

**THE CITY OF BIRMINGHAM  
FIREMEN'S AND POLICEMEN'S  
SUPPLEMENTAL PENSION SYSTEM  
AUDITED FINANCIAL STATEMENTS  
FOR THE YEAR ENDED JUNE 30, 2016**

**THE CITY OF BIRMINGHAM  
FIREMEN’S AND POLICEMEN’S  
SUPPLEMENTAL PENSION SYSTEM**

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## INDEPENDENT AUDITOR'S REPORT

To the Pension Board of the  
City of Birmingham Firemen's and Policemen's  
Supplemental Pension System  
Birmingham, Alabama

We have audited the accompanying financial statements of the City of Birmingham Firemen's and Policemen's Supplemental Pension System (the Plan), which comprise the statement of fiduciary net position as of June 30, 2016, and the related statement of changes in fiduciary net position for the year then ended, 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 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. 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.

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 financial status of the City of Birmingham Firemen's and Policemen's Supplemental Pension System as of June 30, 2016, and the changes in its financial status for the year then ended in accordance with accounting principles generally accepted in the United States of America.

December 8, 2016



**THE CITY OF BIRMINGHAM  
FIREMEN'S AND POLICEMEN'S  
SUPPLEMENTAL PENSION SYSTEM  
STATEMENT OF PENSION NET POSITION  
JUNE 30, 2016**

	<b>2016</b>
<b><u>ASSETS:</u></b>	
Cash and Cash Equivalents	\$ 1,833,348
<b>Total Cash and Cash Equivalents</b>	<b>1,833,348</b>
Receivables	
Interest and dividends	100,296
<b>Total Receivables</b>	<b>100,296</b>
Investments, at Market Value:	
U.S. Government Obligations	2,339,120
Domestic Corporate Bonds & Notes	7,430,145
Domestic Stocks	27,030,937
Alternative Investments	5,597,849
<b>Total Investments</b>	<b>42,398,051</b>
<b>Total Assets</b>	<b>\$ 44,331,695</b>
 <b><u>LIABILITIES</u></b>	
Accounts Payable	\$ 43,171
<b>Total Liabilities</b>	<b>43,171</b>
<b>Net Position Restricted for Pension Benefits</b>	<b>\$ 44,288,524</b>

The notes are an integral part of the financial statements.

**THE CITY OF BIRMINGHAM  
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SUPPLEMENTAL PENSION SYSTEM  
STATEMENT OF CHANGES IN PENSION NET POSITION  
FOR THE YEAR ENDED JUNE 30, 2016**

	<b>2016</b>
<b><u>Additions:</u></b>	
Employer Contributions	4,364,213
Contributions from Plan members	4,348,710
Premium Tax -Fire Insurance	404,462
Total contributions	9,117,385
Investment Income:	
Interest	1,003,072
Investment Income	1,732
Net decrease in fair value of investments	(1,246,550)
Miscellaneous	121
<b>Total Additions</b>	<b>\$ 8,875,760</b>
<b><u>Deductions:</u></b>	
Benefit payments to plan members:	
Regular Service	8,760,617
Survivors	952,473
Drops	3,014,048
Refunds of contributions	1,220,981
R & R supplemental contributions	1,266,519
Administrative Expenses:	
Professional fees	283,661
Salaries and benefits	32,800
Other Administrative Expenses	17,892
<b>Total Deductions</b>	<b>15,548,991</b>
<b>Net Increase in Net Position</b>	<b>(6,673,231)</b>
Net Position Restricted For Pension Benefits, beginning of year (excluding accrued income) at market value	<b>\$ 50,961,755</b>
<b>Net Position Restricted for Pension Benefits End of the Year at Market Value</b>	<b>\$ 44,288,524</b>

The notes are an integral part of the financial statements.

**THE CITY OF BIRMINGHAM  
FIREMEN'S AND POLICEMEN'S  
SUPPLEMENTAL PENSION SYSTEM  
NOTES TO FINANCIAL STATEMENTS**

**1. PLAN DESCRIPTION**

*City of Birmingham Firemen's and Policemen's Supplemental Pension System*- This system covers sworn firemen and policemen and provides retirement benefits for twenty or twenty-five years of service. Membership is mandatory for such personnel and is effective upon employment. Employees hired prior to May 2, 1978, contribute 3.3% of payroll, exclusive of overtime; those hired on or subsequent to May 2, 1978, contribute 5.22% and the City matches these amounts. The plan is funded by contributions from employees, the City, and income from the investment of accumulated funds. The plan was established by state law and is administered by a board of managers.

