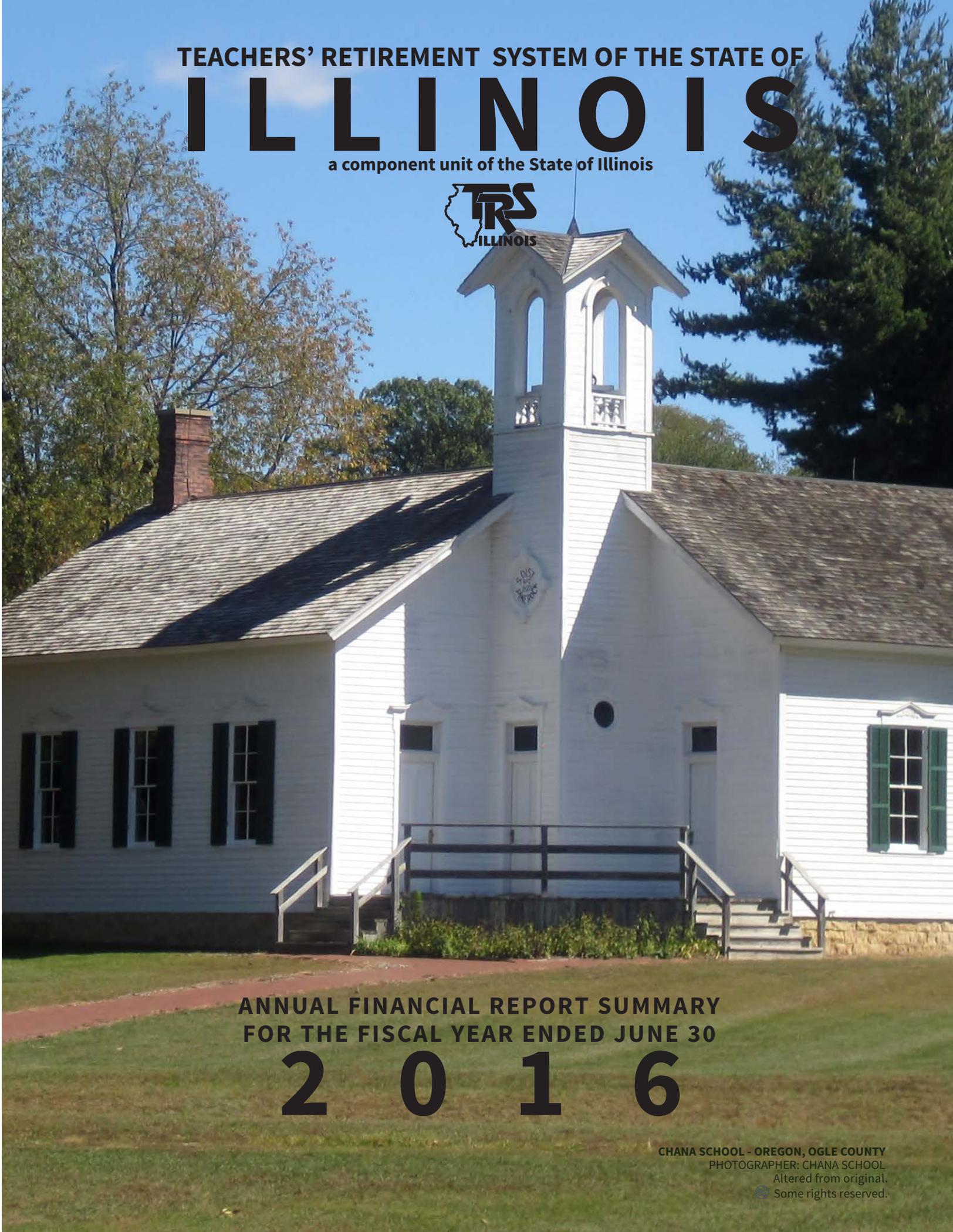


TEACHERS' RETIREMENT SYSTEM OF THE STATE OF
ILLINOIS

a component unit of the State of Illinois



**ANNUAL FINANCIAL REPORT SUMMARY
FOR THE FISCAL YEAR ENDED JUNE 30**

2 0 1 6

CHANA SCHOOL - OREGON, OGLE COUNTY
PHOTOGRAPHER: CHANA SCHOOL

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**BOARD OF TRUSTEES
AS OF DECEMBER 14, 2016**



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Superintendent of Education
River Forest



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Vice President
Elected
Rochester



Mark Bailey
Elected
Palos Park



Ann S. Deters
Appointed
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Rainy Kaplan
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Hoffman Estates



