Annual Financial Report Summary

Teachers' Retirement System of the State of Illinois

for the fiscal years ended June 30, 2013 and June 30, 2012

Teachers' Retirement System of the State of Illinois
a component unit of the State of Illinois
2815 West Washington | P.O. Box 19253 | Springfield, Illinois 62794-9253
http://trs.illinois.gov

Annual Financial Report Summary

for the fiscal years ended June 30, 2013 and June 30, 2012

Board of Trustees

As of December 1, 2013

Sonia Walwyn

Front row, left to right:
Vice President Sharon Leggett; Rainy Kaplan; Cinda Klickna; Marcia Campbell and Cynthia O'Neill
Back row, left to right:
Michael Busby; Mark Bailey; Executive Director Dick Ingram; Enrique M. Vasquez; Bob Lyons; President Christopher A. Koch, Ed. D.
Shown at right: Sonia Walwyn

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As of December 1, 2013

Front row, left to right:
Director of Research Kathleen Farney, CEBS; Senior Assistant General Counsel Cynthia Fain; Director of Administration Jana Bergschneider, CPA; Director of Human Resources Gina Larkin; Executive Assistant Sue Billington and Assistant to the Executive Director Tammy Green
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Teachers' Retirement System of the State of Illinois
2815 West Washington Street | P.O. Box 19253 | Springfield, Illinois 62794-9253
Richard W. Ingram, Executive Director
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December 20, 2013

Dear TRS Members:

This report summarizes the financial condition, investments, actuarial conclusions and statistical information about members, school districts, revenues, and benefits for TRS during the fiscal years ended June 30, 2013 and June 30, 2012.

The presentation of this year's summary mirrors the stylistic and functional upgrades made during 2013 to the TRS website – **http://trs.illinois.gov**. Since the site was launched in 1996, it has steadily grown in importance. In the last year, roughly 1.1 million people visited the TRS website, a volume that easily surpasses any other method of communication.

By all accounts, the long-term funded status of TRS is worst in the nation. TRS's funded ratio at the end of fiscal year 2013 stood at 40.6 percent, on an actuarial basis, with a total long-term unfunded liability of $55.7 billion. The obligations owed members over the next several decades have increased by 162 percent since 2000. However during the same period, TRS assets grew by only 63 percent. According to a media analysis based on assets, TRS currently ranks 41st among both public and private U.S. pension systems, holding $39.9 billion in assets at the end of fiscal year 2013. However, if TRS had been properly funded over the last 74 years, TRS would be among the 10 largest U.S. systems.

For the last two years TRS has played a leading role in pinpointing and explaining the steep challenges faced by the state's five public pension systems. Led by the Board of Trustees, TRS has consistently warned that a growing pension debt and state government's consistent inability to provide actuarially adequate funding will lead to calamity in less than 25 years.

In December 2013 , as this report was being prepared, Gov. Quinn signed legislation into law that is designed to eliminate the TRS unfunded liability by 2045 and stabilize TRS finances for the next 30 years and beyond. While the effective date of the new law is June 1, 2014, a court challenge to the bill's constitutionality is expected. This would likely delay the law's implementation. The long-term stabilization of TRS finances under the new law is accomplished primarily through a reduction in pension benefits for active and retired Tier I members of TRS. The bill also creates a guarantee that state government will provide adequate future contributions to support a fully-funded TRS.

Ensuring the long-term stability and strength of TRS will enable the System to keep the promises made to educators by the State of Illinois for a secure retirement. In good times and bad, TRS has maintained trusted relationships with generations of teachers and has never defaulted on any promises.

TRS has more than fulfilled its duty to properly manage the money entrusted to it by our members. At the end of fiscal year 2013, TRS investments returned 12.8 percent, net of fees, outperforming the System's custom benchmark of 12.5 percent. More importantly, TRS's 30-year investment return exceeded 9 percent, which outperformed the long-term assumed rate of return of 8 percent.

We would like to take this opportunity to express our gratitude to staff, professional consultants and others who have worked so diligently to ensure TRS's successful operation.

