Harris County Hospital District Pension Plan

Independent Auditor's Report, Financial Statements and
Required Supplementary Information

December 31, 2017 and 2016

BKD LLP
CPAs & Advisors

Harris County Hospital District Pension Plan
December 31, 2017 and 2016

Contents

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Independent Auditor's Report

Board of Trustees, Pension and Disability
Committee and Plan Administrator
Harris County Hospital District,
d/b/a Harris Health System
Houston, Texas

We have audited the accompanying financial statements of Harris County Hospital District Pension Plan (the Plan), which comprise the statement of fiduciary net position as of December 31, 2017, 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 entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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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 2017 financial statements referred to above present fairly, in all material respects, the fiduciary net position of the Plan as of December 31, 2017, and the changes in fiduciary net position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Prior Year Audited by Other Auditors

The 2016 financial statements were audited by other auditors whose unmodified report on those statements thereon, dated June 29, 2017, included an emphasis paragraph that described the adoption of Governmental Accounting Standards Board (GASB) Statement No. 72, *Fair Value Measurement and Application*.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and pension information 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 GASB, 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 2017 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 2017 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.

The other auditors did not express an opinion or provide any assurance on the 2016 required supplementary information.

BKD, LLP

Houston, Texas
June 28, 2018

Harris County Hospital District Pension Plan
Management's Discussion and Analysis (Unaudited)
December 31, 2017 and 2016

As management of the Harris County Hospital District, d/b/a Harris Health System (the System), we offer readers of the Harris County Hospital District Pension Plan (the Plan) financial statements, this narrative overview and analysis of the financial activities of the Plan for the years ended December 31, 2017 and 2016.

Financial Highlights

- Net position of the Plan as of December 31, 2017, 2016, and 2015 were $686,312,249, $594,401,173 and $564,716,739, respectively. These net assets are restricted for use for the payment of future employee pension benefits.
- The Plan's net position restricted for pensions increased $91,911,076 for the year ended December 31, 2017. Net position increased $29,684,434 for the year ended December 31, 2016 and decreased $19,544,526 for the year ended December 31, 2015.
- Contributions to the Plan are made solely by the employer, the System, as determined by the Plan's actuaries based on future obligations and required funding to meet those obligations. These contributions totaled $29,432,523, $32,693,266, and $31,758,544 for the years ended December 31, 2017, 2016, and 2015, respectively.
- The Plan's total investment income (loss) in 2017, 2016, and 2015 was $107,519,240, $39,528,831, and ($4,891,065), yielding a total return on investment of 17.9 percent, 6.6 percent, and (1.2 percent), respectively. Investment income consists of interest, dividend income and net appreciation (depreciation) in the fair value of investments. In 2015, the Plan's fund performance reflected waning equity market momentum and a rise in volatility. In 2016, global and U.S. economic activity firmed and strengthened in 2017. A detail of the asset allocation for the years ended December 31, 2017, 2016 and 2015 was as follows:

	2017	2016	2015
Domestic equities (common stock)	33 %	35 %	52 %
International equities (collective investment trust and mutual fund)	28	25	18
Fixed income investments (collective investment trust, mutual fund and fixed income securities)	31	35	30
Hedge funds (collective investment trust)	4	5	-
Real estate funds (collective investment trust)	4	-	-
Total	100 %	100 %	100 %

- Benefit payments are the primary expense of the Plan. Such payments totaled $42,562,562, $40,177,655, and $44,023,057 for the years ended December 31, 2017, 2016, and 2015, respectively. In calendar 2017 there were no lump-sum payouts to terminated vested participants. Calendar 2016 payments included $420,827 in lump-sum payouts to 120 participants.

- Other expenses of the Plan include administrative and investment expenses, which totaled $2,478,125, $2,360,108, and $2,388,948 for the years ended December 31, 2017, 2016, and 2015, respectively.

Overview of the Financial Statements

Our discussion and analysis is intended to serve as an introduction to the Plan's basic financial statements. The Plan's financial statements are composed of financial statements and notes to the financial statements. The financial statements consist of two statements: (1) statements of fiduciary net position and (2) statements of changes in fiduciary net position. These statements present information on all the Plan's assets and liabilities with the difference between the two reported as net position restricted for pensions. Over time, increases or decreases in net position restricted for pensions may serve as a useful indicator of whether the financial position of the Plan is improving or deteriorating. The statements of changes in fiduciary net position present information showing how the Plan's net position restricted for pensions changed during the year. The notes provide additional information that is essential to a full understanding of the data provided in the financial statements.

