

**Firemen's Relief and Retirement Fund**  
**A Fiduciary Fund of the City of McAllen, Texas**

Financial Statements and Required  
Supplementary Information  
And Report of Independent Certified Public Accountants

September 30, 2015

**Firemen’s Relief and Retirement Fund  
of McAllen, Texas  
September 30, 2015**

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# Padgett Stratemann

## Independent Auditor's Report

To the Pension Board of Trustees  
Firemen's Relief and Retirement Fund  
McAllen, Texas

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

We have audited the accompanying financial statements of the Firemen's Relief and Retirement Fund (the "Plan"), a fiduciary fund of the City of McAllen, Texas, as of September 30, 2015 and the related notes to the financial statements, which collectively comprise the Plan's 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.

### ***Auditor's 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 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 Plan'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 Plan'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.

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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 net position of the Plan as of September 30, 2015, and the changes in Plan's net position for the year then ended, in accordance with accounting principles generally accepted in the United States of America.

### ***Emphasis of Matter***

As discussed in Note 1, the financial statements present only the financial position of the Firemen's Relief and Retirement Fund, a fiduciary fund of the City of McAllen, Texas, and are not intended to, and do not, present fairly, the financial position or changes in financial position of the City of McAllen, Texas. They do not purport to, and do not, present the financial position of the City of McAllen, Texas as of September 30, 2015, and the changes in financial 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, Schedule of Changes in Employer Net Pension Liability and Related Ratios – Unaudited, Schedule of Employer Contributions – Unaudited, Schedule of Investment Returns – Unaudited, and Notes to the Required Supplementary Information – Unaudited, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic 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.

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

In accordance with *Government Auditing Standards*, we have also issued our report dated March 2, 2016 on our consideration of the Plan'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 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 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 Plan's internal control over financial reporting and compliance.

Padgett, Stratemann + Co., L.L.P.

San Antonio, Texas

March 2, 2016

## MANAGEMENT’S DISCUSSION AND ANALYSIS

The following is management’s discussion and analysis of the financial performance of the Firemen’s Relief and Retirement Fund the (“Plan”) of McAllen, Texas. It is presented as a narrative overview and analysis for the purpose of assisting the reader with interpreting key elements of the financial statements, notes to the financial statements, and required supplementary information.

### OVERVIEW OF THE FINANCIAL STATEMENTS

Management’s discussion and analysis is intended to serve as an introduction to the Plan basic financial statements, together with the related notes to the financial statements, required supplementary information, and the supporting schedules, all of which are described below:

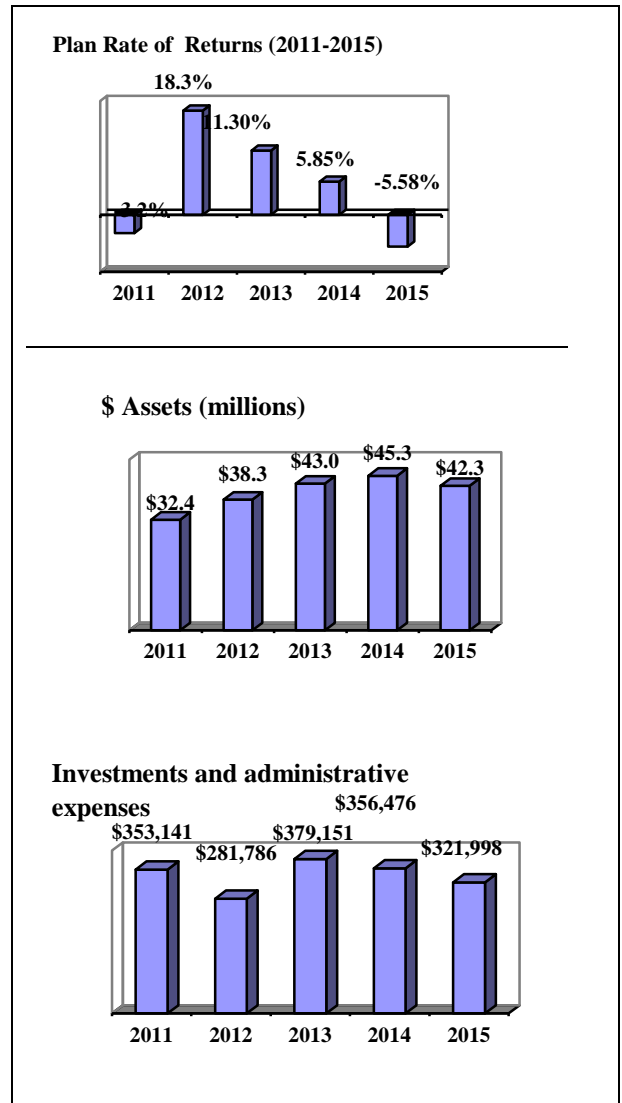
#### Fund Financial Statements:

Statement of Fiduciary Net Position – This statement reports the assets, liabilities, and resultant net position restricted for pension benefits. This statement should be read with the understanding that it discloses the Plan’s financial position on September 30, 2015.