**2. SIGNIFICANT ACCOUNTING POLICIES**

**Basis of Accounting** - The Plan implemented GASB 67 "Financial Reporting for Pension Plans" ("GASB 67") in 2014. GASB 67 replaces the requirements of GASB Statements No. 25 and No. 50 as they related to pension plans that are administered through trusts or equivalent arrangements. GASB #67 establishes standards of financial reporting for plans that issue separate financial reports and also those plans whose financial information is included solely in the financial report of another government as a pension trust fund. GASB 67 specifies the required approach for measuring the pension liability of employers and non-employer contributing entities for benefits provided through pension plans.

The Plan's financial statements are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions to each plan are recognized when due. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

**Estimates** – The preparation of financial statements prepared in conformity with generally accepted accounting principles requires the plan administrator to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results may differ from those estimates.

**Deposits & Investments** – Cash and cash equivalents include cash on hand, demand deposits, savings accounts, and short-term investments with maturities of three months or less at the time of purchase.

The Plan's investments are stated at fair value. Quoted market prices are used to value investments. Investment transactions are recorded on the trade date. Realized gains and losses from sales of securities are determined using the average cost basis. In accordance with the provisions of the Plan in order to state investments at market value, net unrealized appreciation or depreciation for the year is reflected in the statement of changes in pension net position.

**Actuarial Present Value of Accumulated Plan Benefits** – Accumulated plan benefits are those future periodic payments, including lump-sum distributions that are attributable under the Plan's provisions to the service employees have rendered. Accumulated plan benefits include benefits expected to be paid to (a) retired or terminated employees or their beneficiaries, (b) beneficiaries of employees who have died, and (c) present employees or their beneficiaries. Benefits under the Plan are based on employees' compensation during their last ten years of credited service. The accumulated plan benefits for active employees are based on their average compensation during the five years ending on the date as of which the benefit information is presented (the valuation date). Benefits payable under all circumstances – retirement, death, disability, and termination of employment – are included, to the extent they are deemed attributable to employee service rendered to the valuation date. Benefits to be provided via annuity contracts excluded from Plan assets are excluded from accumulated plan benefits.

The actuarial present value of accumulated plan benefits is determined by an actuary from The Segal Group, Inc. and it is that amount that results from applying actuarial assumptions to adjust the accumulated plan benefits to reflect the time value of money (through discounts for interest) and the probability of payment (by means of decrements such as for death, disability, withdrawal, or retirement) between the

**THE CITY OF BIRMINGHAM  
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NOTES TO FINANCIAL STATEMENTS**

**2. SIGNIFICANT ACCOUNTING POLICIES**

valuation date and the expected date of payment. The significant actuarial assumptions used in the valuations as of June 30, 2016 were (a) life expectancy of participants (using the RP-2014 Blue Collar Employee Mortality Table), (b) retirement age assumptions, and (c) investment return. The assumed average rate of return for the 2016 valuation was 7.50%. The actual rate of return, which excluded the employer contributions and benefit payments, was 7.48%. The foregoing actuarial assumptions are based on the presumption that the Plan will continue. Were the Plan to terminate, different actuarial assumptions and other factors might be applicable in determining the actuarial present value of accumulated plan benefits.

**3. FUNDING POLICY**

The contribution requirements of the plan members are established and may be amended by the State Legislature. Plan members were required to contribute 5.22% of their annual covered salary in 2016. The City was required to contribute at a rate of 5.22% of the employees annual covered salary for 2016. All contributions made during 2016 were cash contributions. Administrative costs of the Plan are financed through investment earnings.

**4. BENEFITS**

A participant retiring after 20 years of credited service is entitled to a benefit which is calculated as 50% of final average salary.

The Plan also provides adjusted benefits, in the case of early retirement and death or disability of a participant. Benefit provisions are established and may be amended by the City.

