

**TEACHER RETIREMENT SYSTEM OF TEXAS**

# **Summary Annual Report**

## **2017**




Anita Smith Palmer "The Storm," 2012



## TRS Mission Statement

The mission of the  
Teacher Retirement System of Texas is:

*Improving the retirement security  
of our members by prudently  
investing and managing trust assets  
and delivering benefits  
that make a positive difference in  
their lives.*





## Recognizing Contributions and Dedicated Service of Anita Smith Palmer



*From TRS, with fondness and gratitude, we dedicate the FY 2017 TRS Comprehensive Annual Financial Report to former TRS Trustee, Anita Smith Palmer, featuring her beautiful artwork.*

Anita Smith Palmer of Jacksboro represented retired Texas teachers as a TRS trustee from September 2011 until her death in January of 2017. She was a community volunteer and retired educator with 30 years teaching and administrative experience, including 12 years of service in the Wichita Falls ISD. Anita was also a published author and a truly gifted artist. She was a Special Selected Member of Women Artists of the West, the National Association of Oil and Acrylic Painters, and the American Association of Equine Artists. Anita served as director of the Faith Community Hospital Foundation of Jacksboro and was an active member of The Parish of Jacksboro. Anita was an honorary life member of the National Parent Teacher Association, past district president of the Texas Retired Teachers Association (TRTA), and a former member of TRTA's State Retirement Education Committee. Anita held eight state teaching certifications and served as an adjunct professor at Midwestern State University. She earned bachelor's and master's degrees in education from Southwestern Oklahoma State University.

### Board of Trustees

**R. David Kelly**  
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**Karen Charleston**  
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**Joe Colonna**  
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**Dr. Greg Gibson**  
Schertz

**Christopher Moss**  
Lufkin

**Anita Smith Palmer**  
Jacksboro

*We regret to report the passing of Anita Smith Palmer on January 6, 2017. Thanks to her dedication to the students and public education employees of Texas, her contributions will live on to benefit others for years to come.*



Anita Smith Palmer "Me Too," 2006



Anita Smith Palmer "Barrel Racer," 2000



Brian K. Guthrie  
Executive Director

**TRS investment earnings, combined with contribution increases and benefit changes approved by the 85<sup>th</sup> Texas Legislature, are continuing to enable TRS to provide secure benefits for current and future retirees.**

## From the Executive Director

It is my pleasure to present you with the Teacher Retirement System of Texas' (TRS) *Summary Annual Report* for fiscal year 2017, our 80<sup>th</sup> year of operation. We have prepared this summary of our full *Comprehensive Annual Financial Report* (CAFR) for fiscal year 2017 so you can read about the financial highlights of the past fiscal year. We hope that this CAFR summary will be a convenient resource for those wishing to learn more about TRS developments last year. Our full report is posted on the Publications page of the TRS website.

During the past fiscal year, the System experienced modest growth as membership grew to 1,545,057 participants. The pension trust fund saw positive returns, ending the 2017 fiscal year with a net position of \$147.4 billion compared to \$134.0 billion at the close of the 2016 fiscal year.

TRS investment earnings, combined with contribution increases and benefit changes approved by the 85<sup>th</sup> Texas Legislature, are continuing to enable TRS to provide secure benefits for current and future retirees.

Funding from the 84<sup>th</sup> legislature infused \$768 million into TRS' retiree health benefits program to ensure solvency of the TRS-Care fund through the FY 16-17 Biennium. Even with additional funding, projections for the TRS-Care balance showed a shortfall ranging from \$1.3 to \$1.6 billion for the 2018-19 biennium. The 85<sup>th</sup> Legislature, in regular and special sessions, contributed additional funding to address the current solvency and affordability of TRS-Care. For TRS' active member health benefits program, the TRS Board of Trustees approved a modest increase in premiums and plan design changes for fiscal year 2017. TRS also worked with the 85<sup>th</sup> legislature on options to improve the affordability of TRS-ActiveCare.

During the past year, TRS also continued its program of auditing reports submitted by reporting entities to TRS in response to GASB accounting and American Institute of Certified Public Accounting (AICPA) auditing guidance. TRS Internal Audit staff have tested employer census data for active members. In addition to reviewing elements of this data, TRS auditors are testing eligibility and compensation for accuracy, completeness and compliance with *TRS Laws & Rules*.

