



**HMEPS**  
HOUSTON MUNICIPAL EMPLOYEES PENSION SYSTEM

YOUR FUTURE  
IS WHAT  
KEEPS US  
MOVING  
FORWARD

Houston, Texas

A Component Unit of the  
City of Houston, Texas

2014 **REPORT TO PARTICIPANTS**

**THE CONSTANT NORTH STAR IS ONE OF  
MANKIND'S MOST DEPENDABLE GUIDES.**



**HMEPS**

HOUSTON MUNICIPAL EMPLOYEES PENSION SYSTEM

# CONTENTS

## INTRODUCTION

Letter from the Chairman .....	2
Board of Trustees .....	3
Organizational Overview .....	4
The Staff .....	5

## PARTICIPANT OVERVIEW

Participant Data .....	8
Schedule of Annuitants By Type .....	8
Historical Active Participant Data .....	8

HISTORICAL TIMELINE .....	9
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## INVESTMENTS

System Asset Allocation .....	11
Comparison of Investment Returns – Years Ended June 30 .....	12

## FINANCIALS

Summary Comparative Financial Statements .....	13
Schedule of Changes In Fiduciary Net Position (\$000) .....	14
Historical Actuarial Funding Ratio .....	15
HMEPS Honors Amy Rowley .....	16



### Note to Participants

We prepared this report for our participants to serve as a summary of the primary investment, benefit and financial information you care about. All the information in this report is derived from our Comprehensive Annual Financial Report (CAFR) and is consistent with Generally Accepted Accounting Principles (GAAP). All financial information is as of June 30, 2014. (The full CAFR is available on our website at [www.hmeps.org/publications.html](http://www.hmeps.org/publications.html).)



*Mecom Fountain*



# LETTER FROM THE CHAIRMAN

January 15, 2015

Dear Participants,

I am proud to present the 2014 Report to Participants, which summarizes the HMEPS 2014 Comprehensive Annual Financial Report (CAFR) and provides an overview of our operations.

HMEPS has accomplished a great deal in 2014 in the midst of the ongoing challenging environment for public employee pension systems nationwide. Thanks to the dedication and hard work of the HMEPS Board of Trustees and staff, we continued to provide first-class service to our participants while strengthening the System for the future. As we begin the new calendar year, I am confident HMEPS is well-positioned for 2015 and beyond.

I am delighted to report on HMEPS' outstanding investment performance for Fiscal Year 2014 in which the System achieved an all-time high of \$2.4 billion in assets and a 16.42 percent investment return, gross of fees. HMEPS' strong investment performance is nothing new. The System's 10-, 20- and 25-year returns exceed the 8.5 percent return target, placing HMEPS in the top quartile among its peers.

At HMEPS, we strive to attain the highest standards of accountability, integrity and openness by applying rigorous controls within the System. HMEPS' efforts were once again recognized by the Government Finance Officers Association (GFOA) of the United States and Canada, which for the 20th year in a row awarded HMEPS a Certificate of Achievement for Excellence in Financial Reporting.

During the year, pension systems across the nation continued to face unfair attacks, and HMEPS was no exception. We have stepped up our efforts to respond to misleading or inaccurate comments and reports about the System, and continue to be proactive in telling HMEPS' positive story to policymakers, our participants and the public at large. With the opening of the 84th Session of the Texas Legislature we will continue to be vigilant in monitoring and engaging on pension-related legislation as it arises.

We also have expanded and improved our overall communications efforts. In 2014, we rolled out an upgraded, interactive website at [www.hmeps.com](http://www.hmeps.com), increased messaging via e-blast and grew our social media presence on Facebook and Twitter. In addition, our annual Financial Retirement Employees Educational (F.R.E.E.) Summit, held each Fall, has become so popular that we added a second Spring event, which was also very successful.

Finally, I want to highlight that in December 2014, Houston City Council adopted a new Financial Policies statement for the first time in over a decade. Included in the statement is a greater emphasis on long-term budgetary planning and forecasting, as well as a commitment to "fully and systematically" fund pension system liabilities. I commend City Council for being proactive about its obligations and its commitment to strengthening the System for the long term and we at HMEPS will continue to communicate with City leaders to help them appropriately measure and plan for the City's obligation to the fund.

We look forward to a successful 2015, in which we will continue to work to protect and grow the System for our participants, to communicate effectively about pension issues, and to monitor and engage on legislation and other efforts regarding pensions. We will work diligently to protect your benefits today and for decades to come.

As always, it is an honor to serve as your Chairman.

Sincerely,

Sherry Mose  
Chairman



# BOARD OF TRUSTEES

## ORGANIZATIONAL OVERVIEW

At the heart of HMEPS is the hard work and dedication of everyone who serves it, beginning with the Board of Trustees. A significant responsibility of the Board is to ensure that HMEPS has in place an adequate system of internal controls. The majority of the Board's work is conducted at the Board level and within six committees, each of which addresses a specific aspect of the System's operations.

