

TEACHERS' RETIREMENT SYSTEM OF THE STATE OF ILLINOIS

a component unit of the State of Illinois



ANNUAL FINANCIAL REPORT SUMMARY
For the Fiscal Year Ended June 30, 2017

BOARD OF TRUSTEES

As of December 1, 2017



Tony Smith, Ph.D.
President
Superintendent of Education
River Forest



Cinda Klickna
Vice President
Elected
Rochester



Mark Bailey
Elected
Palos Park



Andrew Hirshman
Elected
Oak Park



Matthew Hower
Appointed
Barrington Hills



Marc Levine
Appointed
Wilmette



Laura P. Pearl
Appointed
Glenview



Fred Peronto
Elected
Elmhurst



Larry Pfeiffer
Elected
Carlinville



Daniel Winter
Elected
Decatur



Randall S. Winters
Appointed
Highland Park

EXECUTIVE CABINET

As of December 1, 2017



Standing, left to right:
Director of Communications Dave Urbanek
Chief Technology Officer Thomas Smith
Executive Director Richard W. Ingram
Chief Benefits Officer Carlton W. Lenoir, JD
Chief Investment Officer Stan Rupnik, CFA
Sitting, left to right:
Chief Human Resources Officer Gina Larkin
Chief Legal Counsel Marcilene Dutton, JD
Chief Financial Officer Jana Bergschneider, CPA

Cover: Elgin History Museum, 360 Park Street, Elgin. The museum traces the cultural, commercial and community history of Elgin since its settlement in 1832. Exhibits include Native American artifacts and Elgin National Watch Company memorabilia. Photo credit: Tom Lee



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

<http://www.trsil.org>

877-927-5877 (877) 9-ASK-TRS

December 12, 2017

Dear TRS Members:

We are pleased to present the *Annual Financial Report Summary* for the Teachers' Retirement System of the State of Illinois (TRS) for the fiscal year ended June 30, 2017. This report highlights some Illinois museums that help teachers and students extend learning beyond the classroom.

For 78 years, TRS has consistently fulfilled its statutory mission to deliver the retirement security promised by the State of Illinois to all of its members. During fiscal year 2017:

- TRS distributed \$6.2 billion in retirement, disability and survivor benefits to more than 120,000 annuitants and beneficiaries.
- TRS benefit payments largely stayed in Illinois and created economic activity throughout the state that helped support more than 41,000 jobs. These jobs have an estimated payroll of \$1.6 billion. In all, economic models show that TRS benefits created a \$3.8 billion economic boost to the State of Illinois.
- TRS investments continued to perform well over the short-term and long-term. The TRS portfolio recorded a positive 12.6 percent rate of return, net of fees, during fiscal year 2017, which exceeded the System's investment benchmark of 11.4 percent. The portfolio's 30-year annualized return rate was a positive 8.1 percent, net of fees. This exceeded the 7 percent long-term actuarial return assumption established by the Board.
- TRS successfully handled more than 1 million telephone calls, emails, other correspondence and counseling sessions with members and employers.

TRS maintained its focus on its members in fiscal year 2017 despite the uncertainty that accompanied a prolonged partisan dispute between the executive and legislative branches of state government over the enactment of a state budget. TRS fared better during the dispute than most state government entities because its operations are self-funded and the annual contribution from the state to fund benefits is automatically approved by a continuing appropriation. TRS received its full statutorily-required funding contribution for fiscal year 2017 of \$4.0 billion.

However, the long-term funded status of TRS continues to be among the worst in the nation. At the end of fiscal year 2017, the System's funded ratio was 40.2 percent, on an actuarial basis, with a long-term unfunded liability of \$73.4 billion. The unfunded obligations owed to members have increased by 544 percent since 2000.

For purposes of financial disclosure, the plan fiduciary net position as a percentage of the total pension liability was 39.3 percent with a net pension liability of \$76.4 billion. TRS ranks as the 82nd largest pension fund in the world when measured by assets under management with a net position of \$49.4 billion at the end of fiscal year 2017. If TRS was fully funded, the System would rank within the top 20 pension systems worldwide and among the top 10 U.S. funds.