Statement of Changes in Fiduciary Net Position – This statement reports the results of operations during the years, categorically disclosing the additions to and deductions from plan net position. The net increase to plan assets on this statement support the change in net position restricted for pension benefits on the Statement of Fiduciary Net Position.

#### Notes to the Financial Statements:

The financial statement notes provide additional information that is essential to a full understanding of the date provided in the fund financial statements.



Firemen's Relief and Retirement Fund  
of McAllen, Texas  
Management's Discussion and Analysis  
September 30, 2015

**THE PLAN FINANCIAL ANALYSIS**

The plan provides retirement benefits to essentially all eligible firefighter employees. These benefits are funded through member contributions, employer contributions, and earnings on investments. Total net position held in trust for pension benefits at September 30, 2015 amounted to \$42,300,964.

***Additions to Net Position***

Additions to the Plan net position held in trust for pension benefits include contributions from members and employer and net investment income. Member contributions totaled \$1,223,445 and employer contributions amounted to \$1,477,483. The Plan recognized net investment loss of \$2,467,023. This net investment loss was attributable to a combination of the following: a market depreciation of \$6,746,265; interest and dividends of the portfolio in the amount of \$924,652; gain in the disposition of investments during the year amounting to \$3,630,518; and investment management expenses in the amount of \$275,928.

<u>Additions to Net Position</u>	<u>2015</u>	<u>2014</u>
Member contributions	\$ 1,223,445	\$ 1,214,786
Employer contributions	1,477,483	1,435,293
Net investment income(loss)	<u>(2,467,023)</u>	<u>2,525,951</u>
 Total net additions	 <u>\$ 233,905</u>	 <u>\$ 5,176,030</u>

***Deductions From Plan Net Position***

Deductions from the Plan net position held in trust for pension benefits are comprised primarily of retirement benefit payments to the Plan retirees, survivors, and beneficiaries. Administrative expenses and refunds of contributions are also included as deductions. For 2015, benefit payments to retirees, survivors, and beneficiaries amounted to \$2,532,106. The administrative expenses amounted to \$46,070; and refunds to terminated employees—\$52,969 and DROP distribution—\$585,633. This combined amount totaled \$638,602. Additional beneficiaries were added during the year: six firemen and two spouses; however, two retirees died during this time period. The combination of these events will add a net additional cost to the plan of approximately \$255,060.

Firemen's Relief and Retirement Fund  
of McAllen, Texas  
Management's Discussion and Analysis  
September 30, 2015

<u>Deductions From Net Position</u>	<u>2015</u>	<u>2014</u>
Benefit payments	\$ 2,532,106	\$ 2,210,191
Refund to terminated employees	52,969	26,742
Drop payments	585,633	351,653
Administrative expenses	<u>46,070</u>	<u>23,959</u>
Total deductions	<u>\$ 3,216,778</u>	<u>\$ 2,612,545</u>

***Investments***

Upon approval by the board of trustees, several realignments in the portfolio were made without changing the investment strategy. Total investments, exclusive of cash holdings and accrued interest receivable, amounted to \$41,966,478 at September 30, 2015. The estimated rate of return of the Plan was approximately -5.58% for the current year. For the year, the fund did not meet its actuarial rate of return of 7.5 percent. The Plan's board of trustees and its consultant remain confident in the long-term potential of the portfolio to deliver upon the desired results of performance in excess of the actuarial requirement with appropriate levels of risk. The approach has served the Plan well historically and the Plan sees no reason to believe it is not attainable going forward.

The following table represents the fair value of investments of the Plan:

Investments at Fair Value

	<u>2015</u>	<u>2014</u>
Fixed income	\$ 8,531,353	\$ 11,105,348
Domestic and international equities	25,035,975	26,473,203
Alternative investments	<u>8,399,150</u>	<u>6,814,878</u>
Total assets	<u>\$ 41,966,478</u>	<u>\$ 44,393,429</u>

**REQUESTS FOR INFORMATION**

This Annual Financial Report is designed to provide a general overview of the Firemen's Relief and Retirement Fund of McAllen, Texas finances for interested parties. Questions concerning any of the information provided herein, or requests for additional financial information, should be addressed to Firemen's Relief and Retirement Fund of McAllen, Texas, P.O. Box 220, McAllen, Texas 78505-0220.