### Board of Trustees | Elected and Appointed Trustees



Sherry Mose  
Chairman



Roy W. Sanchez  
Vice Chairman



Lonnie Vara  
Secretary



David L. Long  
Elected Trustee



Asha Patnaik  
Elected Trustee



Lenard Polk  
Elected Trustee

MOVING TOWARD  
ACHIEVING A BETTER  
TOMORROW



Allen Parkway

- The **Audit Committee** reviews and monitors the System's audit process and oversees the reporting of financial information for HMEPS.
- The **Budget and Oversight Committee** reviews and monitors HMEPS' operational and administrative expenditures, as well as its actuarial process.
- The **Disability Committee** reviews the submitted medical reports and other relevant information for each disability claim and makes recommendations to the Board as to the appropriate course of action.
- The **External Affairs Committee** deals with matters concerning state and federal legislative issues that affect

HMEPS and any agreement or proposed agreement with the City regarding pension issues and benefits.

- The **Investment Committee** reviews investment strategies and has authority over HMEPS' asset allocation, tactical asset allocation, managers and other aspects of HMEPS' operations relating to investments. The Investment Committee is a committee of the entire Board.
- The **Personnel and Procedures Committee** deals with matters concerning HMEPS' employees, changes in policies in the workings of HMEPS, and constructing the procedures for HMEPS' adherence to applicable laws.



Barbara Chelette  
Appointed Trustee



Richard Badger  
Council Appointee



Edward J. Hamb II  
Controller Appointee



Craig T. Mason  
Mayoral Appointee



Adrian Patterson  
Council Appointee



Rhonda Smith  
Executive Director

## Administrative Organization

### Board

Audit Committee  
Budget and Oversight Committee  
Disability Committee  
External Affairs Committee  
Investment Committee  
Personnel and Procedures Committee

### Executive Director

**General Counsel**  
**Chief Investment Officer**  
Investment Managers' Services  
Market Research  
Performance Measurement  
**Financial Division**  
Financial Reporting and Analysis  
Internal Audit and Compliance

### Member Services

Benefit Administration Services  
Member Services  
Financial Counseling  
Communications  
**Information Systems**  
Technology Support  
Records



# THE STAFF

HMEPS' experienced staff members provide expert advice to the Board and make informed decisions every day on a wide range of issues important to the fund and its participants. These individuals are talented professionals who bring their very best to the pension system each day.

## Member Services

The **Member Services** division is responsible for serving the needs of our participants on a daily basis. The division's benefits section oversees members' needs from the time they enter the system through retirement, providing them the support



Tammy Conson,  
Accounting Assistant

needed to understand and access their benefit options.

The Benefits Division has continued its effort to provide information relating to pension benefits by holding seminars in the field and individual benefit meetings at HMEPS. In FY 2014, HMEPS:

- Responded to continued demand for the Outreach Program, which reaches hundreds of members with individual and group sessions provided by our benefits counselors and our Certified Financial Planner. This past year, these staff members conducted 410 individual counseling sessions and hosted 63 joint presentations for various City departments as well as new employee orientations for the benefit of 2,008 attendees. A growing number of participants requested financial counseling based on other participants' recommendations.
- Processed 1,896 benefit applications for the Deferred Retirement Option Plan (DROP) and payroll, including retirements, survivor benefits, refunds, and lump-sum payments.

- Continued social media efforts to provide information relating to pension benefits to participants through Facebook and Twitter, two platforms that provide methods of communicating and interacting with participants.
- Participated in the Spring and Fall Financial Retirement Employees Educational Summits, annual events that help City of Houston employees better plan their financial futures.
- The HMEPS financial counselor conducted 343 one-on-one counseling sessions with participants during the past fiscal year in addition to numerous group presentations. He also monitored pension-related issues nationally and locally, a critical part of fulfilling HMEPS' obligation to keep participants fully informed.

## Investment Division

The **Investment** division develops and implements investment strategies to maximize returns while minimizing risks. This division is responsible for portfolio management and is charged with effectively and prudently investing and monitoring HMEPS' assets while adhering to laws, regulations and policy guidelines.

The System's strategic asset allocation policy is designed to manage risk



Brad Bangen,  
Financial Analyst



by diversifying among public and private asset classes. The strategic asset allocation policy was reevaluated in April 2013. Risk-return assumptions and correlations for asset classes



Chandra Livingston,  
Accounting Manager

were reexamined taking into account current and forecasted economic conditions. A new policy was adopted with the following changes: U.S. Equity and non-U.S. Equity were combined into a single asset class, Global Equity, with the combined target weight being reduced to 35% from 40%. The target allocation to Fixed Income was reduced from 20% to 15%, while Real Estate was reduced from 12% to 10% and Private Equity from 18% to 17.5%. The two asset classes which received an increased target allocation were Absolute Return, which went from 5% to 10% and Inflation Linked Asset Class (ILAC) which increased from 5% to 12.5%. This new asset allocation policy went into effective at the beginning of the fiscal year, on July 1, 2013.

