

# *Judges' Retirement System of Illinois*

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*A Pension Trust Fund  
of the State of Illinois*



*The Illinois Old State Capitol*

## *Judges' Retirement System of Illinois*

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### *On the Cover*

The Old State Capitol is a Greek Revival-style building that served as Illinois' fifth statehouse, the first to be located in Springfield. The building was the seat of state government and a center of Illinois political life from 1839 to 1876. During the dramatic years leading up to the Civil War, the building had an important role in the political struggle between Stephen Douglas and Abraham Lincoln.

Lincoln visited the building frequently as both a lawyer and politician, serving in the building during his last term in the Illinois House of Representatives and delivering the famous 1858 "House Divided" speech in Representatives Hall. The building was also the scene of the assassinated President's final laying-in-state on May 3-4, 1865.

The Capitol was completely reconstructed in the 1960s. In 1961 the building was designated a National Historic Landmark and in 1966 was listed on the National Register of Historic Places.

### *Fiscal Year 2012 Highlights*

|                           |   |
|---------------------------|---|
| 983                       | Total Membership  |
| 968                       | Active Contributing Members                               |
| \$577,976,367             | Net Assets Held in Trust for Pension Benefits, fair value |
| <i>Contributions</i>      |   |
| \$16,444,796              | Participants  |
| \$63,644,099              | Employer  |
| \$(69,096)                | Investment (Loss)   |
| <i>Benefit Recipients</i> |   |
| 725                       | Retirement Annuities                                      |
| 331                       | Survivors' Annuities                                      |
| \$106,653,095             | Benefits Paid   |
| \$2,021,715,796           | Actuarial Accrued Liability                               |
| \$601,219,999             | Actuarial Value of Assets                                 |
| \$1,420,495,797           | Unfunded Actuarial Liability                              |
| 29.7%                     | Funded Ratio  |

### *Mission Statement*

To establish an efficient method of permitting retirement, without hardship or prejudice, of judges who are aged or otherwise incapacitated, by enabling them to accumulate reserves for themselves and their dependents for old age, disability, death and termination of employment.

# JUDGES' RETIREMENT SYSTEM OF ILLINOIS

A Pension Trust Fund of the State of Illinois

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COMPREHENSIVE ANNUAL FINANCIAL REPORT  
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

JUDGES' RETIREMENT SYSTEM OF ILLINOIS

2101 South Veterans Parkway  
P. O. Box 19255  
Springfield, Illinois 62794-9255

Prepared by the Accounting Division

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# INTRODUCTORY SECTION

# LETTER OF TRANSMITTAL



- State Employees' Retirement System of Illinois
- General Assembly Retirement System
- Judges' Retirement System of Illinois

2101 South Veterans Parkway, P. O. Box 19255, Springfield, IL 62794-9255 217-785-7444

January 9, 2013

The Board of Trustees and Members  
Judges' Retirement System of Illinois  
Springfield, IL 62794

Dear Board of Trustees and Members:

The comprehensive annual financial report (CAFR) of the Judges' Retirement System of Illinois (System) as of and for the fiscal year ended June 30, 2012 is hereby submitted. Responsibility for both the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with the System.

To the best of our knowledge and belief, the enclosed data are accurate in all material respects and are reported in a manner designed to present fairly the financial position and results of operations of the System. All disclosures necessary to enable the reader to gain an understanding of the System's financial activities have been included.

Generally accepted accounting principles require that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The System's MD&A can be found immediately following the report of the independent auditors.

The report consists of six sections:

1. The Introductory Section contains this letter of transmittal, the identification of the administrative organization and the Certificate of Achievement for Excellence in Financial Reporting;
2. The Financial Section contains management's discussion and analysis, the report of the Independent Auditors, the financial statements of the System and certain required and other supplementary financial information;
3. The Investment Section contains a report on investment activity, investment policies, investment results and various investment schedules;

4. The Actuarial Section contains the Actuary's Certification Letter and the results of the annual actuarial valuation;

5. The Statistical Section contains significant statistical data; and

6. The Plan Summary and Legislative Section contains the System's plan provisions and current legislative changes.

Generally accepted accounting principles require that the financial reporting entity include:

1. the primary government;
2. organizations for which the primary government is financially accountable; and
3. other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.

Based on the criteria of the Governmental Accounting Standards Board Statement No. 14, there are no other state agencies, boards or commissions, or other organizations required to be combined with the System, however, the System is considered to be part of the State of Illinois financial reporting entity, and is to be combined and included in the State of Illinois' comprehensive annual financial report.

