

Audited Financial
Statements – Retiree | June 30,
Health Plan Trust – 2017
Fiduciary Fund

WCPS | Washington County
Public Schools

CONTENTS

	PAGE
INDEPENDENT AUDITOR'S REPORT	1-2
FINANCIAL STATEMENTS	
<i>Fund Financial Statements</i>	
Statement of Net Position – Retiree Health Plan Trust -Fiduciary Fund	3
Statement of Changes in Net Position – Retiree Health Plan Trust - Fiduciary Fund	4
<i>NOTES TO FINANCIAL STATEMENTS</i>	5 - 9
REQUIRED SUPPLEMENTARY INFORMATION (UNAUDITED)	
Other Post-Employment Benefit Plan	
Schedule of Changes in the Net OPEB Liabilities and Related Ratios	10
Schedule of School System Contributions	11
Schedule of Investment Returns	12
<i>Independent Auditor's 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</i>	13-14



INDEPENDENT AUDITOR'S REPORT

Members of the Board
Washington County Board of Education
Hagerstown, Maryland

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying statement of net position and changes in net position of the Retiree Health Plan Trust fiduciary fund of the Washington County Board of Education, a component unit of Washington County, Maryland, as of and for the year ended June 30, 2017, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to an express 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 auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the 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 respective net position of the Retiree Health Plan Trust fiduciary fund of the Washington County Board of Education as of June 30, 2017, and the respective changes in financial position thereof for the year then ended in conformity 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 required supplementary information on pages 12 through 13 be presented to supplement the basic 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 basic 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 basic financial statements, and other knowledge we obtained during our audit of the basic 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.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the Retiree Health Plan Trust – Fiduciary Fund and do not purport to, and do not present fairly the financial position of the Washington County Board of Education, as of June 30, 2017, the changes in its financial position, or, where applicable, its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

OTHER REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued a report dated November 13, 2017, on our consideration of Washington County Board of Education's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing on internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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 Washington County Board of Education's internal control over financial reporting and compliance.



Hagerstown, Maryland
November 13, 2017

WASHINGTON COUNTY BOARD OF EDUCATION
Statement of Net Position – Retiree Health Plan Trust - Fiduciary Fund
June 30, 2017

	<u>2017</u>
ASSETS	
Investments held in MABE Trust	<u>\$ 55,491,863</u>
TOTAL ASSETS	<u><u>\$ 55,491,863</u></u>
NET POSITION	
Held in trust for retiree health plan benefits	<u>\$ 55,491,863</u>
TOTAL LIABILITIES AND NET POSITION	<u><u>\$ 55,491,863</u></u>

WASHINGTON COUNTY BOARD OF EDUCATION
Statement of Changes in Net Position - Retiree Health Plan Trust - Fiduciary Fund
Year Ended June 30, 2017

	2017
ADDITIONS	
Contributions	\$ 13,884,585
Net investment portfolio results	<u>6,509,385</u>
TOTAL ADDITIONS	20,393,970
DEDUCTIONS	
Benefits paid	<u>9,107,020</u>
TOTAL DEDUCTIONS	<u>9,107,020</u>
Change in Net Position	11,286,950
NET POSITION - BEGINNING OF YEAR	<u>44,204,913</u>
NET POSITION - END OF YEAR	<u><u>\$ 55,491,863</u></u>

WASHINGTON COUNTY BOARD OF EDUCATION
Notes to Financial Statements
June 30, 2017

NOTE 1 OVERVIEW AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Plan Description

The School System provides post-employment health care and life insurance benefits (OPEB) for retired employees, their spouses and dependents, and surviving spouses and dependents. On April 15, 2008, the Board created the Retiree Benefit Trust of the Board of Education of Washington County (the "Trust") in order to arrange for the establishment of a reserve to pay health and welfare benefits for future retirees. The Trust is affiliated with the Maryland Association of Boards of Education Pooled OPEB Investment Trust. The Board reserves the right to establish and amend the provisions of the trust with respect to participants, any benefit provided thereunder, or its participation therein, in whole or in part at any time, by resolution of its governing body and upon advance written notice to the Trustees. The Maryland Association of Boards of Education Pooled OPEB Investment Trust issues an annual financial report for the Trust. That report may be obtained by writing to Maryland Association of Boards of Education, 621 Ridgely Avenue, Suite 300, Annapolis, Maryland 21401, or by calling 1-800-841-8197.