The System's investment portfolio closed its 2014 fiscal year at \$2.46 billion, up from \$2.2 billion at the beginning of the year. The total investment return for the fiscal year was 16.4%. The best performing asset classes for fiscal year 2014 were ILAC (+22.3%) and Global Equity (+21.9%). The System's investment performance was 9.7%, 12.6% and 9.3% for the past three-, five- and ten-year periods. The System outperformed the policy benchmark for fiscal year 2014, in addition to outperforming for the longer ten-year period. Compared to similar investment portfolios (TUCS Master Trusts - Public), the fund posts attractive investment returns over the long term. The Fund ranks in the top decile over the trailing ten-year period ending June 30, 2014.

### Financial Division

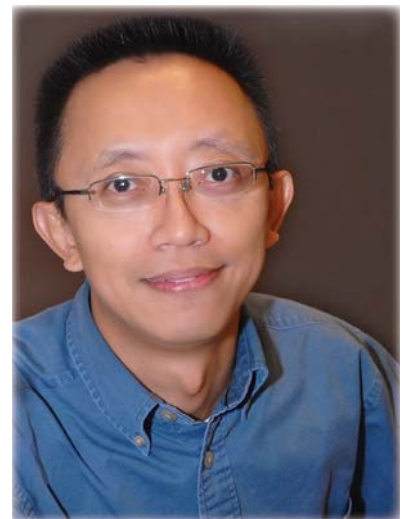
The **Financial** division manages the accounting, budgeting, retiree payments, internal audit and financial reporting functions at HMEPS.

In FY 2014, the Financial division changed to a new enterprise software platform that allows transactions to be integrated with other internal databases thereby improving processing efficiency. In FY2015, the Financial division will continue to innovate internal processes by integrating with the databases at the custodial bank.

### Information Systems Division

The **Information Systems** division is responsible for the technology that is critical to serving HMEPS' participants.

In FY 2014, the Information Systems division replaced the organization's existing server infrastructure with a virtual architecture to improve computer processes and data systems, and to help improve future restoration of the HMEPS computing infrastructure in the event of a major disruption. In the year



Myo Htut,  
Network Administrator

ahead, we will be adding several business continuity components to improve computer services.

### Legal Division

The **Legal** division works with all HMEPS divisions as well as the Board to help ensure that the System is providing the best service possible to our members in compliance with federal, state and local laws.



# PARTICIPANT OVERVIEW

## AS OF JULY 1, 2013 THERE WERE 26,763 PARTICIPANTS IN HMEPS

Our members come from all City departments and serve their communities' diverse and special needs night and day, in good weather and bad – each contributing their special skills to make Houston a great place to live. The System is honored to serve each and every one of our hardworking members.

The System is a defined benefit pension plan covering all municipal employees, except police officers and firefighters (other than certain police officers in the System as authorized by the Pension Statute), employed full time by the City of Houston, elected City Officials, and the full time employees of the System. The System includes a contributory group (Group A) and two noncontributory groups (Group B and Group D) and provides service, disability and death benefits for eligible participants.

As of July 1, 2013, there were 26,763 participants in HMEPS. Included in this figure are active members, inactive participants, service retirees, disabled retirees and beneficiaries and spouses. Of the 11,781 active employees, 6,364 are male and 5,417 are female. HMEPS also serves 7,258 service retirees, 387 disabled retirees, 1,782 beneficiaries, and 5,555 inactive participants.



## PARTICIPANT DATA AS OF JUNE 30, 2013

PARTICIPANT DATA					
	Number	Number Vested	Average Salary or Annual Benefit	Average Age	Average Service
Active Members	11,781	8,627	\$46,683	46.9	11.1
Inactive Participants	5,555	3,298	6,906	—	—
Service Retirees	7,258	—	23,458	68.3	—
Disabled Retirees	387	—	9,827	64.3	—
Beneficiaries & Spouses	1,782	—	13,452	69.6	—

SCHEDULE OF ANNUITANTS BY TYPE						
	June 30, 2013			June 30, 2012		
	Number	Benefits (\$000)	Average Benefit	Number	Benefits (\$000)	Average Benefit
<b>SCHEDULE OF ANNUITANTS BY TYPE</b>						
Retirees Receiving Benefits	7,258	170,255	23,458	7,031	162,527	23,116
Retired on Disability	387	3,803	9,827	391	3,814	9,755
Survivors and Beneficiaries	1,782	23,972	13,452	1,656	21,174	12,786
Total Retirees, Survivors and Beneficiaries	9,427	198,030	21,007	9,078	187,515	20,656
Former Participants Eligible But Not Yet Receiving Benefits	3,298	22,776	6,906	3,237	21,912	6,769
Total Eligible for Benefits	12,725	220,806	53,643	12,315	209,427	17,006