## Financial Statements

**Firemen's Relief and Retirement Fund  
of McAllen, Texas**

Statement of Fiduciary Net Position

September 30, 2015

**Assets**

Cash and cash equivalents	\$ 321,048
Accrued interest receivable	13,438
Investments at fair value:	
Fixed income	8,531,353
Domestic and international equities	25,035,975
Alternative investments	<u>8,399,150</u>
Total assets	<u>42,300,964</u>

**Liabilities**

Accounts payable	<u>-</u>
Total liabilities	<u>-</u>
<b>Net position restricted for pension</b>	<u><u>\$ 42,300,964</u></u>

*The accompanying notes are an integral part of these statements.*

**Firemen's Relief and Retirement Fund  
of McAllen, Texas**

Statement of Changes in Fiduciary Net Position

Year Ended September 30, 2015

**Additions**

Contributions:

Members	\$ 1,223,445
Employer	1,477,483

Total contributions	2,700,928
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Investment income:

Net depreciation in fair value of investments	(6,746,265)
Gain on sale of investments	3,630,518
Interest and dividends	924,652

Less investment expense	(2,191,095) 275,928
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Net investment loss	(2,467,023)
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Total additions	233,905
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**Deductions**

Benefits paid directly to participants or beneficiaries	2,532,106
Refunds to terminated employees	52,969
DROP payments	585,633
Administrative expenses	46,070

Total deductions	3,216,778
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Net decrease in net position	(2,982,873)
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**Net position restricted for pension**

Beginning of year	45,283,837
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End of year	\$ 42,300,964
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*The accompanying notes are an integral part of these statements.*

# Firemen’s Relief and Retirement Fund of McAllen, Texas

## Notes to Financial Statements

September 30, 2015

### 1. Plan Description

The provisions of Firemen’s Relief and Retirement Fund of McAllen, Texas (the “Plan”) are authorized by the Texas Local Fire Fighters’ Retirement Act (“TLFFRA”). The following brief description of the Plan is provided for general information purposes only. The Plan agreement should be referred to for more complete information. The Plan has an actuarial valuation performed biennially in accordance with Governmental Accounting Standards Board (“GASB”) Statement No. 67, *Financial Reporting for Pension Plans— an amendment of GASB Statement No. 25*. The most recent actuarial valuation was performed as of September 30, 2014.

#### *Reporting Entity*

The plan is sponsored by the City of McAllen, Texas (the “City”). The Plan does not purport and does not present the financial position or changes in financial position of the City as of any time or for any period. The Plan meets the criteria of a “fiduciary fund” of the City as established by GASB, and certain information regarding the Plan is included in the City’s financial statements.

#### *Plan Membership*

The Pension Board of Trustees is the administrator of the Plan, which consists of current and former fire fighters of the City, as well as certain beneficiaries of current and former fire fighters. The City is the only contributing employer. The fire fighters covered by the Plan also contribute to the Plan. The types of employees covered, as well as Plan membership data, are as follows:

Number of participants:		
Actives members		161
Retirees and beneficiaries entitled to benefits		95
Retirees and beneficiaries entitled to, but not yet receiving benefits		<u>7</u>
		<u>263</u>

# Firemen's Relief and Retirement Fund of McAllen, Texas

## Notes to Financial Statements

September 30, 2015

### 1. Plan Description (continued)

#### *Plan Benefits*

##### *Service Retirement Benefits*

A member is eligible for service retirement upon completion of 20 years of service and attainment of age 50. A member who retires under the service retirement provisions of the fund will receive a monthly benefit equal to the sum of (a), (b), and (c) where: (a) equal to 2.9 percent of the member's highest 60-month average salary for each of the member's years of service up to and including the 20th year of service and (b) equals the greater of 2.9 percent of the member's highest 60-month average salary, or \$58.00 per month for each of the member's 21<sup>st</sup> and 22<sup>nd</sup> years of service, and (c) equals \$58.00 per month for each year of service in excess of 22 years.