Laura P. Pearl
Appointed
Glenview



Alexander D. Stuart
Appointed
Lake Forest



Daniel Winter
Elected
Decatur



Randall S. Winters
Appointed
Highland Park



**EXECUTIVE CABINET
AS OF DECEMBER 14, 2016**

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*



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

members@trs.illinois.gov | <http://trs.illinois.gov>

(800) 877-7896 | for the hearing impaired: (866) 326-0087

December 14, 2016

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, 2016. A former one-room school house, Chana School in Oregon, Ogle County, Illinois, is the cover for this year's report. TRS honors the legacy of one-room schools in Illinois by highlighting rural school-houses that remain standing in the Prairie State in this year's full *Comprehensive Annual Financial Report* (see pg. 8 bottom). Chana School is currently used as an educational museum.

TRS's mission is to continually deliver the retirement security promised over the last 70 years to our 406,855 members. TRS accomplishes this mission by: putting the best interests of others first, fostering diversity, embracing teamwork, and encouraging continuous improvement at all levels.

- TRS distributed \$5.8 billion in retirement, disability and survivor benefits during fiscal year 2016 to approximately 117,650 annuitants and beneficiaries.
- TRS benefit payments largely stay 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 post steady growth over the long-term, exceeding its 20-year and 30-year benchmarks.

TRS faced its share of challenges that included a lingering uncertainty about state government's financial condition and whether state leaders would be able to make their promised commitment to fund TRS. Due to partisan differences over public policy questions, Illinois government failed to reach a state budget agreement during the fiscal year.

With a net position of \$45.3 billion at the end of fiscal year 2016, TRS ranks as the 80th largest pension fund in the world when measured by assets under management. However, if TRS were fully funded, TRS would rank within the top 25 pension systems worldwide and among the top 10 U.S. funds.

TRS is required by law to publish a report annually with information about the System's financial condition, investment methods and performance, actuarial conclusions that determine financial needs and statistical information about members, school districts, revenues and benefits. This publication summarizes the required report.

Information for this report was gathered by TRS staff under the leadership of the Board of Trustees and the executive director. 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.

A handwritten signature in black ink that reads "Richard W. Ingram".

Richard W. Ingram
Executive Director

A handwritten signature in black ink that reads "Jana Bergschneider".

Jana Bergschneider, CPA
Chief Financial Officer

FINANCIAL HIGHLIGHTS

- The net position of TRS at June 30, 2016 was \$45.3 billion.
- During FY16, the net position of TRS decreased \$1.2 billion.
- Contributions from members, employers, and the State were \$4.8 billion, an increase of \$384 million or 8.6 percent for FY16.
- Total net investment loss was \$44 million, compared to \$1.8 billion in income for FY15, a decrease of \$1.8 billion.
- Benefits and refunds paid to members and annuitants were \$5.9 billion, an increase of \$306 million or 5.4 percent.
- The total actuarial accrued liability was \$118.6 billion at June 30, 2016.
- The unfunded actuarial accrued liability was \$71.4 billion at June 30, 2016. The funded ratio was 39.8 percent at June 30, 2016. 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 \$124.2 billion at June 30, 2016.
- The net pension liability was \$78.9 billion at June 30, 2016. The plan fiduciary net position, as a percentage of total pension liability, was 36.4 percent.

CONDENSED COMPARATIVE STATEMENTS OF FIDUCIARY NET POSITION AS OF JUNE 30

	2016	Percentage Change	2015
Cash	\$40,637,848	(11.1%)	\$45,709,535
Receivables and prepaid expenses	5,279,564,166	(8.1)	5,747,410,436
Investments	45,632,926,356	(1.0)	46,099,664,885
Invested securities lending collateral	3,134,036,175	6.5	2,943,517,231
Capital assets	3,605,993	(8.7)	3,947,730
Total assets	54,090,770,538	(1.4)	54,840,249,817
Total liabilities	8,839,813,807	4.8	8,433,334,224
Net position restricted for pensions	<u>\$45,250,956,731</u>	(2.5%)	<u>\$46,406,915,593</u>

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

	2016	Percentage Change	2015
Contributions	\$4,842,319,410	8.6%	\$4,458,707,579
Net investment (loss)/income	(44,103,178)	(102.5)	1,770,549,533
Total additions	4,798,216,232	(23.0)	6,229,257,112
Benefits and refunds	5,931,207,177	5.4	5,625,037,173
Administrative expenses	22,967,917	5.9	21,686,860
Total deductions	5,954,175,094	5.4	5,646,724,033
Net (decrease)/increase in net position	(1,155,958,862)		582,533,079
Net position restricted for pensions - beginning of year	46,406,915,593	1.3	45,824,382,514
Net position restricted for pensions - end of year	<u>\$45,250,956,731</u>	(2.5%)	<u>\$46,406,915,593</u>