HISTORICAL ACTIVE PARTICIPANT DATA								
Valuation Date	Active Vested/Nonvested			Number of Participants	Annual Payroll (\$000)	Average Salary (\$)	% Salary Increase	
	Group A	Group B	Group D					
July 1, 2004	8,361	3,495		11,856	366,190	30,886	(4.1)	
July 1, 2005	8,811	3,163		11,974	404,565	33,787	9.4	
July 1, 2006	9,544	2,601		12,145	422,496	34,788	3.0	
July 1, 2007	9,947	2,429		12,376	448,925	36,274	4.3	
July 1, 2008	9,587	2,195	871	12,653	483,815	38,237	5.4	
July 1, 2009	8,906	2,153	2,274	13,333	539,023	40,428	5.7	
July 1, 2010	8,323	1,999	2,591	12,913	550,709	42,648	5.5	
July 1, 2011	7,857	1,932	2,556	12,345	544,665	44,120	3.5	
July 1, 2012	7,167	1,759	2,744	11,670	534,394	45,792	3.8	
July 1, 2013	6,777	1,666	3,338	11,781	549,971	46,683	1.9	

Beginning with 2005, a change in methodology now annualizes payroll for new entrants. If the methodology had not been changed, the covered payroll for 2005 would have been \$376,208,345 and the average payroll would have been \$31,422.

All information was derived from the July 1, 2013 Actuarial Valuation.

# HISTORICAL TIMELINE

1943

HMEPS Established by Texas  
Legislature - May 24, 1943



1989

Pension Press first published

Assets increase 400% reaching  
\$546.3 million

1992

Roderick J. Newman elected as the  
first African-American to serve on  
HMEPS' Board



1997

Deferred Retirement Option  
Plan (DROP) implemented

Assets reach \$1.17 billion

Assets surpass  
\$10 million

1960

Membership reaches 4,000+  
participants

An employee retiring with 28 years  
of service receives a \$100 monthly  
pension.

1950



HMEPS and the City enter into  
Meet and Confer Agreement to  
restructure benefits and funding

2004



David L. Long hired as first  
Executive Director

1993

Group B created as first  
non-contributory group

1981



## 2011

Amended and Restated Meet and Confer Agreement provides structured increases to City of Houston's contributions to move towards full funding of the plan.



HMEPS' 10 year investment performance is top 1% of public funds

David L. Long retires after serving 16 years as Executive Director

## 2006

AccessHMEPS introduced online to DROP participants

HMEPS hosts the first Financial Fitness Expo



Rhonda Smith is named as HMEPS' Executive Director.

## 2012

HMEPS joins Facebook, Twitter and YouTube



Assets reach over \$2 billion

Average annuity for a retiree is \$22,783



Fred Holmes steps down as Chairman after serving 35 years as an HMEPS Trustee and Board Officer

Roderick J. Newman becomes first African-American Chairman



Sherry Mose is elected first female Chairman

Group D created as *new* non-contributory group



## 2008

HMEPS launches new and improved website, with advanced features and AccessHMEPS for all participants

HMEPS celebrates its 70th anniversary



50th edition of the Pension Press is published

HMEPS is recognized as one of five pension systems in the U.S. that implemented significant reforms that create a more fiscally sustainable retirement plan

## 2013

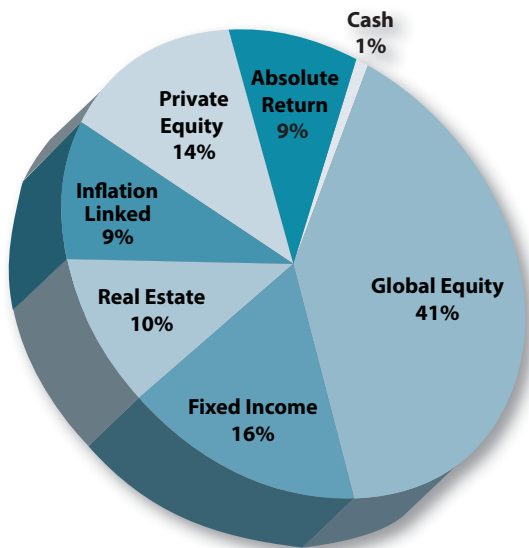


# INVESTMENTS

The 10-year period ended June 30, 2014 encompasses the 2008 financial crisis and has produced volatile returns, both for the markets as a whole, and also for the System. The System generated double digit positive returns in six of the past ten fiscal years, met or exceeded its policy index in six of the ten fiscal years, and outperformed its peer group in eight of those ten years. Due to the diversification of assets, the System's 10-year annualized return is 9.3%, in excess of its return target of 8.5%. The 20-year return stands at 9.4%.

