheriff of Harford County. Bill No. 97-20 assigns the authority to establish and amend the benefit provisions of the Plan to Harford Government by county ordinance. The SOPS provide retirement, disability and death benefits to plan members and their beneficiaries. The SOPS is considered part of the County's financial reporting entity and is included in the County's financial statements as a pension trust fund.

The Internal Revenue Service issued a determination letter on September 20, 2002, which stated that the Plan and its underlying trust qualify under the applicable provision of the Internal Revenue Code, and therefore the trust is exempt from Federal income taxes. In the opinion of the plan administrator, the Plan and its underlying trust have operated within the terms of the Plan and remain qualified under the applicable provisions of the Internal Revenue Code.

The membership data related to the Harford County Sheriff's Office Pension Plan as of July 1, 2011, was as follows:

| <u>Plan Participants</u> | |
|---|--------------------------|
| Retirees and beneficiaries currently receiving benefits | 65 |
| Terminated vested participants | 6 |
| Active plan members | <u>129</u> |
| Total | <u><u>200</u></u> |

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The SOPS fund uses the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the Plan.

HARFORD COUNTY, MARYLAND SHERIFF'S OFFICE PENSION SYSTEM

Notes to the Financial Statements

June 30, 2012

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Use of Estimates

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

Method Used to Value Investments

Investments are reported at fair market value. Short-term investments are reported at cost, which approximates fair value. Securities traded on a national exchange are valued at the last reported sales price at current exchange rates. The County has hired an investment firm to manage the investments of the SOPS.

Interest Rate Risk

The investment policy of the pension plan does not limit investment maturities. Fluctuating rates of return are characteristic of the securities markets; the fund's greatest concern is long-term appreciation of assets and consistency of portfolio returns. However, cash and cash equivalent investments, such as commercial paper, repurchase agreements, etc. are limited to maturities of one year or less.

Credit Risk

The investment manager is allowed substantial discretion within a broad framework of approved investment choices. Equity holdings may be selected from those listed on the major securities markets. The Manager(s) may invest in commercial paper, repurchase agreements, Treasury Bills, certificates of deposit, deposit accounts (with the custodian's bank) which is fully insured and/or fully collateralized, and money market funds to provide income, liquidity for expense payments, and preservation of the fund's principal value. All such assets must represent maturities of one year or less at time of purchase. Standard & Poor's and Moody's must rate commercial paper assets A-2 or P-2 respectively. The fixed income portion of the portfolio will consist primarily of fixed income securities denominated in U.S. dollars issued by the U.S. Government or U.S. corporations rated investment grade or better and having a weighted average maturity of no longer than 10 years. The Manager(s) should maintain the fixed income portion of the portfolio at a risk level roughly equivalent to Barclays Government/Credit Intermediate-Term Bond Index.

HARFORD COUNTY, MARYLAND SHERIFF'S OFFICE PENSION SYSTEM

Notes to the Financial Statements

June 30, 2012

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Credit Risk (continued)

The portfolio's maximum exposure to non benchmark sectors including foreign issues, emerging market debt and high yield securities may not exceed 20% of its market value.

Concentration of Credit Risk

As a means of minimizing risk and providing a consistent return, the investment policy requires diversification. U.S. corporate bonds shall be diversified by issuer type with no more than 5% of the portfolio invested in obligations of any one issuer and no more than 10% in any one outstanding debt issue. Investments by security type are to be diversified as follows:

| | <u>Minimum</u> | <u>Maximum</u> |
|-------------------------|----------------|----------------|
| U.S. Large cap equities | 25% | 47% |
| U.S. Mid cap equities | 3% | 13% |
| U.S. Small cap equities | 3% | 10% |
| International equities | 14% | 27% |
| Fixed income | 21% | 39% |

3. CONTRIBUTIONS AND FUNDING POLICY

Plan members are required to contribute 7% of their annual covered salary. The County is required to contribute at an actuarially determined rate, currently 32.6% of covered payroll. Per Bill 97-20, contribution requirements of the plan members and the County are established and may be amended by County legislature. Administrative costs of the SOPS are to be paid by the trust unless the County decides to do so.