A member may retire after 25 years of service from the Retirement System, and as early as age 55 and 15 years of service from the Pension system. Retirees can continue the same medical coverage they had (including family coverage) as active employees. Retirees receive a subsidy for their post-retirement medical insurance based on points (Age + Service). A minimum of 66 points (with 5 years of service) is required to receive a subsidy. The maximum subsidy of 85% is reached at 85 points (note that this is a blended subsidy percentage based on the subsidy for each plan and the current enrollment distribution). Retirees with less than 66 points are allowed access, but must pay 100% of the published rates.

Fiduciary Fund

The Retiree Health Plan Trust Fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. This fund was established to prefund other postemployment benefits (OPEB) that the School System provides to retirees of the School System and their dependents. It consists of contributions of the Board to establish a reserve to pay health and welfare benefits of future retirees. Contributions to the Trust qualify as contributions and are reported as additions using the economic resource measurement focus and the accrual basis of accounting, under which expenses (deduction) are recorded when the liability is incurred or the benefits are paid.

By definition, Fiduciary Fund assets are being held for the benefit of the third party and cannot be used to satisfy obligations of the School System.

WASHINGTON COUNTY BOARD OF EDUCATION
Notes to Financial Statements
June 30, 2017

NOTE 1 OVERVIEW AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Post-Employment Benefits

The School System partially supports the group insurance plan for retired employees. Eligibility is determined by a point system based on a retiree's age at the date of retirement and the number of years of service with the School System. The School System pays up to a maximum of 85% of the premium of the standard plan, based on the points earned. There were 1,929 eligible retirees and their dependents at June 30, 2017. Total claims paid on behalf of retirees amounted to \$12,725,487 of which \$3,618,467 was reimbursed through contributions received from retirees for the year ended June 30, 2017.

Funding Policy

The School system is required to recognize the *annual required contribution of the employer (ARC)*, an amount actuarially determined in accordance with the parameters of GASB accounting standards. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years.

NOTE 2 POST-EMPLOYMENT HEALTHCARE AND LIFE INSURANCE PLAN

Funded Status and Funding Progress

The funded status of the plan as of June 30, 2017, was as follows:

Total OPEB liability	\$ 293,815,000
Value of plan assets	<u>55,491,863</u>
Net OPEB liability	<u><u>\$ 238,323,137</u></u>
 Funded ratio (actuarial value of plan assets/AAL)	 18.89%

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectation and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

WASHINGTON COUNTY BOARD OF EDUCATION
Notes to Financial Statements
June 30, 2017

NOTE 2 POST-EMPLOYMENT HEALTHCARE AND LIFE INSURANCE PLAN (CONTINUED)

Investments

The MABE Trust’s policy is regard to the allocation of invested assets is established any may be amended by the Trustees by a majority vote of its members. It is the policy of the Trust to pursue an investment strategy that emphasizes growth of principal while avoiding excess risk. Short-term volatility will be tolerated inasmuch as it is consistent with the volatility of a comparable market index. The MABE Trust’s investment policy discourages the use of cash equivalents, except for liquidity purposes and aims to refrain from dramatically shifting asset class allocations over short time spans. The following is the MABE Trust’s adopted asset allocation policy as of June 30, 2017:

Asset Class	Target Allocation
Equity	59.90%
Fixed income	37.10%
Cash	3.00%
Total	100.00%

Rate of Return

For the year ended June 30, 2017, the annual money-weighted rate of return on investments, net of investment expense, was 11.30%. The money-weighted rate of return expresses investment performance, net of investment expense, adjusted for the changing amounts actually invested.