An integral part of HMEPS' overall investment policy is its strategic asset allocation policy. The System's investment allocation provides an efficient diversification of assets designed to achieve portfolio risk and return objectives.

## SYSTEM ASSET ALLOCATION



As shown in the table on page 12, HMEPS' total fund return exceeds its policy portfolio over the last ten years. In addition, HMEPS' total fund performance compares very favorably to the median public fund, as represented by the TUCS Master Trusts – Public Universe, and has also outperformed this benchmark for the ten year period ending June 30, 2014. Over the ten-year period, HMEPS is in the top decile of funds in the TUCS Master Trusts – Public Universe.

The consistent long-term above-benchmark performance is best illustrated by the growth of \$1,000 invested in HMEPS' total fund, the policy benchmark portfolio and median public fund during the past 10 years. The ending points indicate that \$1,000 invested in HMEPS' total fund would have grown to \$2,145, while the same \$1,000 would have grown to \$1,964 and \$1,761 respectively in the policy benchmark portfolio and the median public fund.

## GROWTH OF \$1,000



# MOVING TOWARDS ACHIEVING A BETTER TOMORROW

## COMPARISON OF INVESTMENT RETURNS – YEARS ENDED JUNE 30

(Calculated based on a time-weighted rate of return based on the market rate of return)

	2014	3 Yrs.	5 Yrs.	10 Yrs.	2013	2012	2011	2010
Total Fund	16.39	9.70	12.60	9.31	13.58	-0.14	22.17	12.24
Actuarial Rate	8.5	8.5	8.5	8.5	8.5	8.5	8.5	8.5
Policy Portfolio	15.61	10.74	13.52	8.35	14.00	3.23	22.89	13.03
Median of Wilshire Public Fund Universe/TUCS	16.83	10.01	12.76	7.33	12.27	1.25	21.19	14.80
Global Equity	21.92	n/a	n/a	n/a	n/a	n/a	n/a	n/a
MSCI ACWI IMI	20.92	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Fixed Income	9.22	7.16	9.50	7.05	5.99	6.31	9.33	17.00
Barclays Capital Aggregate Bond Index	4.37	3.67	4.85	4.93	-0.69	7.48	3.90	9.50
Merrill Lynch High Yield Master II Index	11.80	9.27	13.94	8.90	9.57	6.51	15.40	27.53
HMEPS Private Equity	14.31	11.02	14.39	12.31	7.85	11.00	22.54	16.82
S&P 500 Index +3%	27.61	19.58	21.83	10.78	23.60	8.44	33.68	17.43
Real Estate	9.11	8.50	5.09	6.76	12.80	3.78	10.92	-9.52
NCREIF Property Index	11.21	11.32	9.67	8.63	10.73	12.00	16.73	-1.48
Inflation-Linked	22.33	3.02	13.17	n/a	14.52	-21.96	39.72	21.52
Consumer Price Index +4%	6.07	5.83	6.02	6.31	5.75	5.66	7.70	5.05
HMEPS Absolute Return	7.28	5.65	10.64	n/a	10.87	-0.86	13.94	23.39
LIBOR +4%	4.24	4.34	4.33	n/a	4.31	4.46	5.10	4.30

- HMEPS Assets
  - Benchmark



# FINANCIALS

Each year, HMEPS is subject to an independent external audit to review the System's financial statements to provide assurance that the statements are free of material misstatement. This outside opinion considers internal controls over financial reporting. All HMEPS divisions collaborate to produce the System's Comprehensive Annual Financial Report (CAFR). The System's CAFR is submitted to the Government Finance Officers Association (GFOA), which oversees governmental entity CAFR certification. For the 20th consecutive year, HMEPS received the GFOA Certificate of Achievement for Excellence in Financial Reporting for its thorough financial reporting work on the 2013 CAFR.

## Revenues (Additions) and Expenditures (Deductions)

The Summary Comparative Statement of Changes in Fiduciary Net Position table (see below) shows the Fund's primary income is derived from income appreciation on investments, and member and employer contributions. For 2014, net investment income was \$351.8 million dollars and total contributions were \$144.9 million dollars.

On the expenditure side, the majority of the fund's expenses were associated with participants' periodic and one-time (refund or DROP) payments of \$221.9 million, or 97% of total expenses. As shown in the table on page 14, the remainder of the fund's expenses is comprised of administrative expenses of \$5.8 million or 3% of total expenses, and professional fees of \$596,931 or 0.2% of total expenses.