Richard Ingram
Executive Director

Jana Bergschneider, CPA
Director of Administration

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for the fiscal years ended June 30, 2013 and June 30, 2012

Fiscal Year 2013 Financial Highlights

- The TRS net position at June 30, 2013 was $39.9 billion.
- During FY13, the net position of TRS increased $3.3 billion.
- Contributions from members, employers, and the state were $3.8 billion, an increase of $303 million or 8.7 percent for the fiscal year.
- Total investment gain was $4.6 billion, compared to investment gain of $224 million in FY12, an increase of $4.3 billion.
- Benefits and refunds paid to members and annuitants were $5.0 billion, an increase of $344 million or 7.4 percent compared to FY12.
- Total actuarial accrued liability was $93.9 billion at June 30, 2013.
- The unfunded actuarial accrued liability increased from $52.1 billion at June 30, 2012 to $55.7 billion at June 30, 2013. The funded ratio decreased from 42.1 percent at June 30, 2012 to 40.6 percent at June 30, 2013. The unfunded liability and funded ratio for both years are calculated using a smoothed value of assets, as required under Public Act 96-0043.

Condensed Comparative Statements of Net Position as of June 30

	2013	Percentage Change	2012	Percentage Change	2011
Cash	$14,659,145	(14.2%)	$17,092,564	(53.6%)	$36,799,319
Receivables and prepaid expenses	506,901,765	55.7	325,464,952	84.2	176,673,155
Investments	39,681,752,953	7.9	36,782,104,053	(2.6)	37,748,341,891
Invested securities lending collateral	1,932,554,323	(26.2)	2,617,763,246	(15.7)	3,104,528,064
Capital assets	4,358,587	0.6	4,331,011	8.5	3,992,703
Total assets	**42,140,226,773**	**6.0**	**39,746,755,826**	**(3.2)**	**41,070,335,132**
Total liabilities	**2,281,458,274**	**(29.4)**	**3,229,930,487**	**(10.3)**	**3,599,067,938**
Net position	**$39,858,768,499**	**9.2%**	**$36,516,825,339**	**(2.5%)**	**$37,471,267,194**

Condensed Comparative Statements of Changes in Net Position for the Years Ended June 30

	2013	Percentage Change	2012	Percentage Change	2011
Contributions	$3,781,914,113	8.7%	$3,478,920,430	7.5%	$3,235,605,731
Total investment income	4,561,768,383	1,935.5	224,106,719	(96.9)	7,234,539,490
Total additions	8,343,682,496	125.3	3,703,027,149	(64.6)	10,470,145,221
Benefits and refunds	4,981,481,783	7.4	4,638,457,105	7.7	4,304,870,170
Administrative expenses	20,257,553	6.6	19,011,899	6.9	17,792,071
Total deductions	5,001,739,336	7.4	4,657,469,004	7.7	4,322,662,241
Net increase/(decrease) in net position	**3,341,943,160**		**(954,441,855)**		**6,147,482,980**
Net position beginning of year	**36,516,825,339**	**(2.5)**	**37,471,267,194**	**19.6**	**31,323,784,214**
Net position end of year	**$39,858,768,499**	**9.2%**	**$36,516,825,339**	**(2.5%)**	**$37,471,267,194**

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for the fiscal years ended June 30, 2013 and June 30, 2012

Investments

Global financial markets contributed to strong investment returns through the fiscal year ended June 30, 2013. Following the uncertainty and concerns of the prior fiscal year, diminished market volatility and improved fundamentals drove investment performance, led by double-digit gains in global equity markets. All TRS asset classes produced positive returns within this environment. Net of fees, the retirement system's U.S. and international equity portfolios returned 23.3 percent and 13.2 percent, respectively. TRS also enjoyed double-digit investment returns within its private equity, real estate and absolute return portfolios. The TRS investment portfolio posted a positive result, returning 12.8 percent, net of fees, for the fiscal year ended June 30, 2013.