##### *Disability Benefits*

An active member who becomes disabled as defined in the plan will receive a monthly disability benefit. Separate disability benefits are provided for duty-related and off-duty disabilities. Disability benefits are payable in the same joint-and-survivor form as service retirement benefits. However, disability benefits stop if the member recovers to the point that he no longer meets the definition of disability under the fund. If the total monthly amount a disabled member receives from (a) the fund, (b) workers compensation, and (c) the City of McAllen, exceeds the member's monthly rate of pay as of his date of disability, the amount payable from the fund will be reduced so that the member's benefit from all three sources, combined, does not exceed such rate of pay.

##### *Death Benefits*

Duty-related death benefits, payable to a member's spouse for as long as they are living, equal the sum of (a) 38.67% of the member's highest 60-month average salary, (b) plus two-thirds of any additional service benefit earned by the member as of the date of their death. The death benefit is payable for life, but it ceases upon remarriage. Effective January 1, 2006 the widowed spouse of a member who completed 10 or more years of service prior to their death will have the death benefit payments terminated in the event of remarriage. In addition to the above spousal death benefit, each unmarried child of the member will receive a monthly benefit of 7.73 percent of the fire fighter's highest 60-month average salary. Orphan benefits continue until the child reaches age 18. However, benefits will continue until age 22 for a child who is a full-time student. If the member's spouse dies or remarries, or if the member has no spouse on the date of their death, each eligible orphan will receive a monthly benefit of 15.47 percent of the member's highest 60-month average salary. Orphan benefits are continued for life to disabled children. The total of all benefits paid as a result of the death of an active fund member may not exceed the disability or retirement benefits such member had earned as

**Firemen's Relief and Retirement Fund  
of McAllen, Texas**

Notes to Financial Statements

September 30, 2015

**1. Plan Description (continued)**

*Death Benefits (continued)*

of the date of their death. The total of all benefits paid as a result of the death of a retired member may not exceed the retirement benefit the member was receiving as of the date of their death. Benefits are reduced pro rata, if necessary, in order to satisfy these limitations.

*Termination Benefits*

Members who terminate employment with less than 10 years of service will be entitled to the return of the excess of their contributions to the fund over the amount of any benefits they have received from the Plan. Such refunds will not include any interest on the members' contributions. If members terminate on or after the date they have completed 10 years of service but prior to the date they complete 20 years of service, they will be entitled to receive a monthly benefit, starting on the date they would have both completed 20 years of service and attained age 50, had they remained in the service of the fire department. The amount the members will receive will equal the monthly service retirement benefit they had accumulated on the date they separated from service with the fire department, multiplied by the vested percentage of the members.

*The Deferred Retirement Option Plan (DROP)*

A member is eligible to receive their benefits under the plan's DROP provision after they have both completed 20 years of service and attained age 53. The election to participate in the DROP may be made at the time the member elects to retire. The monthly retirement income payable to a member who retires under the DROP will equal their service retirement benefits under the plan based on highest 60-month average salary and years of service as of the member's DROP Eligibility Date. The member's benefit will be calculated, however using the benefit formula in effect on the member's actual date of retirement. A members DROP Eligibility Date is the later of (a) the date the member meets the eligibility requirements for the DROP or (b) the date which is two years prior to the member's actual retirement date: Upon retirement, the member will receive—in addition to their monthly retirement benefit—a single payment equal to the sum of: (a.) the total of the monthly retirement benefits the member would have received between his DROP Eligibility Date and the time they retired under the plan, and (b.) the amount of monthly contributions that the member has made to the fund between their DROP Eligibility Date and the time they retired under the plan.

# **Firemen's Relief and Retirement Fund of McAllen, Texas**

## **Notes to Financial Statements**

September 30, 2015

### **2. Summary of Significant Accounting Policies and Plan Asset Matters**

#### ***Organization***

The Plan was created pursuant to the TLFFRA. The Plan provides pension, disability, death, and severance benefits to employees of the City's fire department and former volunteer firemen eligible to receive benefits pursuant to a single-employer defined benefit pension plan.

#### ***Basis of Accounting***

The financial statements are prepared in conformity with accounting principles generally accepted in the United States of America for local governmental units as prescribed by the GASB. The financial statements are prepared using the accrual basis of accounting. Employee and employer contributions are recognized as revenues in the period in which employee services are performed. Benefits and refunds are recognized when due and payable in accordance with the terms of the Plan.

#### ***Cash Equivalents***

For purposes of the statement of fiduciary net position, short-term, highly liquid investments are considered cash equivalents.