Investment in External Investment Pool

The School System has funds designated for Other Postemployment Benefits (OPEB) that are held by Maryland Association of Board of Education (MABE) in the MABE OPEB Trust (MABE Trust). The MABE Trust is administered by the MABE and is a wholly-owned instrumentality of its members. The nine members who are sole contributors to the MABE Trust are the board of education of the following counties in Maryland: Allegany, Allegany Fiduciary Fund, Caroline, Cecil, Charles, Harford, Kent, Prince George’s, St. Mary’s and Washington.

The investments of the MABE Trust are stated at fair value and are managed by the Wells Fargo Advisors and consist of money market funds, U.S. government and agency fixed income and asset backed securities, equity securities, mutual funds and exchange traded funds, corporate bonds and corporate asset backed securities and municipal bonds. The MABE Trust categorizes its fair value measurements within the fair value hierarchy established by GAAP. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; and Level 3 are significant unobservable inputs. Although all investments of the MABE Trust are considered Level 1 and Level 2, the School System’s membership in the MABE Trust is considered Level 2. As of June 30, 2017, the pooled net

WASHINGTON COUNTY BOARD OF EDUCATION
Notes to Financial Statements
June 30, 2017

NOTE 2 POST-EMPLOYMENT HEALTHCARE AND LIFE INSURANCE PLAN (CONTINUED)

position of the MABE Trust was \$292,672,933 in total, of which the School System's allocated investment balance was \$55,491,863. The School System may terminate its membership in the MABE Trust and withdraw its allocated investment balance by providing written six months prior to the intended date of withdrawal.

The MABE Trust is audited annually by an independent CPA firm. Since 2010, Arthur Bell and Associates of Hunt Valley, Maryland perform the services. The audit report is usually issued by September 1st of each year, a copy of which can be obtained by sending a request to the following address: Administrator of the MABE Pooled Investment Trust, 621 Ridgely Road, Suite 300, Annapolis, MD 21401-1112.

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation and the members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

The medical trend assumption was developed using the Society of Actuaries (SOA) Long-Run Medical Cost Trend Model (released in 2015). The following assumptions were used as input variables into this model:

Rate of inflation	2.3%
Rate of growth in real income/GDP per capita	0.7%
Extra trend due to technology and other factors	1.3%
Expected health share of the GDP in 2020	18.5%
Health share of GDP resistance point	25.0%
Year for limiting cost growth to GDP growth	2075

The SOA Long-Run Medical Cost Trend Model and its baseline projection are based on an econometric analysis of historical U.S. medical expenditures and the judgements of experts in the field. The rate of growth in Real Income was reduced from the baseline assumptions of 1.5% to 0.7% to be consistent with the long-term payroll growth assumption of 3.0% (2.3% inflation plus .7% real wage growth). The long-run baseline projection and input variables have been developed under the guidance of an SOA Project Oversight Group. This model was updated to reflect the future Cadillac Tax. Under the new upcoming GASB 75 standards, the asset returns rate of inflation should be equal to the rate of the inflation used in the Society of Actuaries (SOA) Long-Run Medical Cost Trend Model.

Total payroll is assumed to increase 3% per year. This assumption is used to determine the amortization factor.

WASHINGTON COUNTY BOARD OF EDUCATION
Notes to Financial Statements
June 30, 2017

NOTE 2 POST-EMPLOYMENT HEALTHCARE AND LIFE INSURANCE PLAN (CONTINUED)

Best estimates of real rates of return for each major asset class included in the target asset allocation as of June 30, 2017 (see the discussion of the MABE Trust's investment policy) are summarized in the following table:

Asset Class	Long-Term Expected Real Rate of Return
Equity	5.73%
Fixed income	2.48%
Cash	1.00%

The discount rate used to determine the total OPEB liability was 5.5% for the year ended June 30, 2017. The benefit payment stream for the Plan is discounted based on an index rate for 20-year tax exempt general obligation municipal bonds with an average rate of AA/Aa or higher for years when the projected benefit payouts are expected to be unfunded and 6.9% for years when the projected benefit payouts are expected to be funded.