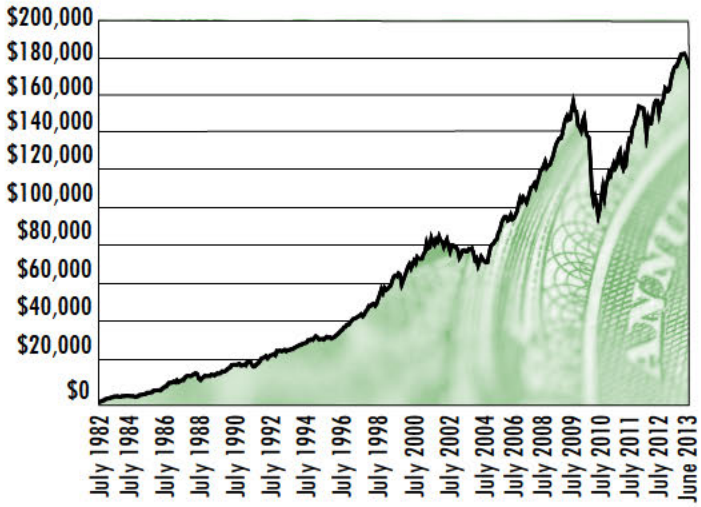
The TRS portfolio remains fully diversified across different asset classes. A number of investment managers are utilized within each asset class to ensure the appropriate mixture across the various investment styles, allowing the portfolio to achieve broad exposure to the market while minimizing overall risk. This broad diversification serves as the best defense against the uncertainty of volatile global markets.

TRS Investment Performance (net of fees)

	1 year	3 years	5 years	10 years
Rate of return	12.8%	12.0%	4.2%	7.2%

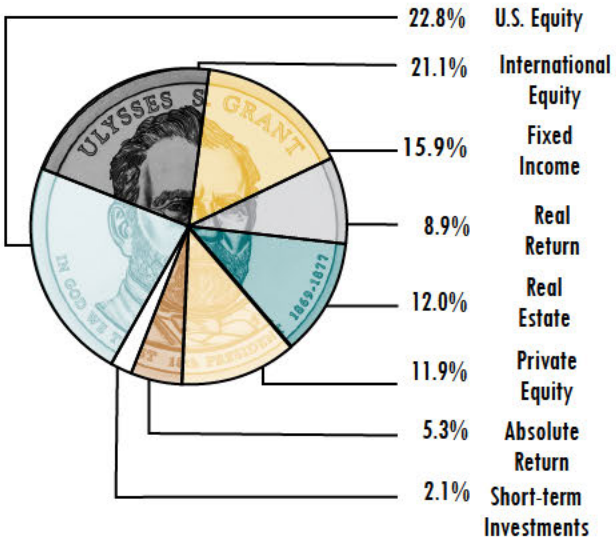
Growth of $10,000

Over the years, TRS's asset allocation has provided consistent overall returns, as represented by the following chart showing the growth of $10,000 since 1982.