#### ***Valuation of Plan Investments***

The Plan's investments are stated at fair value and, accordingly, unrealized appreciation and depreciation are reported in the statement of changes in fiduciary net position. The fair value of money market funds is considered to be the same as the cost of these investments due to their nature. The fair value of common stocks and foreign equities are based on quoted market prices. The fair value of United States Government securities and corporate and foreign bonds are based on quotes from broker dealers. The Plan values investments in alternative funds based on its percentage investment in each such fund. The estimated fair value of each fund is based on market conditions and information reported by the fund manager, and is generally based on the estimated fair value of each funds' underlying investments at the end of the reporting period.

Purchases and sales of investments are recorded on a trade-date basis and, accordingly, the related receivables and payables for any unsettled trades are recorded. Interest income and dividends are recorded on the accrual basis.

#### ***Federal Income Tax***

The Plan is exempt from federal income tax pursuant to applicable regulations.

**Firemen’s Relief and Retirement Fund  
of McAllen, Texas**

Notes to Financial Statements

September 30, 2015

**2. Summary of Significant Accounting Policies and Plan Asset Matters (continued)**

*Estimates*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the Plan administrator to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results may differ from those estimates.

**3. Fiduciary Fund of the City of McAllen, Texas**

Due to the level of oversight responsibility exercised, the Plan is included in the City’s basic financial statements in the fiduciary fund section. Certain administrative functions are performed for the Plan by the City at no cost. The City is under no legal obligation to fund any pension obligation.

**4. Net Pension Liability of the City**

Total pension liability is developed by subtracting the present value of future service costs from the present value of future benefits. The net pension liability is calculated by subtracting the plan fiduciary net position from the total pension liability. The components of the net pension liability of the City at September 30, 2015 were as follows:

Total pension liability	\$ 68,453,587
Plan fiduciary net pension	<u>42,300,964</u>
City's net pension liability	<u><u>\$ 26,152,623</u></u>



# Firemen's Relief and Retirement Fund of McAllen, Texas

## Notes to Financial Statements

September 30, 2015

### 4. Net Pension Liability of the City (Continued)

#### Actuarial Assumptions

The total pension liability was determined by an actuarial valuation as of October 1, 2014 and rolled forward to the measurement date of September 30, 2015, the Plan's fiscal year end.

Valuation date	October 1, 2014
Measurement date	September 30, 2015
Actuarial cost method	Entry age
Amortization method	Level percentage of payroll, open
Equivalent single amortization period of the unfunded liabilities	29.0 years
Asset valuation method	Five-year smoothed value with a 20% of market value corridor
Actuarial assumptions:	
Investment rate of return	7.50% per annum, compounded annually
Projected salary increases	4.00% to 8.60%, including inflation based on service at attained age (fund specific)
Inflation	3.00% per year
Cost-of-living adjustment	None
Mortality	Employee and health annuitant combined rates from the RP-2000 Mortality Table, projected to 2015 using Scale AA, with separate rates for males and females
Other information	There have been no benefit changes since the October 1, 2014 valuation date

**Firemen’s Relief and Retirement Fund  
of McAllen, Texas**

Notes to Financial Statements

September 30, 2015

**4. Net Pension Liability of the City (Continued)**

The investment rate of return and the projected salary increases both used the same assumptions with regard to inflation. Best estimates of long-term real rates of return for each major asset class included in the pension plan’s target asset allocation as of September 30, 2014 are summaries in the table below:

<u>Asset class:</u>	<u>Target allocation</u>	<u>Long-term expected real rate of return</u>
Cash	0.00%	0.68%
Fixed income	29.00%	3.00%
Equities		
(a) Domestic	39.00%	7.36%
(b) International	16.00%	5.25%
Alternative investments	16.00%	3.00%

**Discount Rate**

The discount rate used to measure the total pension liability was 7.50%. The projection of cash flows used to determine the discount rate assumed that contributions from plan members will be made at the current contribution rate and that contributions from the City will be made at contractually required rates. Based on this assumptions, the pension plan’s fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return for the pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

**Sensitivity of the Net Pension Liability to Changes in the Discount Rate**

The table in the following page presents the net pension liability of the City calculated using the discount rate of 7.50%, as well as what the net pension liability would be if it were calculated using a discount rate that is one percentage point lower (6.50%) or one percentage point higher (8.50%).