The TRS Pension Trust Fund finished the year with an investment net value of \$146.1 billion, an increase of \$12.7 billion after contributions and benefit payouts, from fiscal year 2016. For the 12-month period ending August 31, 2017, the portfolio delivered returns of 12.6 percent. Annual rates of return for five- and 10-year periods ending August 31, 2017 were 9.0 percent and 5.8 percent, respectively.

Thank you for your interest in the latest developments of your retirement system.



# Membership

The Teacher Retirement System of Texas was ranked the sixth largest retirement system in the nation for 2017 and continues to be the largest public retirement system in Texas, serving more than 1.5 million participants.

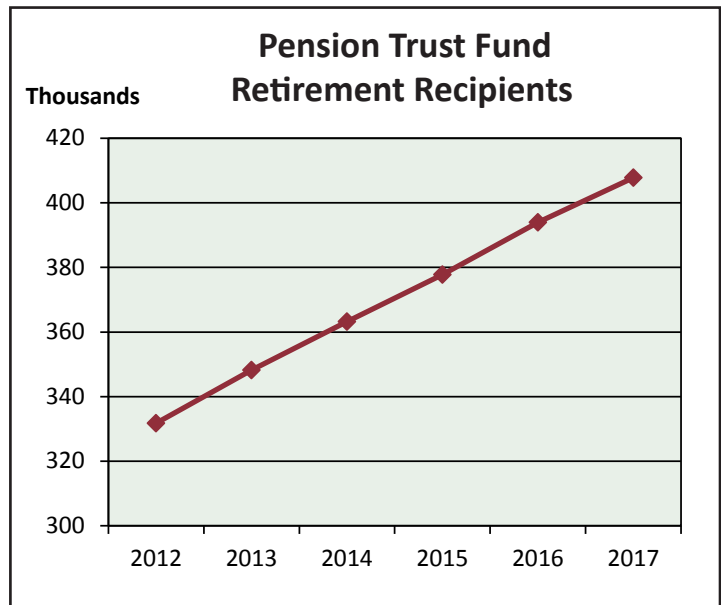
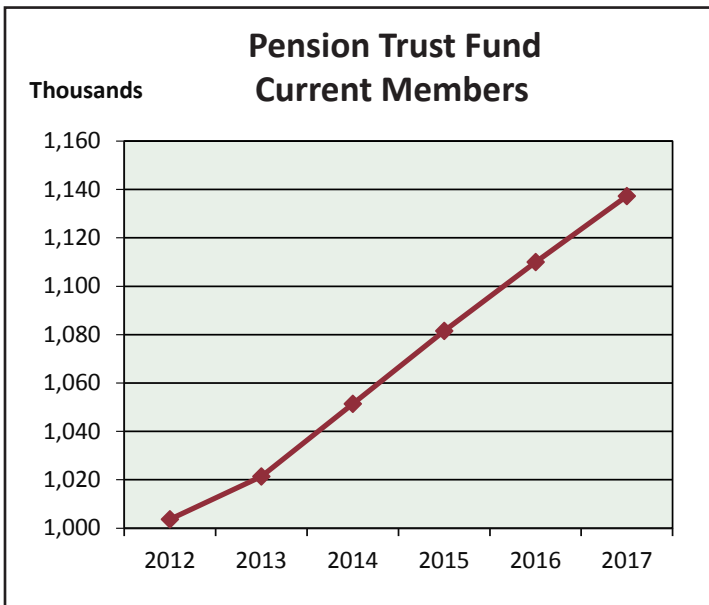
TRS is comprised of current members and retirement recipients. Within these groups are TRS-ActiveCare and TRS-Care participants. The following tables represent TRS Pension Trust Fund membership data for the fiscal year ending Aug. 31, 2017.

TRS membership includes employees and retirees of state-supported educational institutions in Texas. At August 31, 2017, participating employers included the following:

|                                  |              |
|----------------------------------|--------------|
| Public School Districts          | 1,024        |
| Charter Schools                  | 170          |
| Community and Junior Colleges    | 50           |
| Senior Colleges and Universities | 47           |
| Regional Service Centers         | 20           |
| Medical Schools                  | 9            |
| Other Educational Districts      | 4            |
| State Agencies                   | 1            |
| <b>TOTAL</b>                     | <b>1,325</b> |

| Member Categories                  | Year Ended August 31, |                  |
|------------------------------------|-----------------------|------------------|
|                                    | 2017                  | 2016             |
| Current Members:                   |                       |                  |
| Active Contributing                | 864,233               | 847,631          |
| Deferred Retirement Option         | 28                    | 42               |
| Inactive Non-vested                | 174,918               | 167,275          |
| Inactive Vested                    | 98,110                | 95,078           |
| <b>Total Current Members</b>       | <b>1,137,289</b>      | <b>1,110,026</b> |
| Retirement Recipients:             |                       |                  |
| Service                            | 379,765               | 370,761          |
| Disability                         | 11,802                | 9,650            |
| Survivor*                          | 16,201                | 13,503           |
| <b>Total Retirement Recipients</b> | <b>407,768</b>        | <b>393,914</b>   |
| <b>TOTAL MEMBERSHIP</b>            | <b>1,545,057</b>      | <b>1,503,940</b> |