**5. VESTING**

Participants are at all times fully vested in their individual contributions to the Plan. Participants become fully vested in the retirement benefits attributable to them under the Plan, upon the completion of twenty years of continuous service with the City as a Public Safety employee.

**6. INVESTMENTS**

The Plan categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The Plan has the following recurring fair value measurements as of June 30, 2016:

Investment type	Fair Value	Fair Value Measure Using		
		Quoted prices in active markets for identical assets (Level I)	Significant other observable inputs (Level II)	Significant unobservable inputs (Level III)
U.S. Treasury Bonds & Notes	563,387	563,387	-	-
U.S. Government Agency Obligations	1,775,733	-	1,775,733	-
U.S. Corporate Debt Alternatives	7,430,145	-	7,430,145	-
U.S. Corporate Stock	5,597,849	-	-	5,597,849
	27,030,937	27,030,937	-	-
	<u>\$ 42,398,051</u>	<u>\$ 27,594,324</u>	<u>\$ 9,205,878</u>	<u>\$ 5,597,849</u>

**6. INVESTMENTS (Continued)**

**THE CITY OF BIRMINGHAM  
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Debt and equity securities classified in Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities. Debt securities classified in Level 2 of the fair value hierarchy are valued using a matrix pricing technique. Matrix pricing is used to value securities based on the securities' relationship to benchmark quoted prices. Commercial and residential mortgage-backed securities classified in Level 3 are valued using discounted cash flow techniques. Collateralized debt obligations classified in Level 3 are valued using consensus pricing.

The valuation method for investments measured at the net asset value (NAV) per share (or its equivalent) is presented on the following table.

Investments Measured at the NAV

	Fair Value	Redemption Frequency (if Currently Eligible)	Redemption Notice Period
Mesirow Financial -Multi- manager/Multi-strategy Fund of hedge funds	\$ 5,597,849	Quarterly	95 days



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**6. INVESTMENTS (Continued)**

Mesirow Financial Multi-manager/Multi-strategy Fund of hedge funds. This type includes investment in 53 managed hedge funds that pursue multiple strategies to diversify risks and reduce volatility. The fund's strategy allocation is shown in the chart below:

STRATEGY ALLOCATION <sup>6</sup> AS OF 8/1/2016	
Mesirow Institutional Multi-Strategy Fund, L.P. – A	
STRATEGY	%
<b>Credit</b>	19.42
Long / Short Credit	5.36
Long-Biased Credit	12.37
Structured Credit	1.69
<b>Event</b>	10.27
Event Equity	2.34
Merger Arb	2.13
Multi-Strategy Event	4.29
Reinsurance	1.52
<b>Hedged Equity</b>	36.93
Long-Biased Equity	4.31
Loose Neutral Equity	6.76
Opportunistic Equity	22.64
Short-Biased Equity	3.22
<b>Macro &amp; Commodity</b>	9.34
Diversified Global Macro	9.34
<b>Multi Strategy</b>	4.98
Multi-Strategy	4.98
<b>Relative Value</b>	12.98
Multi-Strategy Relative Value	7.99
Strict Market Neutral	3.14
Volatility Arbitrage	1.85
<b>Liquidating/Cash</b>	6.07
Liquidating	0.62
Cash	5.45

Interest Rate Risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Duration (period of time to maturity or redemption) is the primary measure of the sensitivity of investment risk. The Plan has a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation. The Board of Managers recognizes that some risk is necessary to produce long-term investment results that are sufficient to meet the Plan's objectives. However, the investment managers are to make reasonable efforts to control risk, and will be evaluated regularly to ensure that the risk assumed is commensurate with the given investment style and objectives.

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**6. INVESTMENTS (Continued)**

*Custodial Credit Risk* is the risk that the party holding the funds might not be able to pay those funds to the Trust upon maturity or demand. Bank deposits are covered by federal depository insurance (FDIC) or are collateralized by a multiple financial institution collateral pool administered by the State Treasurer.

Concentration of Investments

The Plan did not hold investments in any one organization that represented 5 percent or more of the Pension Plan's fiduciary net position.

Fair Value of Investments

Investments are reported at fair value, based on quoted market prices.