Information for this report was gathered by TRS staff under the leadership of the Board of Trustees and the executive director and it is the responsibility of TRS management. It is intended to provide complete and reliable information as a basis for making management decisions, to determine our compliance with legal provisions and as a means of determining responsible stewardship of the assets contributed by members, their employers and the State of Illinois.

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 W. Ingram
Executive Director

Jana Bergschneider, CPA
Chief Financial Officer

FINANCIAL HIGHLIGHTS

- The net position of TRS at June 30, 2017 was \$49.4 billion.
- During fiscal year 2017, the net position of TRS increased \$4.1 billion.
- Contributions from members, employers, and the State of Illinois were \$5.1 billion, an increase of \$222 million or 4.6 percent for fiscal year 2017.
- Total net investment income was \$5.5 billion, compared to a \$44 million loss for fiscal year 2016, an increase of \$5.6 billion.
- Benefits and refunds paid to members and annuitants were \$6.4 billion, an increase of \$507 million or 8.5 percent.
- The actuarial accrued liability was \$122.9 billion at June 30, 2017.
- The unfunded actuarial accrued liability was \$73.4 billion at June 30, 2017. The funded ratio was 40.2 percent at June 30, 2017. The unfunded liability and funded ratio are calculated using a

smoothed value of assets, as required under Public Act 96-0043.

- The total pension liability was \$125.8 billion at June 30, 2017.
- The net pension liability was \$76.4 billion at June 30, 2017. The plan fiduciary net position, as a percentage of total pension liability, was 39.3 percent.



Illinois Holocaust Museum and Education Center, 9603 Woods Drive, Skokie. The museum honors the victims who perished during the Holocaust, as well as the courage of survivors.
Photo credit: David Siede/DefinedSpace.com

CONDENSED COMPARATIVE STATEMENTS OF FIDUCIARY NET POSITION AS OF JUNE 30

	2017	Percentage Change	2016
Cash	\$38,331,642	(5.7%)	\$40,637,848
Receivables and prepaid expenses	10,059,591,696	90.5	5,279,564,166
Investments	49,180,275,900	7.8	45,632,926,356
Invested securities lending collateral	3,268,211,165	4.3	3,134,036,175
Capital assets	2,913,530	(19.2)	3,605,993
Total assets	62,549,323,933	15.6	54,090,770,538
Total liabilities	13,173,659,415	49.0	8,839,813,807
Net position restricted for pensions	<u>\$49,375,664,518</u>	9.1%	<u>\$45,250,956,731</u>

CONDENSED COMPARATIVE STATEMENTS OF CHANGES IN FIDUCIARY NET POSITION FOR THE YEARS ENDED JUNE 30

	2017	Percentage Change	2016
Contributions	\$5,064,989,441	4.6%	\$4,842,319,410
Net investment income /(loss)	5,520,453,001	12,617.1	(44,103,178)
Total additions	10,585,442,442	120.6	4,798,216,232
Benefits and refunds	6,438,005,920	8.5	5,931,207,177
Administrative expenses	22,728,735	(1.0)	22,967,917
Total deductions	6,460,734,655	8.5	5,954,175,094
Net increase/(decrease) in net position	4,124,707,787		(1,155,958,862)
Net position restricted for pensions - beginning of year	45,250,956,731	(2.5)	46,406,915,593
Net position restricted for pensions - end of year	<u>\$49,375,664,518</u>	9.1%	<u>\$45,250,956,731</u>

INVESTMENTS

The TRS trust fund is invested by authority of the Illinois Pension Code under the “prudent person rule,” requiring investments to be managed solely in the interest of fund participants and beneficiaries. The TRS Investment Policy guides TRS’s investments. Investment principles include preserving the long-term principal of the trust fund, maximizing total return within prudent risk parameters, and acting in the exclusive interest of TRS members.

The TRS investment portfolio increased \$3.5 billion over the past 12 months, ending with a value of \$49.2 billion on June 30, 2017. The TRS portfolio remains fully diversified across different asset classes. This broad diversification serves as the best defense against the uncertainty of volatile global markets.