Investment Policy

The Plan's investment policy requires the Plan to maintain target asset allocation and ranges for the total fund. The asset allocation and ranges are as follows:

	Target	Range
Domestic equities	30 %	23-47 %
International equities	25	18-32
Fixed income investments	35	23-47
Hedge funds	5	3-7
Real estate funds	5	3-7
Total	100 %	

The Plan's investment policy was adhered to during the years ended December 31, 2017, 2016, and 2015.

Fiduciary Net Position

	2017	2016	2015
Cash	$ 9,003,172	$ 2,834	$ -
Common stocks	220,057,617	213,391,279	284,301,375
Mutual funds	233,015,240	205,053,791	125,068,078
Collective investment trusts	131,279,029	83,144,599	53,196,480
Fixed income securities	84,034,860	84,385,114	88,238,574
Short-term investments	19,876,084	17,882,843	17,002,973
Receivables from accrued income and other	708,488	2,643,383	1,312,693
	697,974,490	606,503,843	569,120,173
Liabilities from accrued expenses and other	(11,662,241)	(12,102,670)	(4,403,434)
Net Position Restricted for Pension Benefits	$ 686,312,249	$ 594,401,173	$ 564,716,739

	2017	2016	2015
Beginning balance	$ 594,401,173	$ 564,716,739	$ 584,261,265
Contributions	29,432,523	32,693,266	31,758,544
Investment income (loss)	107,519,240	39,528,931	(4,891,065)
Deductions	(45,040,687)	(42,537,763)	(46,412,005)
	$ 686,312,249	$ 594,401,173	$ 564,716,739

Request for Information

This financial report is designed to provide Plan's finances. Questions about this report and requests for additional financial information should be directed to the Harris County Hospital District, d/b/a Harris Health System, Attn. Benefits Department, 2525 Holly Hall, Houston, TX 77054.

Harris County Hospital District Pension Plan
Statements of Fiduciary Net Position
December 31, 2017 and 2016

	2017	2016
Assets		
Cash	$ 9,003,172	$ 2,834
Investments, at Fair Value		
Fixed income securities	84,034,860	84,385,114
Mutual funds:		
Fixed income	113,615,335	114,234,624
International equity	119,399,905	90,819,167
Common stocks	220,057,617	213,391,279
Collective investment trusts:		
International equity	71,494,038	54,651,693
Multistrategy	30,484,352	28,492,906
Real estate	29,300,639	-
Short-term investments	19,876,084	17,882,843
Total investments	688,262,830	603,857,626
Receivables		
Due from broker for securities sold	204,631	2,084,486
Accrued interest and dividends	503,857	558,897
Total receivables	708,488	2,643,383
Total assets	697,974,490	606,503,843
Liabilities		
Accrued administrative expenses	553,219	557,926
Due to broker for securities purchased	11,109,022	11,544,744
Total liabilities	11,662,241	12,102,670
Net position restricted for pension benefits	$ 686,312,249	$ 594,401,173

Harris County Hospital District Pension Plan

Statements of Changes in Fiduciary Net Position

Years Ended December 31, 2017 and 2016

	2017	2016
Employer Contributions	$ 29,432,523	$ 32,693,266
Investment Income		
Net appreciation in fair value of investments	95,746,648	27,641,231
Interest	2,083,829	1,817,803
Dividends	9,621,968	10,029,185
Other	66,795	40,712
Total investment income	107,519,240	39,528,931
Total additions	136,951,763	72,222,197
Benefits paid to participants and beneficiaries	42,562,562	40,177,655
Administrative expenses	2,478,125	2,360,108
Total deductions	45,040,687	42,537,763
Net Increase in Net Position Restricted for Pensions	91,911,076	29,684,434
Net Position Restricted for Pensions, Beginning of Year	594,401,173	564,716,739
Net Position Restricted for Pensions, End of Year	$ 686,312,249	$ 594,401,173

Harris County Hospital District Pension Plan
Notes to Financial Statements
December 31, 2017 and 2016

Note 1: Description of the Plan

The following description of Harris County Hospital District Pension Plan (the Plan) provides only general information. Participants should refer to the *Summary Plan Description* for more complete information, a copy of which is available from the Harris County Hospital District, d/b/a Harris Health System (the System).

General

The Plan is a noncontributory, single-employer defined-benefit pension plan covering all full-time employees of the System who meet the Plan's service requirements. As a governmental plan, it is exempt from the reporting and disclosure requirements of the Employee Retirement Income Security Act of 1974 and follows the reporting requirements as dictated by the Governmental Accounting Standards Board (GASB).