**7. NET PENSION LIABILITY:**

The components of the net pension liability of the Plan at June 30, 2016 were as follows:

Total Pension Liability	<u>\$ 101,443,350</u>
Plan Fiduciary Net Position	<u>44,229,422</u>
The Plan's Net Pension Liability	<u>\$ 57,213,928</u>
Plan Fiduciary Net Position as a percentage of Total Pension Liability	43.60%

Actuarial Assumptions:

The total pension liability was determined by an actuarial valuation as of July 1, 2015, using the following actuarial assumptions, applied to all periods included in the measurement, with the results rolled forward to June 30, 2016:

Inflation	2.50%
Salary increases	2.50%, plus age-related salary scale based on participant group
Investment rate of return	7.50%, including inflation, net of pension plan investment expense

Health Mortality rates were based on the sex distinct RP-2014 Blue Collar Employee Mortality Table, set forward two years for males and four years for females. Disabled Mortality rates were based on the sex distinct RP-2014 Disabled Retiree Mortality Table. All mortality tables are projected generationally with Scale MP-2015.

The actuarial assumptions used in the July 1, 2015 valuation were based on the results of an experience study for the period July 1, 2010 to June 30, 2015.

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**7. NET PENSION LIABILITY (Continued):**

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return for each major asset class included in the pension plan's target asset allocation as of June 30, 2016 are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Domestic equity	42%	6.75%
International markets equity	20%	7.45%
Core fixed income	20%	1.75%
High yield fixed income	5%	4.95%
Hedge funds	<u>13%</u>	3.75%
Total	100%	

Discount rate: The blended discount rate used to measure the total pension liability was 7.50%. The projection of cash flows used to determine the discount rate assumed contributions will continue to be made at 5.22% of compensation from plan members and 5.22% of compensation from the City. For this purpose, only employer contributions that are intended to fund benefits of current plan members and their beneficiaries are included. Projected employer contributions that are intended to fund the service costs of future plan members and their beneficiaries are excluded, as are projected employee contributions from future plan members. Based on these assumptions, the System's fiduciary net position was not projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on the System's 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 following presents the net pension liability of the County, calculated using the discount rate of 7.50%, as well as what the Plan's 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%) than the current rate:

	1% Decrease (6.50%)	Current Discount (7.50%)	1% Increase (8.50%)
Plan's net pension liability	\$62,243,229	\$57,213,928	\$52,506,192

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**8. MEMBERSHIP INFORMATION**

Membership of the Plan consisted of the following at July 1, 2015, the date of the latest actuarial valuation:

Active employees	1,455
Retired Participants and Beneficiaries	395
Inactive members due a refund of contributions	<u>8</u>
	<u>1,858</u>

**9. DATE OF MANAGEMENT'S REVIEW**

In preparing these financial statements, the Organization has evaluated events and transactions for potential recognition or disclosure through October 21, 2016, the date the financial statements were available to be issued.

**REQUIRED SUPPLEMENTARY INFORMATION**

**THE CITY OF BIRMINGHAM  
FIREMEN'S AND POLICEMEN'S  
SUPPLEMENTAL PENSION SYSTEM  
REQUIRED SUPPLEMENTARY INFORMATION  
FOR YEAR ENDED JUNE 30, 2016**