INVESTMENTS

Global financial markets experienced increased volatility for the fiscal year ended June 30, 2016. During the year, continued accommodative monetary policy was offset by mixed economic data, slowing worldwide growth, and political uncertainty (e.g. the U.S. election cycle and the United Kingdom’s vote to exit the European Union). Within this market environment, TRS’s net of fee return was essentially flat led by losses in the public equity portfolios of 1.5 percent and 9.5 percent for U.S. and international equities, respectively. The System’s real estate assets continued to perform very well, again providing double digit returns to the portfolio, while global fixed income and private equity also contributed positive returns. Overall, the TRS investment portfolio posted a modest positive result, returning 0.7 percent, gross of fees, for the fiscal year ended June 30, 2016.

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.

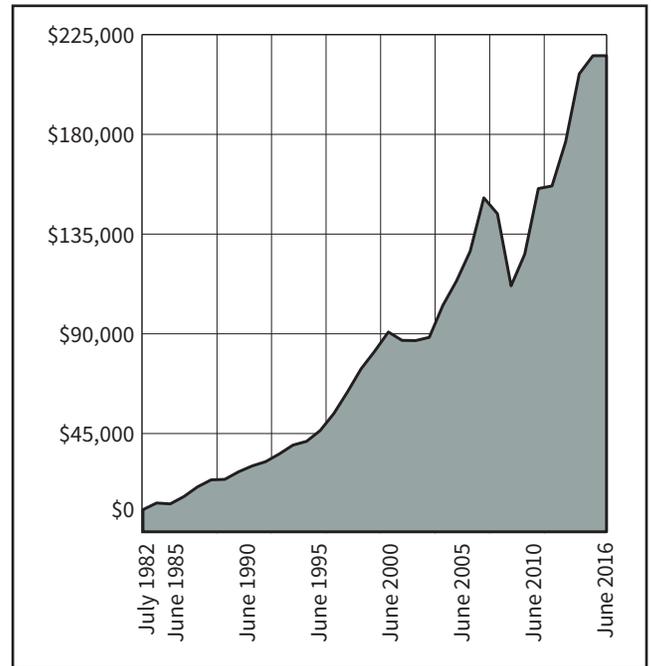
The TRS trust fund is invested by authority of the Illinois Pension Code under the “prudent person rule,” requiring investments to be managed solely in the interest of fund participants and beneficiaries.

TRS INVESTMENT PERFORMANCE (NET OF FEES)

	1 year	3 years	5 years	10 years
Annualized return	0.01%	6.9%	6.8%	5.4%

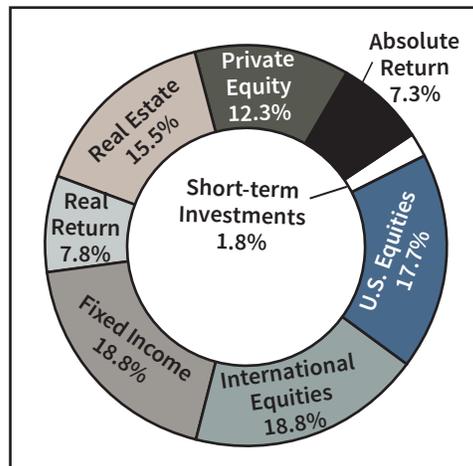
GROWTH OF \$10,000

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.