In October 2006, the System Board of Trustees (Board) amended the Plan to close enrollment to new hires effective January 1, 2007. The amended plan offers employees hired prior to January 1, 2007, a choice to either (1) continue with their current pension plan or (2) elect to participate in the System's enhanced 401(k) retirement savings plan with a match, effective July 2007, of up to 5 percent of participant's compensation provided by the System. All new hires and rehires after December 31, 2006 are only eligible for the System's 401(k) retirement savings plan with a match up to 5 percent.

The Plan is administered by an administrative committee (the Committee) appointed by the Board of the System. The Committee comprises nine members who are responsible for administering the Plan under the terms that are established. The Board, as authorized in the *Plan Document*, approves amendments to the Plan. State Street (the Trustee) serves as trustee and custodian for the Plan.

Pension Benefits

Active employees with one or more years of service, who meet eligibility requirements are entitled to a monthly pension payment beginning at normal retirement age (65) equal to the benefit accrued based on compensation and years of service. The Plan permits early retirement at ages 55 to 64, provided 10 years of service has been completed. If employees terminate after 5 years of service, they retain the right to vested benefits. Participants become 100 percent vested in their accrued benefits after 5 years of service. Each participant shall have a monthly benefit payable for life that is equal to the greater of (a) the number of years of service multiplied by 1.5 percent of the average monthly compensation (average base compensation received in the five highest consecutive calendar years out of the 10 complete calendar years prior to retirement) or (b) the accrued monthly retirement benefit determined as of January 1, 1989, plus the number of years of future service earned after January 1, 1989, multiplied by 1.5 percent of the average monthly compensation, subject to a minimum equal to the benefit earned under the Plan prior to the adoption of the sixth amendment as of September 30, 1991 (applies to non-highly compensated employees only). Monthly benefit payments are subject to a minimum based on the number of years of service multiplied by $6 and a maximum provision permitted to be paid under Section 415 of the Internal Revenue Code (the Code). Participants may also elect to receive their benefits in other optional forms.

If the present value of a terminating participant's vested benefit is $1,000 or less, the benefit will automatically be paid in a lump sum.

During 2017 there were no lump-sum payments made to terminated participants. In 2016 the Plan made lump-sum payments of $420,827 to 120 participants.

Death and Disability Benefits

If an active employee dies, a benefit equal to one-half of the normal pension benefit will be due to the spouse of the participant if the participant has attained 10 years of service. The beneficiary of a deceased retired participant is entitled to a lump-sum payment of $5,000. If a participant becomes disabled, the participant will be paid 55 percent of his/her average monthly compensation, less 64 percent of the monthly primary social security benefit at the time of disability. Disability benefits will be paid during the participant's disability or until retirement age is reached, whichever is shorter.

Plan Membership

Membership of the Plan consisted of the following as of January 1, 2017 and 2016, respectively:

	2017	2016
Inactive Plan members or beneficiaries currently receiving benefits	2,942	2,888
Inactive Plan members entitled to but not yet receiving benefits	1,366	1,450
Active Plan members	2,617	2,668
Total Plan members	6,925	7,006

Note 2: Summary of Significant Accounting Policies

Basis of Accounting

The accompanying financial statements are prepared on the accrual basis of accounting. The Plan applies the GASB pronouncements applicable to benefit plan accounting and reporting.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and changes therein, disclosure of contingent assets and liabilities and the actuarial present value of accumulated Plan benefits at the date of the financial statements and changes therein. Actual results could differ from those estimates.

Risks and Uncertainties

The Plan utilizes various investment securities, including U.S. government securities, corporate debt instruments, mutual funds, corporate stocks, collective investment trust funds and real estate investment trusts. Investment securities, in general, are exposed to various risks, such as interest rate, credit risk, and overall market volatility risks. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the financial statements.

The actuarial present value of accumulated Plan benefits is calculated based on economic and demographic assumptions, including investment return rates, inflation rates, salary increases, retirement ages and mortality rates. Due to uncertainties inherent in the estimations and assumptions processes, it is at least reasonably possible that changes in these estimates and assumptions in the near term would be material to the financial statements.