\* Annuities Certain moved from Service to Survivor in 2017.





## Health Benefit Plans

TRS administers retirement and related benefits to employees and beneficiaries of employees of the public, state-supported, educational institutions of Texas. To this end, TRS administers the Texas Public School Retired Employees Group Benefits Program (TRS-Care) and the Texas School Employees Uniform Group Health Coverage Program (TRS-ActiveCare).



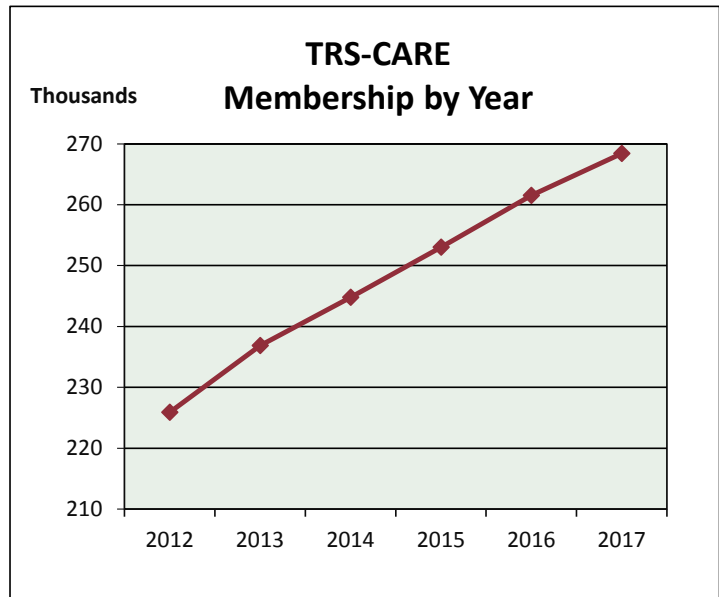
**TRS-Care** provides health care coverage for eligible retirees (and their eligible dependents). The statutory authority for the program is Texas Insurance Code, Title 8, Subtitle H, Chapter 1575, with associated rules found in the Texas Administrative Code, Title 34, Part 3, Chapter 41, Subchapter A. TRS-Care began providing health care coverage on Sept. 1, 1986.

### TEXAS PUBLIC SCHOOL RETIRED EMPLOYEES GROUP INSURANCE PROGRAM (TRS-CARE)

Participation for the Retired Plan is summarized below:

| Member Categories              | 2017           | 2016           |
|--------------------------------|----------------|----------------|
| Retirees                       | 204,987        | 200,231        |
| Surviving Spouses              | 6,672          | 6,351          |
| Surviving Children             | 125            | 106            |
| Dependent Spouses and Children | 56,643         | 54,840         |
| <b>TOTAL</b>                   | <b>268,427</b> | <b>261,528</b> |

There were 1,218 participating employers during fiscal year 2017.





**TRS-ActiveCare** provides health care coverage for eligible employees (and their eligible dependents) of participating public education entities. The statutory authority for the program is Texas Insurance Code, Title 8, Subtitle H, Chapter 1579, with associated rules found in the Texas Administrative Code, Title 34, Part 3, Chapter 41, Subchapter C. TRS-ActiveCare began providing health care coverage on Sept. 1, 2002.