## Financial Markets

During fiscal year 2014, United States equity markets continue to show strong gains despite anemic economic growth. Technology was the best performing sector, with utilities, health-care and energy also showing strong returns. Growth stock indexes led value oriented indexes by moderately large amounts with the Wilshire Large Growth composite up 29.7% vs. 20.7% for the Wilshire Large Value composite. Overall, the US Equity markets, as represented by the Wilshire 5000 index, finished the fiscal year with gains of 24.9%, posting the fifth consecutive positive fiscal year since the credit crisis of 2008-2009.

Turbulence was the theme in international markets. The escalation of tensions between Russia and Ukraine threatened to impact important energy trade flows between Eastern and

**SUMMARY COMPARATIVE STATEMENT OF FIDUCIARY NET POSITION (\$000)**

ASSETS	FY2014	FY2013
Cash and equivalents	\$ 401	\$ 6,167
Receivables on asset sales	12,066	12,395
Receivables on foreign exchanges	378	32
Other receivables	6,430	5,665
Investments	2,464,628	2,202,675
Collateral on securities lending	139,504	161,317
Furniture, fixtures and equipment, net	444	248
<b>Total Assets</b>	<b>2,623,851</b>	<b>2,388,499</b>
LIABILITIES		
Payable on asset purchases	14,147	25,458
Accrued liabilities	5,761	5,109
Collateral on securities lending	139,504	161,317
<b>Total Liabilities</b>	<b>159,412</b>	<b>191,884</b>
<b>FIDUCIARY NET POSITION</b>	<b>\$2,464,439</b>	<b>\$2,196,615</b>

**SUMMARY COMPARATIVE STATEMENT OF CHANGES IN FIDUCIARY NET POSITION (\$000)**

	FY2014	FY2013
<u>Additions</u>		
Contributions	\$ 144,854	\$ 128,900
Investment and interest (loss) income, net	351,793	263,890
Other income	730	1,246
<b>Total additions</b>	<b>497,377</b>	<b>394,036</b>
<u>Deductions</u>		
Benefits paid	221,925	213,178
Contribution refunds	1,213	1,266
Administration and professional fees	6,415	7,212
<b>Total deductions</b>	<b>229,553</b>	<b>221,656</b>
Net increase (decrease) in plan net position	267,824	172,380
Plan net position, beginning of year	2,196,615	2,024,235
<b>FIDUCIARY NET POSITION</b>	<b>\$2,464,439</b>	<b>\$2,196,615</b>



Western Europe, with much of the West proposing sanctions against Russia in response to its absorption of Crimea. The deterioration of Iraq's fragile regime fueled additional investor concern during the fiscal year. However, this turmoil barely provided a pause for global stock markets' upward march in the fiscal year 2014 as the MSCI All World ex-U.S. Index returned 21.8% for the fiscal year. Developed markets, particularly Europe, outperformed emerging markets for the year. Emerging markets lagged due to concern over the economic slowdown in China with the MSCI Emerging Markets Index returning 14.3%.

Fixed income markets reported moderate performance during the fiscal year aided by a modest fall in U.S. Treasury yields as U.S. Treasuries continued to be an attractive safe haven for investors concerned about political instability elsewhere. Overall, investment grade fixed income bonds, as represented by the Barclays U.S. Aggregate bond index, returned 4.4% for the fiscal year. Janet Yellen's initial public statements as the new chair of the U.S. Federal Reserve reassured markets that accommodative Fed monetary policy would stay in place.

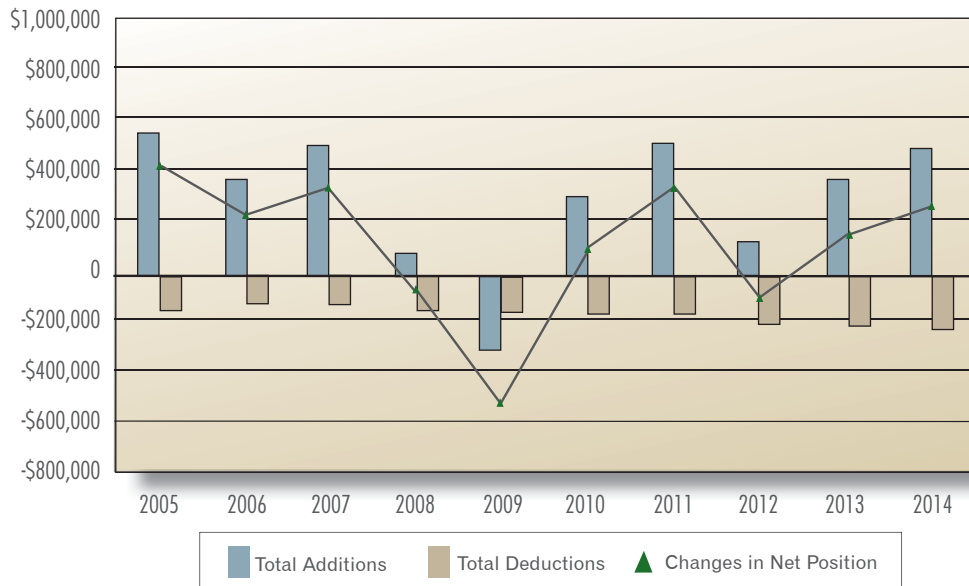
(Cont'd on the following page)