**Firemen’s Relief and Retirement Fund  
of McAllen, Texas**

Notes to Financial Statements

September 30, 2015

**4. Net Pension Liability of the City (Continued)**

	One Percent Decrease (6.50 Percent)	Current Discount Rate (7.50 Percent)	One Percent Increase (8.50 Percent)
Net pension liability	<u>\$ 34,548,819</u>	<u>\$ 26,152,623</u>	<u>\$ 19,127,012</u>

**Money-weighted rate of return**

For the year ended September 30, 2015, the money weighted rate of return was calculated at negative 5.44%. The calculation was determined based on rate of return on pension plan investments, net of pension plan investment expense. Inputs to the money-weighted internal rate of return calculation were determined at least monthly.

**5. Benefits**

Benefit provisions are established under authority of the TLFFRA. Specific plan provisions are governed by a Plan document and a trust agreement executed by the Board of Trustees. The Plan document may be amended as provided in Section 7 of the Texas Fire Fighters’ Retirement Act (Article 6243e. V.T.C.S.). Amending the Plan requires approval of any proposed change by an eligible actuary and a majority of the participating members of the Plan. Both the City and the members of the Plan have specific authority to appoint members of the Board of Trustees under the TLFFRA.

**6. Contributions**

The Plan’s minimum required contribution provisions are established under Title 8, Subtitle A, Chapter 802, Subchapter B, Section 802.101 of the Texas Government Code and under Texas Pension Review Board Guidelines for Actuarial Soundness. Specific Plan contribution rates are governed by the Plan document. Changes in the members’ or the City’s contribution rate requires a plan amendment.

The contribution rates of the Plan members and the City are established under the terms of the Plan. An actuarial valuation is performed biennially to verify that Plan benefits and Plan contributions are in balance. Costs of administering the fund are paid from Plan assets.

# **Firemen's Relief and Retirement Fund of McAllen, Texas**

## **Notes to Financial Statements**

September 30, 2015

Pursuant to the Plan document, a legal instrument binding both the City and its firefighters, the City of McAllen is required to match members' contributions. Benefits paid to former volunteer firefighters are funded by the City when paid to the former volunteer firefighters or beneficiaries. The City's contribution rate for the fiscal year ended September 30, 2015 was 13.25% of annual compensation. Contributions required and paid into the fund as of September 30, 2015 were \$1,223,455 (members) and \$1,477,483 (employer).

### **7. Deposits With Financial Institutions and Investments**

The deposits and investments of the Plan are held separately from those of the City. The TLFFRA authorizes the Plan to invest in:

- Obligations and securities of the United States, the state of Texas, or any county, city, or other political subdivision of the state of Texas;
- Savings and loan association accounts insured by the Federal Deposit Insurance Corporation;
- First lien real estate mortgage securities insured by the Federal Housing Administration;
- Corporate bonds and stocks;
- Guaranteed investment contracts offered by insurance companies;
- Money market funds;
- Mutual funds and other pooled funds; and
- International stocks traded as American Depository Receipts;
- Derivatives; and
- Alternative investments.

**Firemen’s Relief and Retirement Fund  
of McAllen, Texas**

Notes to Financial Statements

September 30, 2015

**7. Deposits With Financial Institutions and Investments (Continued)**

***Investments***

Investments at fair value as of September 30, 2015 are as follows:

	<u>Fair Value</u>	<u>% of Portfolio</u>	<u>Investment Policy of Asset Allocation</u>
Equities:			
Domestic	\$ 18,434,763	44%	30-60%
International	<u>6,601,212</u>	16%	10-30%
Total equities	<u>25,035,975</u>		
Fixed income:			
Treasury and agency securities and corporate bonds	<u>8,531,353</u>		
Total fixed income	<u>8,531,353</u>	20%	20-50%
Alternative funds	<u>8,399,150</u>	20%	0-20%
Total investment portfolio	<u>\$ 41,966,478</u>	100.00%	

Because of the complexity of the portfolio, the Board of Trustees uses a consultant to provide the guidance to accomplish the Plan’s objectives. The Board also understands that return objectives can be achieved while assuming “market” volatility. The Board is willing to forgo potential return in strong markets in return for protection against a severe decline during weak periods.

*Concentration of credit risk.* As noted in the above schedule, none of the sectors exceed their percentage of asset allocation. The Plan is diversified; with no one issue exceeding 5%. Under normal market conditions, the portfolio can be liquidated within one to two days if so desired. Alternative funds can only be liquidated quarterly.