Valuation of Investments and Income Recognition

Investments are reported at fair value. Quoted market prices, if available, are used to value investments. Mutual funds are valued at the net asset value (NAV) of shares held by the Plan at year-end. Common stocks are valued at the closing price reported on the active market on which the individual securities are traded. Fixed income securities are valued on the basis of yields currently available on comparable securities of issuers with similar credit ratings. Units of collective investment trust funds are stated at fair value as determined by the issuer of the fund based on the fair value of the underlying investments

Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date. Net appreciation in fair value of investments includes the Plan's gains and losses on investments bought and sold, as well as held during the year.

Management fees and operating expenses charged to the Plan for investments in mutual funds are deducted from income earned on a daily basis and are not separately reflected. Consequently, management fees and operating expenses are reflected as a reduction of investment return for such investments.

Administrative Expenses

All administrative expenses incurred in the operation of the Plan are paid by the Plan as provided in the *Plan Document*. The Plan Sponsor provides accounting and certain other administrative services to the Plan at no charge.

Payment of Benefits

Benefit payments to participants are recorded upon distribution.

Contributions

Contributions to provide benefits under the Plan are made solely by the System. The System makes annual contributions based on an actuarial valuation of the Plan. The actuarial recommended contribution includes normal cost, plus amortization of the expected unfunded liability, if any.

Note 3: Investments

The fair value of investments as of December 31, 2017 and 2016 is presented in the following table:

	2017	2016
Common stocks	$ 220,057,617	$ 213,391,279
Mutual funds	233,015,240	205,053,791
Collective investment trusts	131,279,029	83,144,599
Fixed income securities	84,034,860	84,385,114
Short-term investments	19,876,084	17,882,843
Total	$ 688,262,830	$ 603,857,626

The Plan categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure fair value of the assets. Level 1 are quoted prices in an active market for identical assets, Level 2 are significant other observable inputs and Level 3 are significant unobservable inputs.

The mutual funds held by the Plan are actively traded and valued at the daily closing price as reported by the fund and are disclosed as investments in Registered Investment Companies. The collective investment trusts held by the Plan are valued at net asset value of the respective investments as a practical expedient to estimate fair value. This practical expedient would not be used if it is determined to be probable that the investment will be sold for an amount different from the reported net asset value.

Harris County Hospital District Pension Plan
Notes to Financial Statements
December 31, 2017 and 2016

The following is a summary of the hierarchy of the fair value of investments of the Plan as of December 31, 2017 (in thousands):

	2017 Fair Value Measurement Using		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	December 31, 2017 Total
Debt securities:			
U.S. Treasury securities	$ -	$ 44,954	$ 44,954
Asset backed	-	4,026	4,026
Agencies	-	2,762	2,762
Commercial mortgage-backed securities	-	5,191	5,191
Corporate bonds	-	22,918	22,918
Mortgages	-	2,902	2,902
Municipals	-	1,282	1,282
Fixed income mutual funds	113,615	-	113,615
Total debt securities	113,615	84,035	197,650
Equity securities:			
Domestic	220,058	-	220,058
International	119,400	-	119,400
Total equity securities	339,458	0	339,458
Short-term investment funds	0	19,876	19,876
Total investments by fair value level	$ 453,073	$ 103,911	556,984
Collective investment trusts measured at the net asset value (NAV):			
International equity			71,494
Hedge funds - multistrategy			30,484
Real estate			29,301
Total investments at NAV			131,279
Total investments measured at fair value			$ 688,263

The following is a summary of the hierarchy of the fair value of investments of the Plan as of December 31, 2016 (in thousands).

	2016		
	Fair Value Measurement Using		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	December 31, 2016 Total
Debt securities:			
U.S. Treasury securities	$ -	$ 44,066	$ 44,066
Asset backed	-	4,394	4,394
Commercial mortgage-backed securities	-	5,726	5,726
Corporate bonds	-	20,260	20,260
Mortgages	-	9,582	9,582
Municipals	-	357	357
Fixed income mutual funds	114,235	-	114,235
Total debt securities	114,235	84,385	198,620
Equity securities:			
Domestic	213,391	-	213,391
International	90,819	-	90,819
Total equity securities	304,210	0	304,210
Short-term investment funds	0	17,883	17,883
Total investments by fair value level	$ 418,445	$ 102,268	520,713
Collective investment trusts measured at the net asset value (NAV):			
International equity			54,652
Hedge funds - multistrategy			28,493
Total investments at NAV			83,145
Total investments measured at fair value			$ 603,858

Investments Measured Using the Net Asset Value per Share Practical Expedient

The following table summarizes investments for which fair value is measured using the net asset value per share practical expedient as of December 31, 2017 and 2016. There are no participant redemption restrictions for these investments; the redemption notice period is applicable only to the Plan.