**Schedule of Changes in the Plan's Net Pension Liability and Related Ratios**

	2016	2015	2014
<b><u>Total Pension Liability</u></b>			
Service Cost	\$ 8,428,083	\$ 7,944,887	\$ 7,504,493
Interest	6,601,838	6,642,762	6,517,060
Changes of Benefit Terms	627,885	-	-
Differences Between Expected and Actual Experience	(16,324)	(869,040)	-
Changes of Assumptions	(23,025,349)	365,390	-
Benefit Payments, Including Refunds of Employee Contributions	(15,214,638)	(11,943,335)	(11,712,272)
<b>Net Change in Total Pension Liability</b>	<b>(22,598,505)</b>	<b>2,140,664</b>	<b>2,309,281</b>
<b>Total Pension Liability – Beginning</b>	<b>124,041,855</b>	<b>121,901,191</b>	<b>119,591,910</b>
<b>Total Pension Liability - Ending (a)</b>	<b>\$ 101,443,350</b>	<b>\$ 124,041,855</b>	<b>\$ 121,901,191</b>
<b><u>Plan fiduciary net position</u></b>			
Contributions – Employer	\$ 4,364,213	\$ 4,212,776	\$ 4,090,689
Contributions- Employee	4,348,710	4,197,254	4,074,251
Contributions-Fire tax	404,462	362,196	209,691
Transfer from Limited Firemen's Pension	-	-	104,208
Net Investment Income	(445,516)	1,028,214	6,708,660
Benefit Payments, Including Refunds of Employee Contributions	(15,214,638)	(11,943,335)	(11,712,272)
Administrative Expense	(72,692)	(75,251)	(36,850)
<b>Net Change in Plan Fiduciary Net Position</b>	<b>(6,615,461)</b>	<b>(2,218,146)</b>	<b>3,438,377</b>
<b>Plan Fiduciary Net Position – Beginning</b>	<b>50,844,883</b>	<b>53,063,029</b>	<b>49,624,652</b>
<b>Plan Fiduciary Net Position - Ending (b)</b>	<b>44,229,422</b>	<b>50,844,883</b>	<b>53,063,029</b>
<b>The Plan's Net Pension Liability - Ending (a) - (b)</b>	<b>\$ 57,213,928</b>	<b>\$ 73,196,972</b>	<b>\$ 68,838,162</b>
<b><u>Plan Fiduciary Net Position as a Percentage of the Total Pension Liability</u></b>			
Covered Employee Payroll	\$ 83,308,621	\$ 80,407,165	\$ 78,050,785
The Plan's Net Pension Liability as a Percentage of covered Employee Payroll	68.68%	91.03%	88.20%
<b><u>Schedule of Investment Returns</u></b>			
Annual money-weighted rate of return, net of investment expense	.19%	2.20%	

Notes to the above schedule:

The only change in benefit provisions since GASB 67 implementation was an increase in the Retirement and Relief contribution rate from 6.50% to 7.00%, which impacts the transfers from this System to the Retirement and Relief System. The discount rate for GASB reporting purposes 5.73% as of June 30, 2014, 5.67% as of June 30, 2015, and 7.50% as of June 30, 2016. A detailed study of experience for the five-year period ending June 30, 2015 was performed and the recommendations of the experience study were approved by the Board in May, 2016. Historical information prior to the implementation of GASB 67/68 is not required.

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SUPPLEMENTAL PENSION SYSTEM  
REQUIRED SUPPLEMENTARY INFORMATION  
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**Schedule of the Employer's Contributions**

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Actuarially Determined Contributions*	\$4,960,548	\$ 6,038,436	\$ 5,839,810
Contributions in Relation to the Actuarially Determined Contributions	<u>4,364,213</u>	<u>4,212,776</u>	<u>4,090,689</u>
Contribution Deficiency (Excess)	<u>596,335</u>	<u>1,825,660</u>	<u>1,749,121</u>
Covered Employee Payroll**	83,308,621	80,407,165	78,050,785
Contributions as a Percentage of Covered Employee Payroll	5.24%	5.24%	5.24%

Notes to Schedule:

\*The actuarially determined contribution is equal to the total calculated contribution in the most recent actuarial valuation, minus the portion expected to be covered by employee contributions.

\*\*Payroll is estimated based on the actual employee contributions received and a 5.22% contribution rate. Historical information prior to implementation of GASB 67/68 is not required.

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SUPPLEMENTAL PENSION SYSTEM  
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION**

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

Valuation date	7/1/15
Actuarial cost method	Entry Age
Amortization method	Level percent of payroll, using 2.50% annual increases
Remaining amortization period	Rolling 30 years
Asset valuation method	Market value of assets less unrecognized returns in each of the last five years. Unrecognized return is equal to the difference between the actual market return and the expected return on the market value, and is recognized over a 5 year period, further adjusted, if necessary, to be within 20% of the market value.

Actuarial assumptions:

Investment rate of return	7.50%, including inflation, net of pension plan investment expense
Projected salary increase	2.50%, plus age-related salary scale based on participant group
Inflation rate	2.50%
Cost of living adjustments	N/A