*Interest rate risk.* Only the fixed income securities of the Plan are subject to interest rate risk due to the possibility that prevailing interest rates could change before the securities reach maturity. Securities that are subject to interest rate risk as of September 30, 2015 amount to \$7,191,517 and have weighted-average duration of 3.78 years. Duration is defined as the change in the value of a fixed income security that will result from a 1% change in interest rates. Duration is stated in years. For example, five year duration means the bond will decrease in value by 5% if interest rates rise 1% and increase in

**Firemen's Relief and Retirement Fund  
of McAllen, Texas**

Notes to Financial Statements

September 30, 2015

**7. Deposits With Financial Institutions and Investments (Continued)**

value by 5% if interest rates fall 1%. The investment policy is silent on the subject of interest risk. Securities that are subject to interest rate risk are shown in the following table.

Investment Type	Fair Value	Percentage of Total	Weighted-Average Duration (Years)
Corporate bonds	\$ 788,196	10.96%	5.56
Government agencies	1,351,536	18.79%	0.51
Government bonds	4,669,346	64.93%	5.82
Government Mortgage Back Securities	382,078	5.31%	5.06
Supranationals	5,567	0.08%	-0.10
Municipals & Derivatives	(5,206)	-0.07%	-0.10
Total fixed income investments	<u>\$ 7,191,517</u>	100.00%	<u>3.78</u>

*Credit risk.* Using Standard and Poor's rating system for fixed income securities as of September 30, 2015 the Plan's fixed income investments were rated as noted below. The investment policy is silent on the subject of credit risk.

S&P Rating	Fair Value	Percentage of Total
AAA	\$ 1,918,372	26.68%
AA	390,106	5.42%
A	1,033,831	14.38%
BBB	1,727,439	24.02%
BB	1,081,299	15.04%
B	728,357	10.13%
CC	10,139	0.14%
C	6,759	0.09%
CCC	230,125	3.20%
Not rated	<u>65,090</u>	<u>0.91%</u>
Total fixed income investments	<u>\$ 7,191,517</u>	100.00%

*Foreign currency risk.* The Plan has three equity investment managers that have direct foreign currency exposure, which amounted to \$6,601,221 at the end of September 30, 2015. The investment policy is silent on the subject of foreign currency risk.

# **Firemen's Relief and Retirement Fund of McAllen, Texas**

## **Notes to Financial Statements**

September 30, 2015

### **8. Risks and Uncertainties**

The Plan invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market rate, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the value of investment securities will occur in the near term and those changes could materially affect the amounts reported in the statement of fiduciary net position.

Plan contributions are made and the actuarial present value of accumulated plan benefits are reported based on certain assumptions pertaining to interest rates, inflation rates, and employee demographics, all of which are subject to change. Due to uncertainties inherent in the estimations and assumptions process, it is at least reasonably possible that changes in these estimates and assumptions in the near term would be material to the financial statements.

### **9. Change in State Oversight Agency**

An agency from the State of Texas conducted a sunset review of the Texas Local Fire Fighters' Retirement agency. After the review, it was decided that this agency should be abolished and its duties were transferred to the Pension Review Board, another state agency. The Pension Review Board agency is currently assessing its additional responsibilities towards the local pension plans, which will now fall under its jurisdiction.

### **10. Funding Responsibility**

In September 2003, Texas voters approved an amendment to the Texas Constitution, which provided that once certain benefits are granted to retirees, those benefits may not be subsequently reduced. It was codified as Article XVI, Section 66, of the Texas Constitution. The amendment applies only to the City of McAllen Firefighters' Relief and Retirement Plan. It further provided that the City and the retirement system that finance benefits under the retirement system are jointly responsible for ensuring that benefits are not reduced or otherwise impaired, which could potentially require the City to involuntarily increase its funding due to under-performing investments, plan improvements as well as other factors outside the control of the City. The amendment also permitted the City to be exempt from its requirements upon holding an election in which the majority of the votes favored the exemption. On May 15, 2004, a special City election was held, in which the majority of the voters voted in favor of exempting the City of McAllen and the McAllen Firefighters' Relief and Retirement Plan from the application of this amendment, Article XVI, Section 66 of the Texas Constitution.