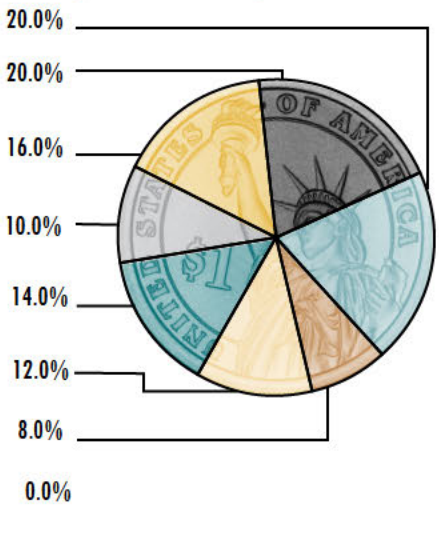


Source: TRS

Fiscal Year 2013 Asset Allocation



Long-Term Target Allocation



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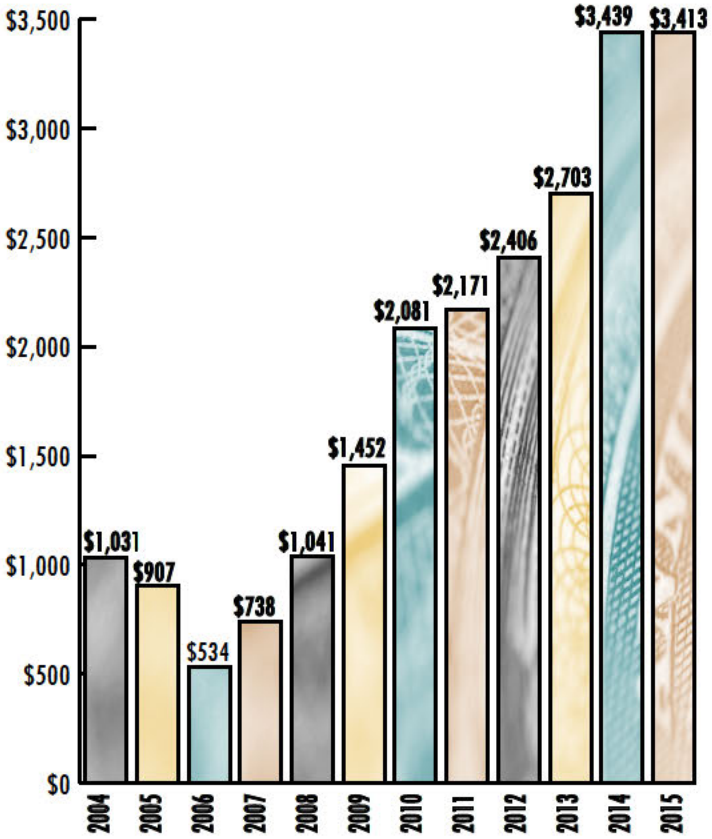
Actuarial

State Funding Requirements

The state's liability for benefits earned by active and inactive teachers and retirees is called the actuarial accrued liability. It is based on the benefit provisions in effect on June 30, 2013 and the retirement system's economic and demographic assumptions. Dividing the accrued liability by assets yields the funded ratio, an indication of how much of the liability is covered by assets. The difference between the accrued liability and assets is the unfunded liability.

The benefit and funding reductions of Public Act 98-0599 are not reflected in the actuarial results presented here. If they are upheld in the expected legal challenge, they become effective after June 30, 2013.

Annual State Appropriations ($ in millions)



Actuarial Valuation ($ thousands)

	Years Ended June 30	
	2013	2012
Total actuarial accrued liability	**$93,886,988**	**$90,024,945**
Less actuarial value of assets	38,155,191	37,945,397
Unfunded liability	**$55,731,797**	**$52,079,548**
Funded ratio	40.6%	42.1%

The actuarial valuation is used to determine the state funding requirements for the coming fiscal year. The objective of the statutory funding plan in effect on June 30, 2013 was to achieve a 90 percent funded ratio by the end of fiscal year 2045. The fiscal year 2015 state contribution certified by the TRS Board of Trustees is actually less than the fiscal year 2014 contribution due to improvements in actuarial methodology and fiscal year 2013 investment performance. Public Act 98-0599 does not contain any provisions for lowering the fiscal year 2015 state contributions below the certified amount shown.

State Funding Requirements Under Current Statutory Funding Plan

	FY15	FY14
Benefit Trust Reserve	$3,411,878,000	$3,437,478,000
Minimum benefit reserve	1,000,000	1,100,000
Total state funding amount	**$3,412,878,000**	**$3,438,578,000**

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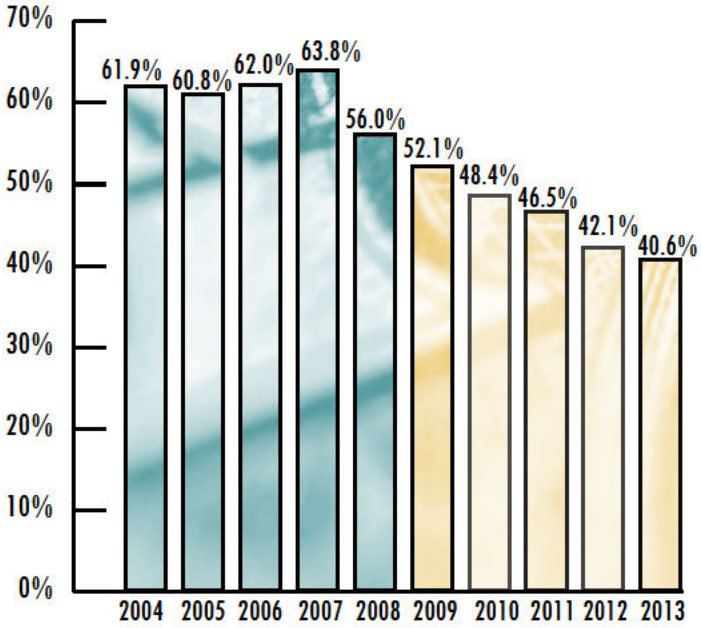
for the fiscal years ended June 30, 2013 and June 30, 2012