**TEXAS ACTIVE SCHOOL EMPLOYEES UNIFORM GROUP BENEFITS PROGRAM (TRS-ACTIVECARE)**

Participation for the Active Plan is summarized below:

| <b>Member Categories</b> | <b>2017</b>    | <b>2016</b>    |
|--------------------------|----------------|----------------|
| Employees                | 305,234        | 296,523        |
| Dependents               | 187,083        | 187,793        |
| <b>TOTAL</b>             | <b>492,317</b> | <b>484,316</b> |

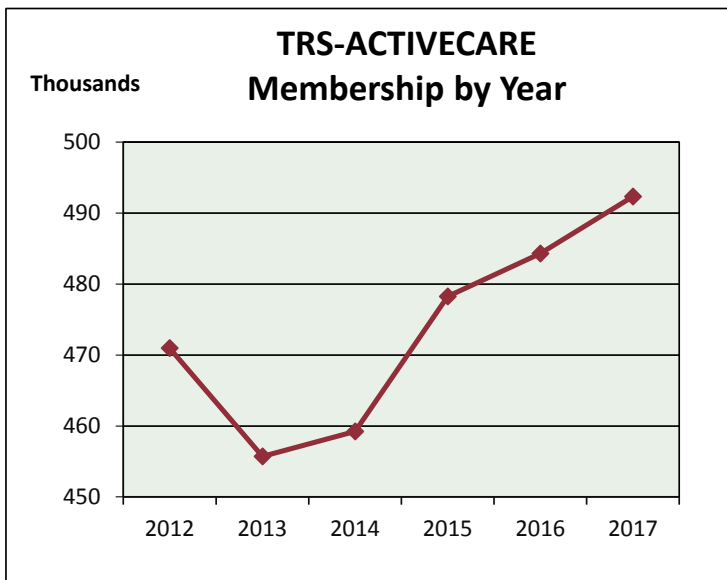
As of August 31, 2017 there were 1,093 participating employers.



Anita Smith Palmer "Lonely," ©2000



Anita Smith Palmer "Boots & Rope," ©2000





## Pension Fund

### Overview of Pension Trust Fund

The Teacher Retirement System of Texas (TRS or System) is a public employee retirement system (PERS) that operates primarily under the provisions of the Texas Constitution, Article XVI, Section 67 and Texas Government Code, Title 8, Subtitle C. The TRS Pension Trust Fund is a multiple-employer, cost-sharing, defined benefit retirement plan with a special funding situation that is a qualified pension trust under Section 401(a) of the Internal Revenue Code.

### Benefit Payments to TRS Retirees and their Beneficiaries

During the past fiscal year, TRS paid pension benefit payments to more than 407,000 retirees and their beneficiaries totaling \$9.9 billion. These benefits were funded from a combination of cumulative investment income, member contributions, and state and employer contributions. Not only does TRS provide great value to its members, but it also benefits Texans by adding significant dollars to the state and local economies.

**The fund ended the 2017 fiscal year with a net position of \$147.4 billion compared to \$134.0 billion at the close of the 2016 fiscal year.**



Anita Smith Palmer "Morning Count," ©2000



Anita Smith Palmer "Roundup," 2001 Founders Award in Painting, American Academy of Equine Art





### Pension Trust Fund

#### Funding Status (Dollars in Millions)

|   | 2017         | 2016         |
|---|--------------|--------------|
| Actuarial Accrued Liability             | \$ 181,753   | \$ 174,239   |
| Actuarial Value of Assets               | \$ (146,282) | \$ (138,786) |
| Unfunded Actuarial<br>Accrued Liability | \$ 35,471    | \$ 35,453    |
| Funded Ratio                            | 80.5%        | 79.7%        |

### Funding Status of TRS Pension Fund

An important measure of the financial strength of a pension fund is the funding status. This is a measure of the assets held by the plan versus the future benefits that will be paid out. If projected future benefits exceed the assets, there is an unfunded liability.

As of August 31, 2017, the System had a funded ratio of 80.5 percent with an Unfunded Actuarial Accrued Liability (UAAL) of \$35.5 billion.

The System earned a return of 12.9 percent on market value, compared to an assumed rate of 8.0 percent. These investment gains more than offset the prior year's deferred investment loss-

es which resulted in a gain on the actuarial value of assets. As a result, the System is now deferring net investment gains of \$1.1 billion.

The period of time necessary to amortize the unfunded liability has decreased from 33.6 years to 32.2 years. Given that current contributions cannot amortize the unfunded liability in less than 31 years, the System does not currently meet the definition for actuarial soundness.

In 2013, the Legislature adopted Senate Bill 1458 that provided a stair-step increase in the member contribution rate from 6.4 percent in FY 2014 to 7.7

percent in FY 2017. The state contribution rate for FY 2017 was 6.8 percent and school districts that do not participate in Social Security pay a 1.5 percent contribution rate to the System. It is estimated that the unfunded liability will increase over the next decade before beginning to decline.

TRS will be conducting an experience study over the coming months to ascertain if the assumption set, including the 8 percent return assumption, continues to be appropriate for the System. The impact of any change to the assumption set has yet to be determined.