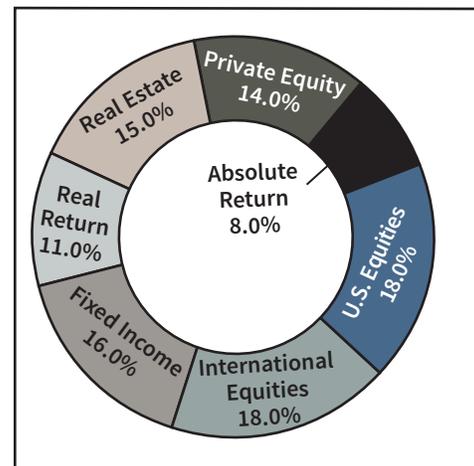
Source: TRS

FISCAL YEAR 2016 ASSET ALLOCATION



Source: TRS

LONG-TERM TARGET ALLOCATION



Source: TRS

ACTUARIAL STATE FUNDING

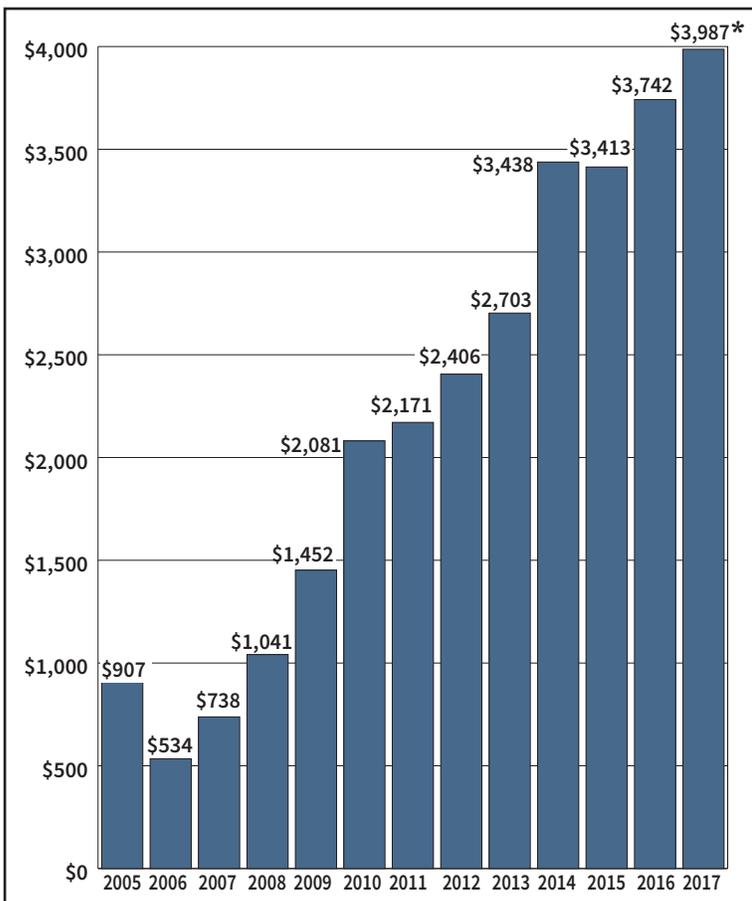
Public Act 88-0593 was enacted in 1994 and first affected state contributions in fiscal year 1996. The law established a 50-year funding plan that includes a 15-year phase-in period. By the end of the funding period in fiscal year 2045, TRS will have a 90 percent funded ratio. A key feature of this act 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, 2016 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 \$10.5 billion in fiscal year 2016 to \$118.6 billion at June 30, 2016.

The actuarial unfunded liability is the present value of future benefits payable that are not covered by the actuarial value of assets as of the valuation date. The actuarial unfunded liability increased \$8.7 billion during fiscal year 2016 to \$71.4 billion at June 30, 2016. The funded ratio reflects the percentage of the actuarial accrued liability covered by the actuarial value of assets. The funded ratio decreased from 42.0 percent on June 30, 2015 to 39.8 percent on June 30, 2016.

ANNUAL STATE APPROPRIATIONS (\$ IN MILLIONS)



* Certified amount

ACTUARIAL VALUATION (\$ THOUSANDS)

Year ended June 30, 2016	
Based on actuarial value of assets	
Total actuarial accrued liability	\$118,629,890
Less actuarial value of assets*	47,222,098
Unfunded liability	<u>\$71,407,792</u>
Funded ratio*	39.8%
Based on fair value of assets	
Total actuarial accrued liability	\$118,629,890
Less assets at fair value	45,250,957
Unfunded liability	<u>\$73,378,933</u>
Funded ratio	38.1%

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

STATE FUNDING REQUIREMENTS UNDER THE CURRENT STATUTORY FUNDING PLAN

Fiscal Year 2018	
Benefit Trust Reserve (excludes federal and school district contributions)	\$4,564,252,674
Minimum benefit reserve	700,000
Total State funding amount	<u>\$4,564,952,674</u>
Employer’s normal cost as a percentage of active member payroll	10.10%

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.

In 2012, the TRS Board of Trustees resolved to certify State funding requirements under generally accepted actuarial principles and standards. For fiscal year 2018, the Board certified two State contribution amounts:

Funding law in effect on June 30, 2015 (90% funded in 50 years with projected unit credit cost method)	\$4.565 billion
Actuarial standard (100% funded in 20 years with layered amortization and entry age normal cost method)	\$6.876 billion

FUNDING ANALYSIS BY TIER

Public Act 96-0889 established a new tier of benefits for teachers who first contribute to TRS on or after January 1, 2011. These Tier II 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. Members in both tiers pay 9 percent of pay towards the cost of their benefits.