Funded Ratio



The funded ratio based on the actuarial value of assets has declined each year since fiscal year 2007. Investment returns were lower than expected in fiscal year 2008, and the world-wide financial collapse occurred in fiscal year 2009. State law was then amended in 2009 to require smoothing of the differences between actual and expected investment returns in order to stabilize state funding requirements. The 2009 losses were gradually phased in over the five-year period that ended June 30, 2013, offset by better than expected investment returns in most subsequent years.

Historical Underfunding

Most of the TRS unfunded liability is due to insufficient state contributions since the system was established in 1939. Financing costs have been the main driver of state contribution requirements.

In 2012, the TRS Board of Trustees resolved to certify state funding requirements under generally accepted actuarial principles and standards. For fiscal year 2015, the Board is certifying three state contribution amounts:

2015 TRS Board Certified State Contribution Amounts	
Funding law in effect on June 30, 2013	$3.413 billion
Minimum actuarial standards (100% funded in 30 years)	$4.062 billion
Keep unfunded liability from growing during fiscal year 2015	$5.092 billion

The funding changes contained in Public Act 98-0599 become effective in fiscal year 2016.

Statistical

Member Statistics

Full and Part-time Active Members

Average age	42
Average years of service	12
Average annual salary	$67,558
Oldest full-time teacher	80

Retired Members

Average age	70
Average service	28
Average annual benefit	$49,800
Oldest retired teacher	109

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Fiscal Year 2013 Highlights

	2013	2012
Active contributing members	160,692	162,217
Inactive noncontributing members	120,325	99,052
Benefit recipients*	108,783	105,447
Total membership	389,800	366,716
Actuarial accrued liability (AAL)	$93,886,988,000	$90,024,945,000
Less actuarial value of assets (smoothed assets)	38,155,191,000	37,945,397,000
Unfunded actuarial accrued liability (UAAL)	$55,731,797,000	$52,079,548,000
Funded ratio (% of AAL covered by assets, based on smoothed assets)	40.6%	42.1%
Total fund investment return, net of fees	12.8%	0.8%
Expenses		
Benefits paid	$4,893,084,234	$4,553,822,073
Refunds paid	88,397,549	84,635,032
Administrative expenses	20,257,553	19,011,899
Total expenses	$5,001,739,336	$4,657,469,004
Income		
Member contributions	$921,422,657	$917,661,328
Employer contributions	157,179,243	154,894,946
State of Illinois contributions	2,703,312,213	2,406,364,156
Total investment income	4,561,768,383	224,106,719
Total income	$8,343,682,496	$3,703,027,149

**Benefit recipients includes retiree, disability, and survivor beneficiaries.*

TRS Receives GFOA Award

The Government Finance Officers Association of the United States and Canada (GFOA) has given an Award for Outstanding Achievement in Popular Annual Financial Reporting to the Teachers' Retirement System of the State of Illinois (TRS) for its Popular Annual Financial Report for the fiscal year ended June 30, 2012. The Award for Outstanding Achievement in Popular Annual Financial Reporting is a prestigious national award recognizing conformance with the highest standards for preparation of state and local government popular financial reports.

In order to receive an Award for Outstanding Achievement in Popular Annual Financial Reporting, a government unit must publish a Popular Annual Financial Report, whose contents conform to program standards of creativity, presentation, understandability, and reader appeal.

An Award for Outstanding Achievement in Popular Annual Financial Reporting is valid for a period of one year only. TRS has received a Popular Award for the last 13 consecutive years. We believe this June 30, 2013 report also conforms to the Popular Annual Financial Reporting requirements, and we are submitting it to GFOA.

This publication is a summary of the Comprehensive Annual Financial Report *for the fiscal years ended June 30, 2013 and June 30, 2012. The comprehensive report is available online, http://trs.illinois.gov.*

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