Harris County Hospital District Pension Plan
Notes to Financial Statements
December 31, 2017 and 2016

		Fair Value	Unfunded Commitments	Redemption Frequency (if currently eligible)	Redemption Notice Period
December 31, 2017:					
International equity	$	71,494	None	Daily	None
Hedge funds - multistrategy		30,484	None	Monthly	95 days
Real estate		29,301	None	Quarterly	45 days
Total investments at NAV	$	131,279			
December 31, 2016:					
International equity	$	54,652	None	Daily	None
Hedge funds - multistrategy		28,493	None	Monthly	95 days
Total investments at NAV	$	83,145			

For collective investment trust assets that are measured at NAV per share, the valuation provided by the fund manager is used. All partnerships provide audited financial statements, along with unaudited quarterly reports.

International equity - The trust's investment is an international equity and the investment objective is to seek long-term capital appreciation above the MSCI All Country World Ex-U.S. Investable Market Index (net), by investing at least 80 percent of its total assets in a diversified portfolio of common stocks and in securities convertible into, exchangeable for or having the right to buy such common stocks that issued by companies of all sizes domiciled outside the United States.

Hedge funds - multistrategy - This type invests in hedge funds that pursue multiple strategies to diversify risks and reduce volatility, primarily through limited partnerships. The fund is organized by investing substantially all assets through a master feeder structure and may use a wide range of investment strategies.

Real estate – This type invests in institutional quality real estate private equity funds to provide income, low-correlation to other investments and a hedge against inflation.

During the Plan years ended December 31, 2017 and 2016, the Plan's investments (including investments bought, sold and held during the Plan year) appreciated in value by $95,746,648 and by $27,641,231 respectively, as follows.

	2017	2016
Common stocks	$ 48,369,334	$ 27,461,290
Mutual funds	27,115,001	272,341
Collective investment trusts	20,262,313	(92,400)
Total	$ 95,746,648	$ 27,641,231

During the years ended December 31, 2017 and 2016, interest and dividends earned on the Plan's investments amounted to $11,705,797 and $11,846,988, respectively.

Note 4: Investment Risk Disclosures

Investment Policy

Substantially all of the Plan's investments are held by the Trustee. The Committee authorizes various portfolio managers to manage investments within the guidelines of the Plan's statement of investment policy (the Policy) set forth by the Committee. The Policy mandates a diversified portfolio, which includes investments in collective investment trusts, fixed income securities and equity securities. GAAP requires disclosure of common deposit and investment risks, including credit risk, concentration of credit risk, custodial credit risk, interest rate risk and foreign currency risk of investments.

The Policy in regard to the allocation of invested assets is established and may be amended by the System's Board of Trustees by a majority vote of its members. It is the policy of the Plan Board to pursue an investment strategy that reduces risk through the prudent diversification of the portfolio across a broad selection of distinct asset classes. The Policy discourages the use of cash equivalents, except for liquidity purposes and aims to refrain from dramatically shifting asset class allocations over short time spans. The following was the Board of Trustee's adopted asset allocation as of December 31, 2017 and 2016:

Asset Class	2017 Target allocation	2016 Target allocation
International equity	25 %	25 %
Fixed income	35	35
Domestic equity	30	35
Hedge funds	5	5
Real estate funds	5	-
	100 %	100 %

Money-weighted Rate of Return

For the years ended December 31, 2017 and 2016, the annual money-weighted rate of return on pension plan investments, net of pension investment expenses, was 17.93 percent and 6.65 percent, respectively. The money-weighted rate of return expresses investment performance, net of investment expense, adjusted for the changing amounts actually invested.

Credit Risk and Concentration of Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. The Policy establishes minimum acceptable credit ratings for certain investment instruments. Fixed income investment managers are expected to invest in a well-diversified mix of debt instruments, including U.S. Treasury, agency, mortgage-backed, asset-backed, corporate, Eurodollar, and Yankee issue. The Core Plus Fixed Income Investment manager may also invest in derivative instruments such as options, future contracts or swap agreements. With the exception of the U.S. Treasury and its agencies, no more than five percent of the market value of the portfolio should be invested in the securities of a single issuer. No more than fifteen percent of the Fixed Income Investment Manager's portion of the Plan or one hundred twenty percent of the benchmark's allocation, whichever is greater, shall be rated less than "A" quality. Bonds of foreign issuers are permitted to comprise up to thirty percent of a Fixed Income Investment Manager's portfolio. The duration of the portfolio is expected to be within fifty percent of the index's duration. Guidelines for diversification and risk tolerance are detailed within the Policy. Additionally, the Policy includes specific investment strategies for fund groups that address each group's investment options and describes the priorities for suitable investments. GAAP does not require disclosure of U.S. government obligations explicitly guaranteed. As of December 31, 2017 and 2016, below are the Plan's fixed income investments, excluding U.S. government obligations, at fair value:

	2017		2016	
Security Type	**Fair Value**	**Quality**	**Fair Value**	**Quality**
Fixed income securities:				
Asset backed	$ 4,025,714	AAA	$ 4,394,216	AAA
Agencies	2,762,136	AAA	-	
Commercial mortgage-backed securities	5,190,524	AAA	5,725,705	AAA
Mortgages	2,902,276	AA+	9,582,440	AA+
Corporate	22,917,705	A	20,259,586	A-
Municipal	1,282,448	AA+	356,922	AA+
Mutual funds	113,615,335	A-	114,234,624	BBB+
Total	$ 152,696,138		$ 154,553,493	

Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The System mitigates these risks by emphasizing the importance of a diversified portfolio. All funds must be sufficiently diversified to eliminate the risk of loss resulting from overconcentration of assets in a specific maturity, a specific issuer or a specific class of securities. In particular, no more than 5 percent of an equity portfolio may be invested in a single company without consent of the Committee. Holdings in any one industry or sector are not to exceed 30 percent of the portfolio market value. No more than 20 percent of the portfolio may be invested in cash equivalents and fixed income securities with fixed income securities not exceeding 15 percent. Concentration by issuer for other investment instruments is limited to 5 percent. The Policy does specify that acceptable investment instruments must have high-quality credit ratings and, consequently, risk is minimal.

As of December 31, 2017 and 2016, the Plan did not hold more than 5 percent of assets in any single issuer other than mutual funds, U.S. government obligations, collective investment trust funds or obligations of U.S. government chartered entities.

The Plan maintained no investments in derivatives as of December 31, 2017 or 2016,

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of failure of a depository financial institution, the Plan will not be able to recover its deposits or will not be able to recover collateral securities that are in possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the Plan will not be able to recover the value of its investment or collateral securities that are in possession of another party.

The Plan does not have a formal policy for custodial credit risk. As of December 31, 2017 and 2016, all investments are held in a nominee name of the custodian for the benefit of the Plan.

Interest Rate Risk

All investments carry the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater is the sensitivity of its fair market value to changes in market interest rates. The Plan does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from changing interest rates. Interest rate risk is limited by the short-term nature of the investments.

As of December 31, 2017 and 2016, the Plan had the following investments in its fixed income accounts.

	2017		2016	
Security Type	**Fair Value**	**Weighted-average maturity in years**	**Fair Value**	**Weighted-average maturity in years**
Fixed income securities:				
Asset backed	$ 4,025,714	6.21	$ 4,394,216	5.27
Agencies	2,762,136	4.51	-	
Commercial mortgage-backed securities	5,190,524	5.51	5,725,705	5.64
Mortgages	2,902,276	1.98	9,582,440	4.63
Corporate	22,917,705	4.7	20,259,586	5.09
Municipal	1,282,448	7.79	356,922	7.42
U.S. Treasury	44,954,057	4.26	44,066,245	4.37
Mutual funds	113,615,335	7.04	114,234,624	6.68
Total	$ 197,650,195		$ 198,619,738	

Foreign Currency Risk

Foreign currency risk is the risk that fluctuations in the exchange rate will adversely affect the value of investments denominated in a currency other than the U.S. dollar.

The Plan holds investments in collective investment trust funds and mutual funds that are invested in international equities. These investments are denominated in U.S. dollars and accounted for at fair value. The Plan has no exposure to foreign currency fluctuations.

Note 5: Net Pension Liability of the System

The components of the net pension liability of the System as of December 31, 2017 and 2016 were as follows (in thousands):

	2017	2016
Total pension liability	$ 866,805	$ 828,711
Plan fiduciary net position	686,312	594,401
System net pension liability	$ 180,493	$ 234,310
Plan fiduciary net position as a percentage of the total pension liability	79.18%	71.72%

Harris County Hospital District Pension Plan
Notes to Financial Statements
December 31, 2017 and 2016

Actuarial Assumptions

The total pension liability was determined by an actuarial valuation as of December 31, 2017 and 2016, using the following actuarial assumptions.