### SCHEDULE OF CHANGES IN FIDUCIARY NET POSITION (\$'000)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
<b>Additions</b>										
Employer contributions	363,247 <sup>1</sup>	66,968	70,265	73,272	76,837	82,052	87,285	97,161	111,859	128,274
Member contributions	23,488	21,888	20,966	21,176	20,449	19,736	19,326	18,473	17,041	16,580
Investment Income	184,419	272,766	337,259	(29,133)	(440,298)	195,433	391,095	(11,963)	263,891	351,793
Other income	17,250	26,950	29,031	29,839	489	557	1,185	654	1,246	730
<b>Total additions</b>	<b>588,404</b>	<b>388,572</b>	<b>457,521</b>	<b>95,154</b>	<b>(342,523)</b>	<b>297,778</b>	<b>498,891</b>	<b>104,325</b>	<b>394,037</b>	<b>497,377</b>
<b>Deductions</b>										
Benefit payments	175,480	154,311	157,716	169,483	180,361	191,048	189,199	200,014	213,178	221,925
Refund of contributions	992	1,037	1,398	1,760	1,795	1,285	1,620	2,206	1,266	1,213
Professional services fees	1,088	708	883	638	792	805	1,103	1,048	871	597
Cost of administration	4,718	5,072	5,223	5,837	6,420	6,290	6,020	6,264	6,341	5,818
<b>Total deduction</b>	<b>182,278</b>	<b>161,128</b>	<b>165,220</b>	<b>177,718</b>	<b>189,368</b>	<b>199,428</b>	<b>197,942</b>	<b>209,532</b>	<b>221,656</b>	<b>229,553</b>
<b>Changes in net position</b>	<b>406,126</b>	<b>227,444</b>	<b>292,301</b>	<b>(82,564)</b>	<b>(531,891)</b>	<b>98,350</b>	<b>300,949</b>	<b>(105,207)</b>	<b>172,381</b>	<b>267,824</b>
<b>Net position as of June 30</b>	<b>1,824,852</b>	<b>2,052,296</b>	<b>2,344,597</b>	<b>2,262,033</b>	<b>1,730,142</b>	<b>1,828,492</b>	<b>2,129,441</b>	<b>2,024,234</b>	<b>2,196,615</b>	<b>2,464,439</b>

<sup>1</sup> 2005 employer contributions include \$300 million pension obligation note

CHANGES IN FIDUCIARY NET POSITION (IN THOUSANDS)  
YEARS ENDED JUNE 30



\* 2005 employer contributions include \$300 million pension obligation note

High yield bonds as represented by the Merrill Lynch High Yield Master Trust II Index benefited from investors searching for yield, gaining 11.8% for the fiscal year.

Among the alternative asset classes, Inflation Linked once again provided the best returns within the portfolio for the second consecutive year. The 22.3% return for the Inflation Linked Asset Class was largely driven by outstanding performance by Master Limited Partnerships (MLPs). HMEPS' MLP investment managers returned 39.4% for the fiscal year vs. 23.1% for the Alerian MLP Index.

Overall, the System's investments returned 16.4%, compared to the actuarially assumed return of 8.5%. Through the efforts of the Board of Trustees, the System's investment portfolio is more broadly diversified than most public pension plans and

benchmark return of 15.6%, but lagged the return of the median fund in the TUCS Master Trusts – Public Universe of 16.8%.

## Funding Status

The HMEPS' funding objective is to establish contributions which, when combined with present assets and future investment returns, will be sufficient to meet the financial obligations to present and future retirees and beneficiaries.

Annual actuarial valuations measure the progress toward these goals, as well as test the adequacy of the contribution rate. The System's actuary assumes that the System's investments will return 8.5 percent over the long-term. The funded ratio, the ratio of the actuarial value of assets (AVA) to the actuarial accrued liability (AAL), is a standard measure of a plan's

funded status. As of July 1, 2013, the System had a funded ratio of 57.7%, which is lower than the 59.1% funded ratio as of July 1, 2012.