## Financial

TRS tracks many complex financial data points throughout each fiscal year. The following information represents financial highlights of budgets and appropriation administration for the fiscal year ending Aug. 31, 2017.

The administrative costs and capital asset outlay for each of the system's funds and programs are controlled by annual budgets approved by the board of trustees.

The Pension Trust Fund receives state contributions for retirement benefits from general revenue appropriations. In fiscal years 2017 and 2016, contributions were made by the State of Texas to the retirement system at the rate of 6.8 percent of the aggregate compensation paid to active retirement system members for each year. Although appropriated by the legislature, administrative expenses and capital outlay for the Pension Trust Fund are paid from the fund's Expense Account, and not from the state's General Fund.

TRS-Care received contributions from the state's General Fund equal to 1.00 percent of salaries paid to public education employees in fiscal year 2017. Administrative expenses for this program are paid from the trust fund.

### Pension Trust Fund Statement of Net Position

(Dollars in Thousands)

|                           | Fiscal Year<br>2017   | Fiscal Year<br>2016   |
|---------------------------|-----------------------|-----------------------|
| Total Assets              | \$ 165,379,342        | \$ 152,925,647        |
| Total Liabilities         | \$ 18,017,420         | \$ 18,917,009         |
| <b>Total Net Position</b> |                       |                       |
| Restricted for Pensions   | <u>\$ 147,361,922</u> | <u>\$ 134,008,638</u> |

### Statement of Changes in Net Position

(Dollars in Thousands)

|                               | Fiscal Year<br>2017  | Fiscal Year<br>2016 |
|-------------------------------|----------------------|---------------------|
| Total Additions               | \$ 23,690,002        | \$ 15,359,304       |
| Total Deductions              | \$ 10,336,717        | \$ 9,889,373        |
| <b>Change in Net Position</b> | <u>\$ 13,353,285</u> | <u>\$ 5,469,931</u> |

The two Enterprise Funds, TRS-ActiveCare and the 403(b) Administrative Program, are supported by fees and receive no appropriations from the state for administrative expenses.

Effective September 1, 1997, legislation authorized TRS to administer a governmental excess benefit arrangement under section 415(m) of the Internal Revenue Code of 1986 (26 U.S.C.). Contributions to this arrangement are made from the state's general revenue appropriations. They yield no net position; therefore, for reporting purposes only the contributions and benefits are reflected in the Statement of Changes in Fiduciary Net Position for the pension fund.



## TRS-Care

### Statement of Net Position

(Dollars in Thousands)

|                           | Fiscal Year<br>2017 | Fiscal Year<br>2016 |
|---------------------------|---------------------|---------------------|
| Total Assets              | \$ 526,398          | \$ 777,316          |
| Total Liabilities         | \$ 126,862          | \$ 135,830          |
| <b>Total Net Position</b> | <b>\$ 399,536</b>   | <b>\$ 641,486</b>   |

### Statement of Changes in Net Position

(Dollars in Thousands)

|                               | Fiscal Year<br>2017 | Fiscal Year<br>2016 |
|-------------------------------|---------------------|---------------------|
| Total Additions               | \$ 1,146,592        | \$ 1,067,835        |
| Total Deductions              | \$ 1,388,542        | \$ 1,399,268        |
| <b>Change in Net Position</b> | <b>\$ (241,950)</b> | <b>\$ (331,433)</b> |

## TRS-ActiveCare

### Statement of Net Position

(Dollars in Thousands)

|                           | Fiscal Year<br>2017 | Fiscal Year<br>2016 |
|---------------------------|---------------------|---------------------|
| Total Assets              | \$ 373,677          | \$ 349,990          |
| Total Liabilities         | \$ 275,872          | \$ 296,439          |
| <b>Total Net Position</b> | <b>\$ 97,805</b>    | <b>\$ 53,551</b>    |

### Statement of Revenues, Expenses, and Changes in Net Position

(Dollars in Thousands)

|                               | Fiscal Year<br>2017 | Fiscal Year<br>2016 |
|-------------------------------|---------------------|---------------------|
| Total Revenue                 | \$ 2,244,998        | \$ 2,076,999        |
| Total Expenses                | \$ 2,200,744        | \$ 2,111,263        |
| <b>Change in Net Position</b> | <b>\$ 44,254</b>    | <b>\$ (34,264)</b>  |