Although the Judges' Retirement System, State Employees' Retirement System and General Assembly Retirement System share a common administration, they are separate entities for legal and financial reporting purposes. Therefore, the financial statements of the Judges' Retirement System do not include plan net asset information nor the changes in plan net assets of the State Employees' Retirement System or General Assembly Retirement System.

## PLAN HISTORY & SERVICES PROVIDED

The Judges' Retirement System was established as a single-employer public employee retirement system (PERS) by state statute on July 1, 1941. As of June 30, 1942, the end of the System's first fiscal year of operations, there were a total of 260 participants and the plan net assets valued at cost amounted to approximately \$84,000. The fair value of plan net assets at the end of fiscal year 2012 amounted to approximately \$578.0 million, and there were 968 active participants.

The mission of the System as prescribed by state statute is to "establish an efficient method of permitting retirement, without hardship or prejudice, of judges who are aged or otherwise incapacitated, by enabling them to accumulate reserves for themselves and their dependents for old age, disability, death, and termination of employment."

## INVESTMENTS

The System's investments are managed by the Illinois State Board of Investment (ISBI) pursuant to Chapter 40, Article 5/22A of the Illinois Compiled Statutes, using the "prudent person rule".

This rule states that fiduciaries shall discharge their duties solely in the interest of the fund participants and beneficiaries and with the degree of diligence, care and skill which prudent men and women would ordinarily exercise under similar circumstances in a like position.

The ISBI maintains a wide diversification of investments within this fund which is intended to reduce overall risk and increase returns. As further detailed in the Investment Section, the ISBI Commingled Fund earned 0.1%, net of expenses, for the fiscal year ended June 30, 2012.

## FUNDING

Funding is the process of specifically allocating monies for current and future use. Proper funding includes an actuarial review of the fund balances to ensure that funds will be available for current and future benefit payments. The greater the level of funding, the larger the ratio of accumulated assets to the actuarial accrued liability and the greater the level of investment potential.

The funding plan for the System, enacted in 1994 with subsequent modifications, requires that state contributions be paid to the System so that by the end of fiscal year 2045, the ratio of the actuarial value of assets to the actuarial accrued liability will be 90%. For fiscal years 2011 through 2045, the required state contributions are to be computed as a level percentage of participant payroll.

For fiscal years up through 2010, the required state contributions, except for fiscal years 2006 and 2007, were to be increased incrementally as a percentage of the participant payroll so that by fiscal year 2011 the state is contributing at the required level contribution rate to achieve the financing objective by the end of fiscal year 2045. For fiscal years 2012 and 2011, the statutorily required state contributions were \$63,628,000 and \$62,377,000, respectively. The total amount of contributions received from the state for fiscal years 2012 and 2011 was \$63,628,000 and \$62,428,783, respectively.

The funding legislation also provides for the establishment of a continuing appropriation of the required state contributions to the System. This has, in effect, removed the appropriation of these funds from the annual budgetary process.

The actuarial determined liability of the System using the projected unit credit actuarial cost method at June 30, 2012, amounted to \$2,021.7 million. The actuarial value of assets amounted to \$601.2 million resulting in an unfunded accrued actuarial liability of \$1,420.5 million as of the same date. A detailed discussion of funding is provided in the Actuarial Section of this report.

## ACCOUNTING SYSTEM & INTERNAL CONTROL

This report has been prepared to conform with the principles of governmental accounting and reporting pronounced by the Governmental Accounting Standards Board and the American Institute of Certified Public Accountants.

The accrual basis of accounting is used to record the financial transactions and activities of the System. Revenues are recognized in the accounting period in which they are earned, without regard to the date of collection, and expenses are recognized when the corresponding liabilities are incurred, regardless of when payment is made.

# LETTER OF TRANSMITTAL

The System also uses the State of Illinois, Statewide Accounting Management System (SAMS) as a basis for the preparation of the financial statements.

In developing the System's accounting system, consideration is given to the adequacy of internal accounting controls. These controls are designed to provide reasonable assurance regarding the safekeeping of assets and the reliability of financial records. The concept of reasonable assurance recognizes that the cost of a control should not exceed the benefits likely to be derived and that the valuation of costs and benefits requires estimates and judgements by management. Constant effort is directed by the System at improving this level to assure the participants of a financially sound retirement system.

## PROFESSIONAL SERVICES

Independent consultants are retained by the Board of Trustees to perform professional services that are essential to the effective and efficient operation of the System. Actuarial services are provided by Gabriel, Roeder, Smith & Company, Chicago, Illinois. The System's investment function is managed by the Illinois State Board of Investment.

The annual financial audit of the System was conducted by the accounting firm of BKD, LLP, under the direction of the Auditor General of the State of Illinois. In addition to the annual financial audit, a compliance attestation examination is also performed by the auditors.