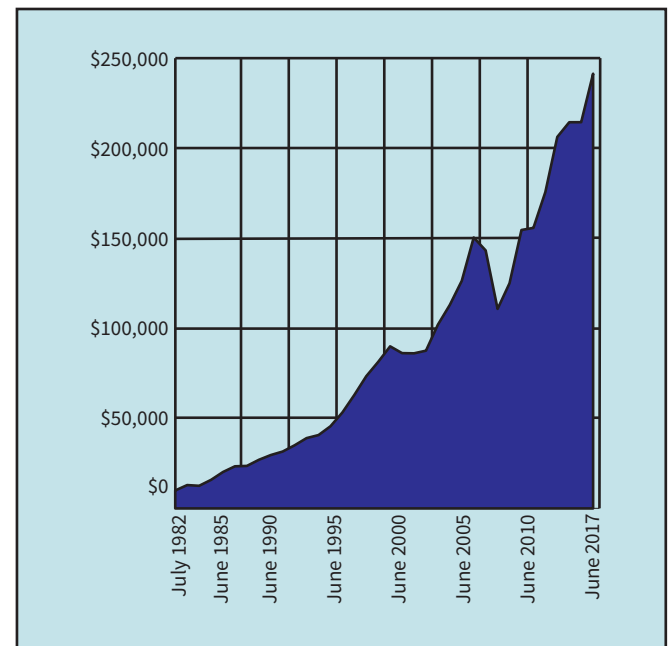
Global financial markets experienced steady growth. Strong corporate earnings and continued accommodative monetary policy, combined with unprecedented low volatility, provided the backdrop for very robust equity returns during the year, with the System’s U.S. and international equities portfolios returning 20.0 percent and 22.0 percent net of fees, respectively. All asset classes produced positive returns, contributing to the overall TRS portfolio posting a return of 12.6 percent, net of fees, for the fiscal year ended June 30, 2017.

TRS INVESTMENT PERFORMANCE (NET OF FEES)

	1 year	3 years	5 years	10 years
Annualized return	12.6%	5.4%	9.2%	4.8%

GROWTH OF \$10,000

TRS’s asset allocation has provided consistent overall returns over the years, as represented by the following chart showing the growth of \$10,000 since July 1, 1982.



STRATEGIC INVESTMENT LISTING ALLOCATION TARGETS VS. TOTAL ASSETS

Asset Class	As of June 30, 2017				As of June 30, 2016	
	Total Fund \$ (Million)	Actual Percent	Interim Target	Long-term Target	Actual Percent	Long-term Target
Domestic equity	\$7,623.4	15.6%	18.0%	18.0%	17.7%	18.0%
International equity	10,172.4	20.9	18.0	18.0	18.8	18.0
Private equity	6,439.7	13.2	12.0	14.0	12.3	14.0
Real estate (opportunistic)	1,518.7	3.1	3.0	4.0	3.3	4.0
Total Equity	25,754.2	52.8	51.0	54.0	52.1	54.0
Real estate (core - value add)	5,572.4	11.4	12.0	11.0	12.2	11.0
Other real assets	1,109.1	2.3	3.0	3.0	2.1	3.0
Total Real Assets	6,681.5	13.7	15.0	14.0	14.3	14.0
Absolute Return	3,069.3	6.3	8.0	8.0	7.3	8.0
Risk Premia/Global Macro	2,804.8	5.7	6.5	8.0	5.7	8.0
Total Diversifying Strategies	5,874.1	12.0	14.5	16.0	13.0	16.0
Global fixed income	9,501.2	19.5	18.5	16.0	18.8	16.0
Short-term	1,008.4	2.0	1.0	-	1.8	0.0
Total Income	10,509.6	21.5	19.5	16.0	20.6	16.0
Pending settlements/expenses	360.9	N/A	N/A	N/A	N/A	N/A
Total TRS Fund	\$49,180.3	100.0%	100.0%	100.0%	100.0%	100.0%

Sources: State Street Bank and Trust and TRS

ACTUARIAL STATE FUNDING

Public Act 88-0593 was enacted in 1994 and first affected state contributions in fiscal year 1996. The law established a 50-year funding plan that includes a 15-year phase-in period. By the end of the funding period in fiscal year 2045, TRS will have a 90 percent funded ratio. A key feature of this act is the “continuing appropriation” language that requires state contributions to be made automatically to TRS, provided state funds are available.