Annual Pension Cost (APC) for the year ended June 30, 2012 and Net Pension Obligation (NPO) as of June 30, 2012 and 2011 of Harford County for this SOPS are as follows:

| | | |
|--|-----------|--------------------|
| Net pension obligation, beginning of year | \$ | - |
| Annual required contribution | | 2,258,322 |
| Contributions made | | <u>(2,258,322)</u> |
| Net Pension Obligation, End of Year | \$ | <u>-</u> |

HARFORD COUNTY, MARYLAND SHERIFF'S OFFICE PENSION SYSTEM

**Notes to the Financial Statements
June 30, 2012**

3. CONTRIBUTIONS AND FUNDING POLICY (continued)

The annual required contribution for the year ended June 30, 2012 was determined as part of the July 1, 2011, actuarial valuation using the projected unit cost method. Under this method, the actuarial liability represents the present value of projected benefits prorated for service to date for current participants. The normal cost represents the present value of projected benefits allocated to the current year for active participants who have not attained normal retirement age. Any actuarial gains and losses resulting from actual plan experiences either more or less favorable than anticipated on the basis of the actuarial assumptions and asset valuation method will result in direct adjustments of the unfunded actuarial accrued liability. These adjustments will be amortized over a rolling 15-year period.

Generally, contributions toward the funding of the plan are derived as the sum of the normal cost and a payment toward the amortization of the unfunded actuarial liability. The original unfunded accrued liability will be amortized over the next 10 years: various adjustments are being amortized over 10 to 29 years. Payments toward the unfunded liability increase by 3% per year. The actuarial assumptions included (a) a 7.50% investment rate of return compounded annually and (b) salary increases of 9.50% for each of the first four years of service, 6.50% for the fifth year, 5.50% for each of the next five years, 5.00% for each of the next 15 years and 3.50% annually thereafter. Three years of trend information is as follows:

| Fiscal Years Ending | Annual Pension Cost (APC) | % of APC Contributed | Net Pension Obligation |
|--------------------------------|--------------------------------------|---------------------------------|-----------------------------------|
| 2010 | \$ 2,019,123 | 100% | NONE |
| 2011 | 2,140,299 | 100% | NONE |
| 2012 | 2,258,322 | 100% | NONE |

The following is the funded status information for the plan as of July 1, 2011 and two preceding years:

| | (1) | (2) | (3) | (4) | (5) | (6) |
|--------------------------|--|--|--|--|----------------------------|--|
| As of July 1, | Actuarial Value of Assets | Actuarial Accrued Liability (AAL) | Percentage Funded (1)/(2) | Unfunded AAL (UAAL) (2)-(1) | Covered Payroll | UAAL as a Percentage of Covered Payroll ((2-1)/5) |
| 2009 | \$31,366,930 | \$45,900,102 | 68.3% | \$14,533,172 | \$ 6,636,738 | 219.0% |
| 2010 | 32,478,788 | 47,756,509 | 68.0% | 15,277,721 | 6,728,974 | 227.0% |
| 2011 | 34,629,058 | 50,273,394 | 68.9% | 15,644,336 | 6,942,604 | 225.3% |

HARFORD COUNTY, MARYLAND SHERIFF'S OFFICE PENSION SYSTEM

Notes to the Financial Statements

June 30, 2012

4. REQUIRED SUPPLEMENTARY INFORMATION

Required supplementary information is designed to provide information about the Plans progress in accumulating sufficient assets to pay benefits when due. Ten years of trend data is presented as required supplementary information.