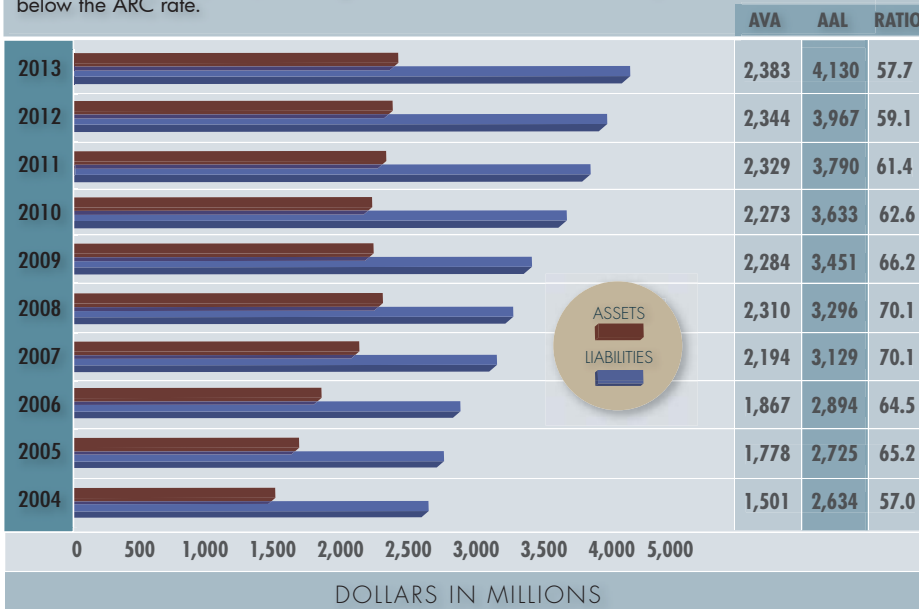
Based on actuarial estimates, the System's projected funded ratio as of July 1, 2013 would be 68.1%, or approximately 16 percentage points higher, if the City had contributed the annual required contribution rate (ARC) in each of the preceding 10 years.

The current Meet and Confer Agreement provides a program for steadily improving the funded status of the System, as future City contributions will increase by at least 2% or \$10 million per year until the actuarially determined contribution rate is met, at which time the actuarially determined contribution rate will be the required rate.

Like most large public pension plans, HMEPS was significantly impacted by the volatility in the investment markets after 2008. While the 2010, 2011 and 2013 returns substantially exceeded the 8.5% assumed rate of return, the 2012 return was significantly less than the assumed rate. In the absence of future investment gains, the contribution rate needed to amortize the unfunded liability will increase over the next few valuation cycles.

## HISTORICAL ACTUARIAL FUNDING RATIO

The funding ratio reflects the System's actuarial value of assets (AVA) relative to its actuarial accrued liability (AAL). This chart indicates a 10-year history of the plan for each year that a valuation was prepared, reflecting the 2008 financial crisis and City's contribution rate below the ARC rate.



exhibits less volatility, particularly during extreme market environments. Over long periods of time (10 years), the System's investment performance ranks in the top 1% in the TUCS Master Trusts – Public peer group. During the 10 year period ending June 30, 2014, the system's annualized return was 9.3%, with the median comparable fund returning 7.3%.

## Fiscal Year 2014 Financial Highlights

For the fiscal year ended June 30, 2014, the System returned 16.4%. This rate of return exceeded the System's policy

# HMEPS HONORS STAFF MEMBER AMY ROWLEY FOR HER 29 YEARS OF SERVICE

Our Congratulations and Thanks to Amy Rowley!

HMEPS wants to congratulate Naomi “Amy” Rowley on her retirement and thank her for her 29 years of distinguished service to the City, the System and the people of Houston.

Rowley officially joined the City of Houston on Sept. 12, 1985 as an accounting clerk, working for David L. Long in capital improvements in the City’s Finance and Administration department. She had worked for Long as a temporary worker for a couple of years before he convinced her to come work for him full-time. It was the start of a long and productive career.

She started working for HMEPS in May 1993, two months before Long was named the System’s first executive director. Rowley became Long’s executive assistant and liaison to the HMEPS Board of Trustees, a role she continued after Long retired and Rhonda Smith took over as Executive Director.

“It truly has been an honor to work here. David Long was the best leader that anyone could have. Rhonda had big shoes to fill, and she and the HMEPS team are doing an outstanding

job,” said Rowley, who also completed her National Society of Pension Professionals Chartered Pension Executive training in August 2009.

Following her retirement, Rowley plans to work on her photography, another job she excelled at while working part-time as photographer for the Mayor’s office and City Council from 1992-2000. In that role, she photographed a number of prominent people, including the Queen of England and Prince Philip. She also plans to spend time with her family, including her husband, Ryan, their five children, 12 grandchildren and three great-grandchildren – plus one more on the way!



Rowley dedicated her career to the public and to the employees who serve them. She has been an integral part of HMEPS, working with commitment and diligence for

the members of the fund.

We thank Rowley for her years of hard work and dedication to the City and HMEPS. She will be greatly missed, and we here at HMEPS wish her the very best in the next phase of her life.



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