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, 2017 and the retirement system’s economic and demographic assumptions. Dividing the accrued liability by assets yields the funded ratio, which is an indication of how much of the liability is covered by assets. The difference between the accrued liability and assets is the System’s unfunded liability.

For statutory funding and financial reporting, an actuarial valuation is performed annually and measures the total liability for all benefits earned to date. The actuarial

accrued liability is a present value estimate of all the benefits that have been earned to date but not yet paid. The actuarial accrued liability increased \$4.3 billion in fiscal year 2017 to \$122.9 billion at June 30, 2017.

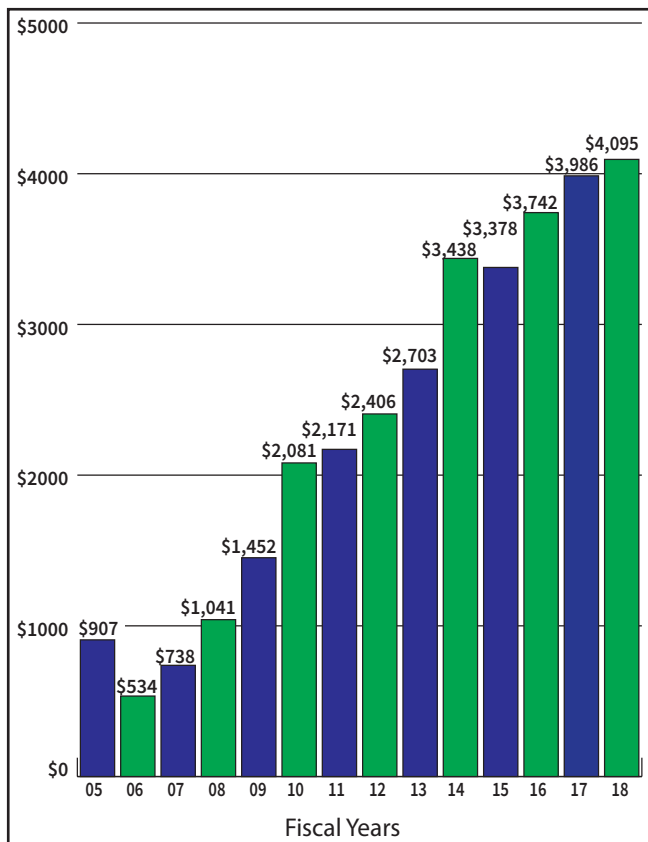
The unfunded liability is the present value of future benefits payable that are not covered by the assets on the valuation date.

ACTUARIAL VALUATION (\$ THOUSANDS)

	Year ended June 30, 2017
Based on actuarial value of assets	
Total actuarial accrued liability	\$122,904,034
Less actuarial value of assets*	49,467,525
Unfunded liability	\$73,436,509
Funded ratio*	40.2%
Based on fair value of assets	
Total actuarial accrued liability	\$122,904,034
Less assets at fair value	49,375,665
Unfunded liability	\$73,528,369
Funded ratio	40.2%

* Five-year prospective smoothing began in fiscal year 2009.

ANNUAL STATE APPROPRIATIONS (\$ IN MILLIONS)



William Fithian Home and Vermilion County Museum, 116 North Gilbert Street, Danville. In Sept. 1858, Abraham Lincoln brought his campaign for the U.S. Senate to Danville and the home of Dr. William Fithian. Following a political rally, Lincoln spoke from a balcony to a crowd gathered outside. The Fithian Home is adjacent to the Vermilion County Museum, which is designed to resemble the old county courthouse built in 1833.

HISTORICAL UNDERFUNDING

Most of the TRS unfunded liability is due to insufficient state contributions accumulated since 1939. Because state contributions annually failed to meet actuarial requirements, the largest share of the annual state contribution is dedicated to paying off the unfunded liability.