Required Supplementary Information



## Firemen's Relief and Retirement Fund of McAllen, Texas

### Schedule of: Investments and the Long-term Expected Rate of Return On Pension Plan Assets; Employer Contributions; and Changes in Net Pension Liability and Related Ratios (Unaudited)

Discount Rate	7.50%	7.50%
Annual Increase in Payroll	4.25%	4.00%
Measurement Date	<u>9/30/2014</u>	<u>9/30/2015</u>
<b>Total Pension Liability</b>		
1. a. Service Cost (Pension benefits)	\$ 1,549,238	\$ 1,778,456
b. Service Cost (Administrative expenses)	23,959	46,070
2. Interest	4,841,219	4,884,830
3. Changes in Benefit Terms	-	-
4. Difference Between Expected and Actual Experience	-	221,439
5. Changes in Assumptions	-	(3,414,995)
6. Benefit Payments (including refunds of member contributions)	(2,588,586)	(3,170,707)
7. Net Change In Total Pension Liability	3,825,830	345,093
8. Total Pension Liability-Beginning of the Year	64,282,664	68,108,494
9. Total Pension Liability-End of the Year	68,108,494	68,453,587
<b>Plan Fiduciary Net Position</b>		
10. Contributions - employer	1,435,293	1,477,483
11. Contributions - members	1,214,786	1,223,445
12. Expected Net Investment Income	2,525,951	3,376,943
13. Gain or (Loss) Due to Difference in Projected vs Actual Earnings	-	(5,843,966)
14. Benefit Payments (including refunds of member contributions)	(2,588,586)	(3,170,707)
15. Expected Administrative Expenses	(23,959)	(46,070)
16. Other	(1)	-
17. Net Changes in Plan Fiduciary Net Position	2,563,484	(2,982,873)
18. Plan Fiduciary Net Position-Beginning of the Year	42,720,353	45,283,837
Plan Fiduciary Net Position-End of the Year	45,283,837	42,300,964
19. Net Position Liability-End of the Year (line 9 minus line 18)	22,824,657	26,152,623
20. Plan Fiduciary Net Position as a Percentage of the Total Pension Liability-End of the Year	66.49%	61.80%
21. Covered Employee Payroll	11,043,509	11,365,262
22. Net Pension Liability-End of the Year as a Percentage of Covered Employee Payroll	206.68%	230.11%
23. Annual Money-weighted Rate of Return Net of Pension Plan Investment Expense With Inputs Determined At Least Monthly	5.90%	-5.44%
24. Actuarially Determined Contribution	1,435,293	1,477,483
25. Contributions in Relation to the Actuarially Determined Contribution	1,435,293	1,477,483
26. Contribution Deficiency (Excess)	-	-
27. Contribution as a Percentage of Covered-employee Payroll	13.00%	13.00%

**Note: In accordance with Paragraph 50 GASB Statement No. 67, this schedule only includes information which has been measured in conformity with Statement No. 67. Disclosures for years in which information was not developed in accordance with GASB 67 Statement have not been included.**

**Firemen’s Relief and Retirement Fund  
of McAllen, Texas**

Schedule of: Investments and the Long-term Expected Rate of Return On Pension Plan  
Assets; Employer Contributions; and Changes in Net Pension Liability and Related Ratios  
(Unaudited)

**Actuarial Assumptions**

The total pension liability was determined by an actuarial valuation as of October 1, 2014 and rolled forward to the measurement date of September 30, 2015, the Plan’s fiscal year end.

Valuation date	October 1, 2014
Measurement date	September 30, 2015
Actuarial cost method	Entry age
Amortization method	Level percentage of payroll, open
Equivalent single amortization period of the unfunded liabilities	29.0 years
Asset valuation method	Five-year smoothed value with a 20% of market value corridor
Actuarial assumptions:	
Investment rate of return	7.50% per annum, compounded annua
Projected salary increases	4.00% to 8.60%, including inflation based on service at attained age (fund specific)
Inflation	3.00% per year
Cost-of-living adjustment	None
Mortality	Employee and health annuitant combined rates from the RP-2000 Mortality Table, projected to 2015 using Scale AA, with separate rates for males and females

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## Padgett Stratemann

### 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*

To the Pension Board of Trustees  
Firemen's Relief and Retirement Fund  
McAllen, Texas

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 Firemen's Relief and Retirement Fund (the "Plan"), a fiduciary fund of the City of McAllen, Texas, as of September 30, 2015 and the related notes to the financial statements, which collectively comprise the Plan's financial statements, and have issued our report thereon dated March 2, 2016.

#### ***Internal Control Over Financial Reporting***

In planning and performing our audit of the financial statements, we considered the Plan'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 opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Plan's internal control. Accordingly, we do not express an opinion on the effectiveness of the Plan'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 Plan'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.

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### ***Compliance and Other Matters***

As part of obtaining reasonable assurance about whether the Plan'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 results of that testing, and not to provide an opinion on the effectiveness of the Plan'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 Plan's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Padgett, Stratemann + Co., L.L.P.*

San Antonio, Texas

March 2, 2016