Jerry Albright  
Chief Investment Officer

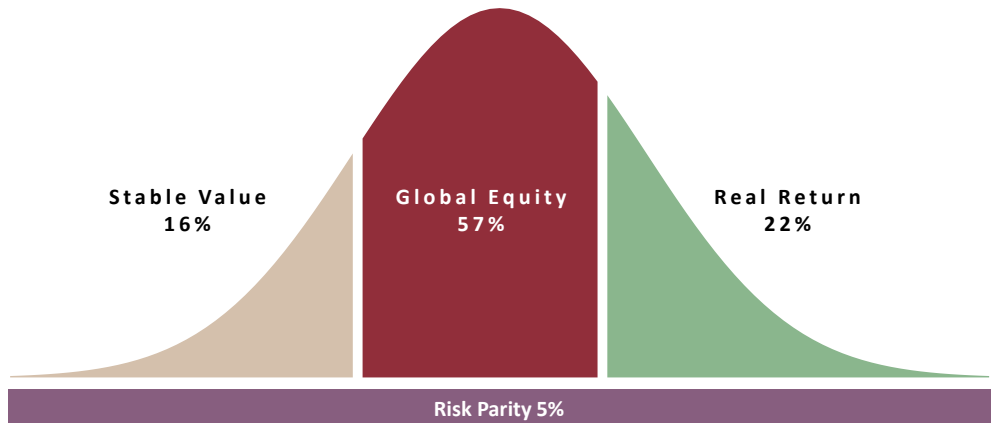
## Investment

### From the Chief Investment Officer

“The TRS Pension Fund is the second largest return-seeking enterprise in our state – only the giant corporation Exxon is larger. TRS is expected to earn approximately 8 percent per year. To place that in context, our portfolio is expected to earn about \$5 million per hour. Not only is our portfolio highly diversified, well managed, carefully monitored, and independently calculated, but the people who work for the fund are passionate about producing results for our members. The result is one of the most secure investment portfolios in our country.”

- Jerry Albright, CIO

Investment performance is calculated using a time-weighted rate of return. Returns are calculated by State Street Bank and Trust Company, the system’s custodian bank, using industry best practices. When comparing returns, consideration should be given to the long-time horizon of TRS investment performance.



**Real Return Portfolio:** TRS’ inflation-sensitive portfolio, designed to generate returns for the Trust in environments where price levels are increasing faster than expected. Allocations within this portfolio include Inflation-linked Bonds, Commodities, Energy and Natural Resources, and Real Assets.

**Stable Value Portfolio:** constructed to generate returns in deflationary environments marked by slowing global growth, providing valuable diversification to the rest of the Trust during periods of market stress. This is accomplished by allocations to Long Treasuries, Cash, Absolute Return assets, and Stable Value Hedge Fund strategies.



**TRS Investment Risks** are diversified over a very broad range of market sectors and securities. TRS' investment strategy is designed to address three different potential market scenarios and has an advantage in each of them by allocating 57 percent to Global Equities, 22 percent to Real Return, 16 percent to Stable Value, and 5 percent to Risk Parity, which has a balanced exposure to all three economic scenarios. This allocation is designed to minimize downside risk while capturing upside performance in any of the three scenarios. This strategy reduces portfolio risk from adverse developments in sectors and issuers experiencing unusual difficulties and offers opportunity to benefit from future markets. Actual allocation percentages as of August 31, 2017 are 58.6 percent to Global Equities, 19.5 percent to Real Return, 16.9 percent to Stable Value, and 5 percent to Risk Parity.

**Risk Parity Portfolio:** seeks equal risk exposure across economic conditions, providing the Trust a portfolio that is balanced across varying environments and outcomes. The TRS Risk Parity portfolio is diversified across allocations to nominal bonds, inflation-linked bonds, commodities, public equities, and credit.

**Global Equity Portfolio:** the Trust's key driver of returns in normal economic conditions, marked by steady growth and stable inflation. This portfolio includes publicly listed equities in the U.S., Developed Non-U.S. and Emerging Markets, as well as allocations to the alternative asset classes of equity-sensitive Directional Hedge Funds and Private Equity.



**Rate of return results for the total fund for period ending Aug. 31, 2017:**

|                 |              |
|-----------------|--------------|
| <b>1 Year</b>   | <b>12.6%</b> |
| <b>3 Years</b>  | <b>6.4%</b>  |
| <b>5 Years</b>  | <b>9.0%</b>  |
| <b>10 Years</b> | <b>5.8%</b>  |

# Notes





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**[www.trs.texas.gov](http://www.trs.texas.gov)**