Public Act 100-0023, enacted in 2017, makes two changes affecting TRS funding and requires TRS to recertify the fiscal year 2018 state contribution. First, changes in actuarial assumptions made since the fiscal year 2012 actuarial valuation are to be phased in over five-year periods to reduce volatility in the state contribution. Second, the act requires employers to contribute to TRS an amount that covers the employer normal cost on earnings that exceed the governor’s statutory salary. Another 2017 law, Public Act 100-0340, lowers the contribution rate that employers pay for teachers paid from federal funds. The net effect of the two laws was to lower the fiscal year 2018 state contribution by \$470 million, as shown in the table on state contribution requirements.

FISCAL YEAR 2018 & FISCAL YEAR 2019 STATE CONTRIBUTION REQUIREMENTS

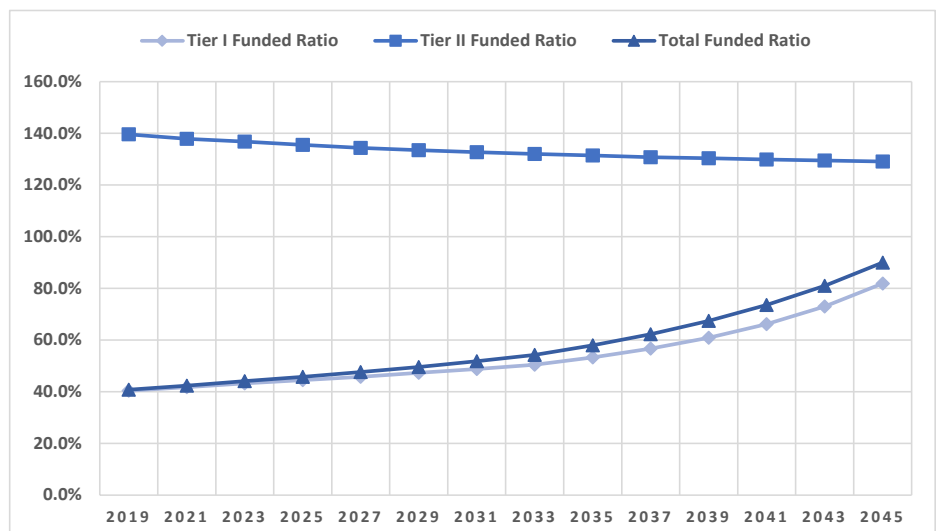
	Fiscal Year 2018 Original Certification	Fiscal Year 2018 Recertification (PA 100-0023 & PA100-0340)	Fiscal Year 2019 Certification
Based on Statutory Funding Plan			
Benefit Trust Reserve	\$4,564,252,674	\$4,094,616,146	\$4,465,578,109
Minimum Annuity Reserve	700,000	700,000	600,000
Total State Contribution	\$4,564,952,674	4,095,316,146	\$4,466,178,109
Based on TRS Board Funding Policy			
Benefit Trust Reserve	\$6,875,583,032	\$6,992,332,528	\$7,370,330,484
Minimum Annuity Reserve	700,000	700,000	600,000
Total State Contribution	\$6,876,283,032	\$6,993,032,528	\$7,370,930,484
Employer Normal Cost Rate	10.10%	10.10%	9.85%

FUNDING ANALYSIS BY TIER

Public Act 96-0889 established a new tier of benefits for teachers who first contribute to TRS or another reciprocal pension system on or after January 1, 2011. Tier 2 teachers have later retirement dates, longer vesting requirements, salary caps for pensions lower than the Social Security wage base, and lower cost of living increases after retirement that are not compounded. On July 1, 2016, the rate for both tiers decreased from 9.4 percent to 9.0 percent.

Under the 50-year funding plan, TRS will attain a funded ratio of 90 percent by 2045. The following chart illustrates how the tiers would be funded if they were operated as separate retirement plans. Tier 2 would be overfunded because member contributions are higher than the cost of Tier 2 benefits. The surplus

Tier 2 assets lower the employer/state contributions required for Tier 1. Tier 2 active members are projected to outnumber Tier 1 active members by 2024. By 2045, Tier 1 would be 82 percent funded and Tier 2 would be 129 percent funded, with the combined plan attaining the 90 percent target funded ratio. In practice, the two tiers are combined for administrative and funding purposes and their assets are commingled.