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

The following presents the net OPEB liability of the School System, as well as what the School System's net OPEB liability would be if it were calculated using a discount rate that is 1-percentage-point lower (4.5%) or 1-percentage-point higher (6.5%) than the current discount rate:

	1% Decrease to 4.5%	Discount Rate of 5.5%	1% Increase 6.5%
Net OPEB liability	\$284,544,140	\$238,323,140	\$200,797,140

Sensitivity of the net OPEB liability to changes in the healthcare cost trends rates

The following presents the net OPEB liability of the School System, as well as what the School System's net OPEB liability would be if it was calculated using the healthcare cost trend rates that are 1-percentage-point lower (3.9% decreasing to 2.9) or 1-percentage-point higher (3.9% increasing to 4.9) than the current healthcare cost trend rates:

	1% Decrease rate in 2075 of 2.9%	Health Care Cost Trend Rate of 2075 of 3.9%	1% Increase rate in 2075 of 4.9%
Net OPEB liability	\$196,050,140	\$238,323,140	\$292,322,140

WASHINGTON COUNTY BOARD OF EDUCATION
Required Supplementary Information
For Other Postemployment Benefit Plan
Last 10 Fiscal Years* (Unaudited)

Schedule of Changes in the Net OPEB Liability and Related Ratios
Last 10 Fiscal Years

	2017
Total OPEB liability	
Service cost	\$ 7,943,000
Interest	14,681,000
Changes of benefit terms	-
Difference between expected and actual experiences	3,092,020
Changes of assumptions	(25,134,000)
Benefit payments	(9,107,020)
Net change in total OPEB liability	(8,525,000)
Total OPEB liability - beginning	302,340,000
Total OPEB liability - ending	<u>\$ 293,815,000</u>
 Plan Fiduciary Net Position	
Contributions - employer	\$ 13,884,585
Net investment income	6,509,385
Benefit payments	(9,107,020)
Net change in plan fiduciary net position	11,286,950
Plan fiduciary net position - beginning	44,204,913
Plan fiduciary net position - ending	<u>\$ 55,491,863</u>
School System's net OPEB liability - ending	<u>\$ 238,323,137</u>
Plan fiduciary net position as a percentage of the total OPEB liability	18.89%
Covered employee payroll	\$ 158,314,625
 School System's net OPEB liability as a percentage of covered-employee payroll	150.54%

* Information for fiscal year 2016 and prior is not available

WASHINGTON COUNTY BOARD OF EDUCATION
Required Supplementary Information
For Other Postemployment Benefit Plan
Last 10 Fiscal Years* (Unaudited)

Schedule of School System Contributions
Last 10 Fiscal Years

	2017
Actuarially determined contribution	\$ 29,162,000
Contributions in relation to the actuarially determined contribution	13,884,583
Contribution deficiency (excess)	<u>\$ 15,277,417</u>
Covered - employee payroll	158,314,625
Contribution as a percentage of covered employee payroll	8.77%

*Information for fiscal year 2016 and earlier is not available

WASHINGTON COUNTY BOARD OF EDUCATION
Required Supplementary Information
For Other Postemployment Benefit Plan
Last 10 Fiscal Years* (Unaudited)

Schedule of Investment Returns
Last 10 Fiscal Years

	2017
Annual money-weighted rate of return, net of investment expense	11.30%

*Information for fiscal year 2016 and earlier is not available



**INDEPENDENT AUDITOR'S 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***

Members of the Board
Washington County Board of Education
Hagerstown, Maryland

We have audited, 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, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Washington County Board of Education (School System), a component unit of Washington County, Maryland, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the School System's basic financial statements and have issued our report thereon dated September 21, 2017.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements, we considered the School System'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 School System's internal control. Accordingly, we do not express an opinion on the effectiveness of the School System'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 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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. 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 School System's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants 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 results of that testing, and not to provide an opinion on the effectiveness of the entity'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 entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Smith Elliott Heavens & Company, LLC

Hagerstown, Maryland
November 13, 2017