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

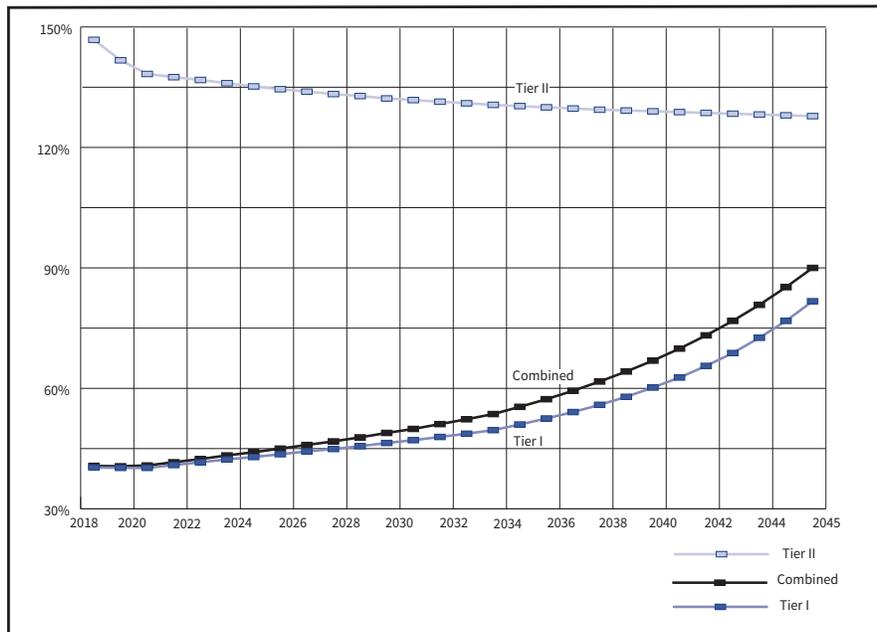
If operated as separate tiers, Tier I would be 82 percent funded by 2045 and Tier II would be 128 percent funded, with the combined plan attaining the 90 percent target funded ratio. The surplus Tier II assets lower the employer/State contributions required for Tier I.

In practice, the two tiers are combined for administrative and funding purposes and their assets are commingled.

STATISTICAL

Full and Part-time Active Members		Retired Members	
Average age	42	Average age	71
Average years of service	13	Average service	28
Average annual salary	\$70,868	Average annual benefit	\$54,252
Oldest full-time teacher	79	Oldest retired teacher	108

FUNDED RATIO BY TIER



FISCAL YEAR HIGHLIGHTS

	As of June 30, 2016
Active contributing members	159,735
Inactive noncontributing members	129,470
Benefit recipients*	117,650
Total membership	406,855
Investment return	
Total fund investment return, net of fees	0.01%
For funding purposes	
Actuarial accrued liability (AAL)	\$118,629,890,305
Less actuarial value of assets (smoothed assets)	47,222,097,809
Unfunded actuarial accrued liability (UAAL)	\$71,407,792,496
Funded ratio (% of AAL covered by assets, based on smoothed assets)	39.8%
For financial disclosure	
Total pension liability (TPL)	\$124,187,003,384
Less fiduciary net position (FNP)	45,250,956,731
Net pension liability (NPL)	\$78,936,046,653
FNP as a percentage of TPL	36.4%
Income	
Member contributions	\$951,809,398
Employer contributions	148,040,767
State of Illinois contributions	3,742,469,245
Total investment income	(44,103,178)
Total income	\$4,798,216,232
Expenses	
Benefits paid	\$5,848,180,208
Refunds paid	83,026,969
Administrative expenses	22,967,917
Total expenses	\$5,954,175,094

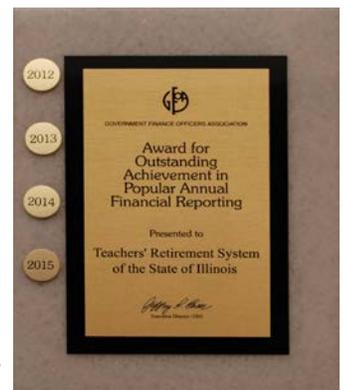
* Benefit recipients includes retiree, disability, and survivor benefit recipients.

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, 2015. 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 16 consecutive years. We believe this June 30, 2016 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 year ended June 30, 2016. The comprehensive report is available online, <http://trs.illinois.gov/pubs/cafr/FY2016/fy16.pdf>.