	2017	2016
Actuarial cost method	Entry age normal	Entry age normal
Inflation	3.0%	3.0%
Postretirement benefit increase		
Investment rate of return - net of expenses	7.0%	7.5%
Projected salary increases (ultimate rate)	3.0%	4.0%
Cost of living adjustment	-	-
Assumed retirement age	Various retirement age rates were assumed for ages 55 through 70	Various retirement age rates were assumed for ages 55 through 70
Mortality rate:	Healthy:	Healthy:
	RP-2014 Bottom Quartile Mortality Table, adjusted to 2006 with generational mortality improvement projected after year 2006 using Scale MP-2017 with generational mortality improvement of Scale MP-2014	RP-2014 Bottom Quartile Mortality Tables with generational mortality improvement projected after 2014 with 50% of Scale MP-2014
	Disabled:	Disabled:
	RP-2014 Disability Mortality Table, adjusted to 2006, with generational mortality improvement projected after year 2006 using MP-2017 with generational mortality improvement of Scale MP-2017	RP-2014 Disability Mortality Table
	Mortality lmprovement:	Mortality lmprovement:
	The mortality tables include fully generational mortality improvement projected after year 2006 using Scale MP-2017	The mortality table for healthy lives includes fully generational mortality improvement projected after year 2014 using 50% of Scale MP-2014

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 Plan's target asset allocation as of December 31, 2017 and 2016 (see the discussion of the Plan's investment policy) are summarized in the following table.

	Expected Real Rate of Return 2017	Expected Real Rate of Return 2016
Asset class:		
Domestic equity - large cap	8.40 %	9.13
Domestic equity - small cap	9.32	10.15
International equity	8.86	9.33
Fixed income	5.03	6.54
Hedge funds	10.87	10.55
Real estate	7.30	-

Discount Rate

The discount rate used to measure the total pension liability was 7.0 percent and 7.5 percent in 2017 and 2016, respectively. The projection of cash flows used to determine the discount rate assumed that employer contributions will be made at rates equal to the actuarially determined contribution rates. Based on those 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 on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability. The foregoing actuarial assumptions are based on the presumption that the Plan will continue. If the Plan were to terminate, different actuarial assumptions and other factors might be applicable in determining the actuarial present value of accumulated Plan benefits.

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

The following represents the net pension liability calculated using the stated discount rate, as well as what the net pension liability would be if it were calculated using a discount rate that is one percentage point lower or one percentage point higher than the current rate:

System Net Pension Liability	1% Decrease (6%)	Current Discount Rate (7%)	1% Increase (8%)
		(In Thousands)	
December 31, 2017	$ 282,215	$ 180,493	$ 93,984

System Net Pension Liability	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
		(In Thousands)	
December 31, 2016	$ 331,517	$ 234,310	$ 151,651

Note 6: Tax Status

The Plan has received a determination letter from the Internal Revenue Service dated June 10, 2014, stating that the Plan and related trust, as then designed, were in compliance with the applicable requirements of the Internal Revenue Code and therefore not subject to tax. The Plan has been amended since receiving the determination letter. However, the Plan Administrator believes that the Plan and related trust are currently designed and being operated in compliance with the applicable requirements of the Internal Revenue Code.

Note 7: Plan Termination

Although it has not expressed any intention to do so, the System has the right under the Plan, in certain circumstances, to discontinue contributions to the Plan and to terminate the Plan. In the event that the Plan is terminated, the net assets of the Plan will be allocated generally to provide the following benefits in the order indicated:

- Benefits due to participants who have reached the age of 65 and to beneficiaries of deceased participants
- Benefits due to participants qualified for early retirement, as defined by the Plan
- Benefits due to other participants in proportion to the actuarial value of their accumulated benefits

In the event the assets are not sufficient to carry out any of the foregoing purposes in full, the allocations to the accounts of individuals thereunder shall be made in the proportion that the assets available bear to the assets required to carry out the purpose in full.

Required Supplementary Information
(Unaudited)

Harris County Hospital District Pension Plan

Schedule of Changes in Net Pension Liability and Related Ratios – Last 10 Fiscal Years (which may be built prospectively)

Years Ended December 31, 2017, 2016, 2015 and 2014

(Dollar amounts in thousands)