REQUIRED SUPPLEMENTARY INFORMATION

HARFORD COUNTY, MARYLAND SHERIFF'S OFFICE PENSION SYSTEM

**Schedule of Funding Progress (unaudited)
June 30, 2012**

| | (1) | (2) | (3) | (4) | (5) | (6) |
|----------------------|----------------------------------|--|----------------------------------|------------------------------------|------------------------|--|
| As of July 1, | Actuarial Value of Assets | Actuarial Accrued Liability (AAL) | Percentage Funded (1)/(2) | Unfunded AAL (UAAL) (2)-(1) | Covered Payroll | UAAL as a Percentage of Covered Payroll ((2-1)/5) |
| 2002 | \$ 19,084,468 | \$ 33,135,041 | 57.6% | \$ 14,050,573 | \$15,054,891 | 93.3% |
| 2003 | 22,205,448 | 40,090,697 | 55.4% | 17,885,249 | 15,082,253 | 118.6% |
| 2004 | 25,066,065 | 46,834,894 | 53.5% | 21,768,829 | 15,921,090 | 136.7% |
| 2005 | 29,066,454 | 60,388,789 ¹ | 48.1% | 31,322,335 | 17,077,674 | 183.4% |
| 2006 | 24,009,239 | 37,394,897 ² | 64.2% | 13,385,658 | 4,828,725 | 277.2% |
| 2007 | 26,445,775 | 40,988,678 | 64.5% | 14,542,903 | 6,222,088 | 233.7% |
| 2008 | 29,402,030 | 43,903,198 | 67.0% | 14,501,168 | 6,863,159 | 211.3% |
| 2009 | 31,366,930 | 45,900,102 | 68.3% | 14,533,172 | 6,636,738 | 219.0% |
| 2010 | 32,478,788 | 47,756,509 | 68.0% | 15,277,721 | 6,728,974 | 227.0% |
| 2011 | 34,629,058 | 50,273,394 | 68.9% | 15,644,336 | 6,942,604 | 225.3% |

1 Represents increase in plan's cost of living adjustment from a maximum 1.5% to a maximum of 3% per year.

2 Adjusted by the accrued transfer of assets to the state LEOPS as of July 1, 2006.

HARFORD COUNTY, MARYLAND SHERIFF'S OFFICE PENSION SYSTEM

Schedule of Employer Contributions (unaudited) June 30, 2012

| Years Ended June 30, | Annual Required Contribution | Percentage Contributed |
|-------------------------------------|---|-----------------------------------|
| 2003 | \$ 2,118,700 | 100% |
| 2004 | 2,126,895 | 100% |
| 2005 | 3,372,995 | 100% |
| 2006 | 4,789,795 | 100% |
| 2007 | 1,410,000 | 100% |
| 2008 | 2,388,571 | 100% |
| 2009 | 2,745,971 | 100% |
| 2010 | 2,019,123 | 100% |
| 2011 | 2,140,299 | 100% |
| 2012 | 2,258,322 | 100% |

The information presented in the required supplemental schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation is as follows:

| | |
|-------------------------------|---|
| Valuation date | July 1, 2011 |
| Actuarial cost method | Projected Unit Credit Method |
| Amortization method | Level Percentage of Payroll |
| Remaining amortization period | Original Unfunded Liability established 7/1/97—10 years remaining Buck to Mercer Conversion established 7/1/98—10 years remaining Assumption Change as of 7/1/98—10 years remaining Assumption Change as of 7/1/99—10 years remaining Plan Change established 7/1/02—20 years remaining Assumption Change as of 7/1/04—22 years remaining Plan Change established 7/1/05—23 years remaining Plan Change established 7/1/06—24 years remaining Assumption Change as of 7/1/07—25 years remaining Assumption Change as of 7/1/10—28 years remaining Plan Change as of 7/1/11—29 years remaining Assumption Change as of 7/1/11—29 years remaining Cumulative actuarial (gain)/loss combined 7/1/11—15 years remaining |
| Asset valuation method | 5-year Smoothed Market |

HARFORD COUNTY, MARYLAND SHERIFF'S OFFICE PENSION SYSTEM

Schedule of Employer Contributions (unaudited) June 30, 2012

Actuarial assumptions:

| | |
|--|---|
| Investment rate of return | 7.5%, compounded annually, gross of investment expenses |
| Projected salary increases | 9.50% for each of the first four years of service, 6.50% for the fifth year, 5.50% for each of the next five years, 5.00% for each of the next fifteen years, and 3.50% annually thereafter |
| Post Retirement Cost-of-Living Adjustments | 3% |