STATISTICAL

Member Statistics for the Fiscal Year Ended 2017

Full and Part-time Active Members

Full and Part-time Active Members		Retired Members	
Average age	42	Average age	71
Average service	13	Average service	27
Average annual salary	\$71,773	Average annual benefit	\$55,764
Oldest full-time teacher	84	Oldest retired teacher	106

FISCAL YEAR HIGHLIGHTS

As of June 30, 2017

Active contributing members	160,488
Inactive noncontributing members	131,812
Benefit recipients*	120,151
Total membership	412,451

Investment return

Total fund investment return, net of fees	12.6%
---	-------

For funding purposes

Actuarial accrued liability (AAL)	\$122,904,034,268
Less actuarial value of assets (smoothed assets)	49,467,525,209
Unfunded actuarial accrued liability (UAAL)	\$73,436,509,059
Funded ratio (% of AAL covered by assets, based on smoothed assets)	40.2%

For financial disclosure

Total pension liability (TPL)	\$125,773,806,438
Less fiduciary net position (FNP)	49,375,664,518
Net pension liability (NPL)	\$76,398,141,920
FNP as a percentage of TPL	39.3%

Income

Member contributions	\$929,130,165
Employer contributions	149,495,577
State of Illinois contributions	3,986,363,699
Total investment income	5,520,453,001
Total income	\$10,585,442,442

Expenses

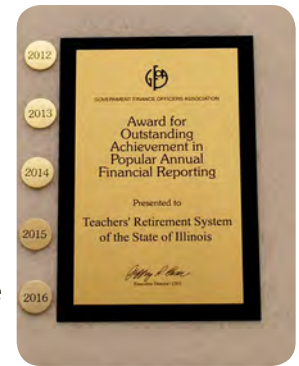
Benefits paid	\$6,152,867,751
Refunds paid	285,138,169
Administrative expenses	22,728,735
Total expenses	\$6,460,734,655

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

This publication is a summary of the *Comprehensive Annual Financial Report* for the fiscal year ended June 30, 2017. The comprehensive report is available online at: <https://www.trsil.org/financial/cafrs/fy2017>.

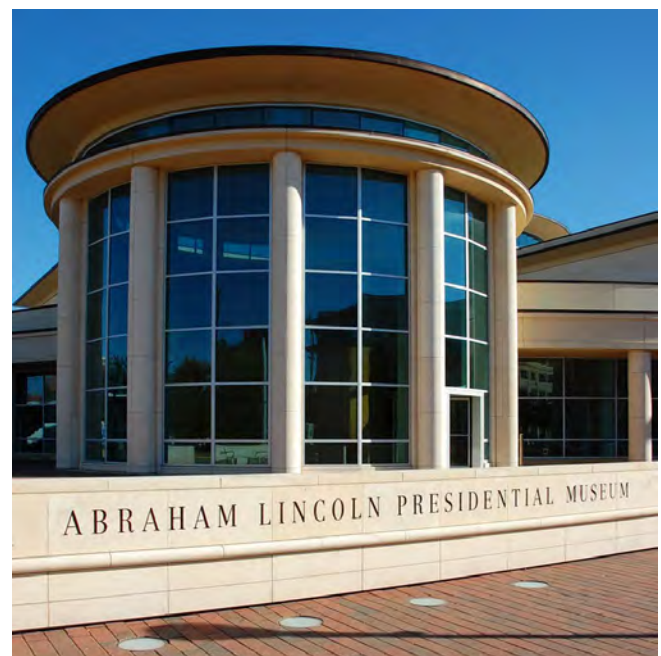
TRS RECEIVES GFOA AWARD

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, 2016. 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 17 consecutive years. We believe this June 30, 2017 report also conforms to the Popular Annual Financial Reporting requirements, and we are submitting it to GFOA.



Abraham Lincoln Presidential Library and Museum, 212 N. 6th St., Springfield. Lincoln's life and presidency through a crucial turning point in history is outlined and examined with modern story-telling methods.