	2017	2016	2015	2014
Total pension liability:				
Service cost	$ 6,803	$ 7,232	$ 7,795	$ 8,642
Interest	61,427	59,397	57,482	52,342
Changes of benefit terms:				
Difference between expected and actual experience	1,718	(4,063)	4,637	(1,909)
Changes of assumptions	10,709	-	-	40,689
Benefit payments	(42,563)	(40,178)	(44,023)	(34,444)
Net change in total pension liability	38,094	22,388	25,891	65,320
Total pension liability - beginning	828,711	806,323	780,432	715,112
Total pension liability - ending	866,805	828,711	806,323	780,432
Plan fiduciary net position:				
Contributions - employer	29,433	32,693	31,759	31,292
Net investment income	107,519	39,529	(4,891)	37,068
Benefit payments	(42,563)	(40,178)	(44,023)	(34,444)
Administrative expense	(2,478)	(2,360)	(2,389)	(2,301)
Net change in plan fiduciary net position	91,911	29,684	(19,544)	31,615
Plan fiduciary net position - beginning	594,401	564,717	584,261	552,646
Plan fiduciary net position - ending	686,312	594,401	564,717	584,261
System net pension liability - ending	$ 180,493	$ 234,310	$ 241,606	$ 196,171
Plan fiduciary net position as a percentage of the total pension liability	79.18%	71.73%	70.04%	74.86%
Covered payroll	$ 173,272	$ 182,060	$ 197,360	$ 210,728
System net pension liability as a percentage of covered payroll	104.17%	128.70%	122.42%	93.09%

Notes to schedule:

Changes of assumptions - In 2014, amounts reported as changes of assumptions resulted primarily from adjustments to assumed life expectancies as a result of adopting the RP-2014 Bottom Quartile Mortality Tables with generational mortality improvement projected after 2014 with 50% of Scale MP-2014 for purposes of developing mortality rates. In 2017, amounts reported as changes of assumptions resulted from adjustments to the discount rate or investment rate of return.

Harris County Hospital District Pension Plan

Schedule of Investment Returns – Last 10 Fiscal Years (which may be built prospectively) – Unaudited

Years Ended December 31, 2017, 2016, 2015 and 2014

	2017	2016	2015	2014
Annual money-weighted rate of return, net of investment expense	17.93%	6.65%	-1.19%	6.35%

Harris County Hospital District Pension Plan
Schedule of Employer Contributions – Unaudited
Year Ended December 31, 2017
(Dollar amounts in thousands)

	Actuarially Determined Contribution	Actual Annual Contribution	Contribution Deficiency (Excess)	Covered Payroll	Contributions as a % of Covered Payroll
Plan year ended:					
December 31, 2008	$ 17,800	$ 17,800	100 %	$ 257,521	7 %
December 31, 2009	27,538	27,538	100	255,127	11
December 31, 2010	25,219	25,219	100	250,454	10
December 31, 2011	23,657	23,657	100	241,076	10
December 31, 2012	27,486	27,486	100	229,056	12
December 31, 2013	33,959	33,959	100	220,398	15
December 31, 2014	31,292	31,292	100	210,728	15
December 31, 2015	31,759	31,759	100	197,360	16
December 31, 2016	32,693	32,693	100	182,060	18
December 31, 2017	29,433	29,433	100	173,272	17

Harris County Hospital District Pension Plan
Notes to Required Supplementary Information
Year Ended December 31, 2017
(Dollar amounts in thousands)

The information on the required supplementary information was computed as part of the actuarial valuations at the dates indicated.

Additional information as of the latest actuarial valuation is as follows:

Valuation date	December 31, 2017
Actuarial cost method	Entry age normal
Amortization method	Level dollar amortization of unfunded liabilities
Asset valuation method	Market value
Inflation	3.0%
Salary increase (ultimate rate)	3.0%, a decrease from 4.0% from December 31, 2016.
Investment rate of return	7.0%, a decrease from 7.5% from December 31, 2016

Mortality

Healthy:

RP-2014 Bottom Quartile Mortality Table, adjusted to 2006, with generational mortality improvement projected after 2006 using Scale MP-2017 with generational mortality improvement of Scale MP-2017 (RP-2014 Bottom Mortality Tables with generational mortality improvement projected after 2014 with 50% of Scale MP-2014 for December 31, 2016 valuation date).

Disabled:

RP-2014 Disability Mortality Table, adjusted to 2006, with generational mortality improvement projected after year 2006 using Scale MP-2017 with generational mortality improvement of Scale MP-2017 (RP-2014 Disability Mortality Table for December 31, 2016 valuation date).

Mortality Improvement:

The mortality tables include fully generational mortality improvement projected after year 2006 using Scale MP-2017

(The Mortality Table for healthy lives includes fully generational mortality improvement projected after year 2014 using 50% of Scale MP-2014 for December 31, 2016 valuation date).