The purpose of the compliance attestation examination was to determine whether the System obligated, expended, received and used public funds of the state in accordance with the purpose for which such funds have been authorized by law.

## CERTIFICATE OF ACHIEVEMENT

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the Judges' Retirement System of Illinois for its comprehensive annual financial report for the fiscal year ended June 30, 2011.

The Certificate of Achievement is a prestigious national award recognizing excellence in the preparation of state and local government financial reports. To be awarded a Certificate of Achievement, a governmental unit must publish an easily readable and efficiently organized CAFR, whose contents meet or

exceed program standards. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. The Judges' Retirement System of Illinois has received a Certificate of Achievement for the past twenty-three consecutive years (fiscal years ended June 30, 1989 through June 30, 2011).

We believe our current report continues to conform to the Certificate of Achievement program requirements, and we are submitting it to the GFOA to determine its eligibility for another certificate.

## ACKNOWLEDGMENTS & COMMENTS

The preparation of this report reflects the combined efforts of the System's staff under the direction of the Board of Trustees. It is intended to provide complete and reliable information as a basis for making management decisions, as a means of determining compliance with legal provisions, and for determining responsible stewardship for the assets contributed by the members in the State of Illinois.

On behalf of the Board of Trustees, we would like to express our appreciation to the staff and professional consultants who worked so effectively to ensure the successful operation of the System.

Respectfully submitted,

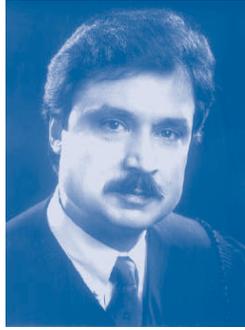


Timothy B. Blair  
Executive Secretary

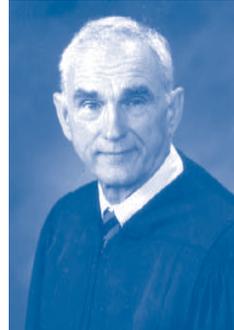


David M. Richter, CPA  
Accounting Division

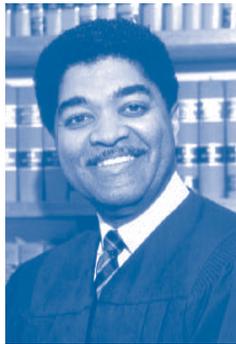
## ADMINISTRATION



JUSTICE  
Thomas E. Hoffman  
Chairman



JUSTICE  
John J. Bowman  
Vice-Chairman



CHIEF JUDGE  
Timothy C. Evans

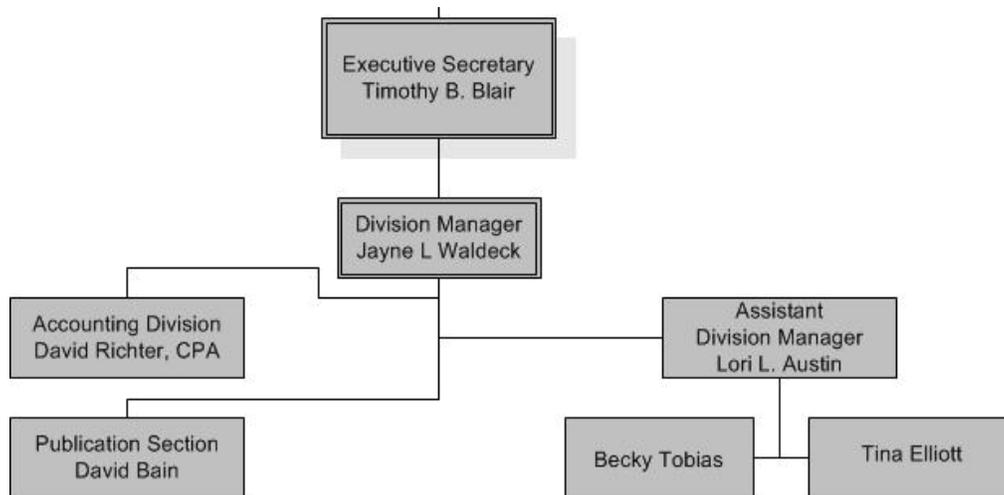


CHIEF JUSTICE  
Thomas L. Kilbride



STATE TREASURER  
Dan Rutherford

## BOARD OF TRUSTEES



### *Advisors, Auditors, and Administrators*

|                    |   |
|--------------------|---|
| Consulting Actuary | Gabriel, Roeder, Smith & Company<br>Chicago Illinois    |
| External Auditor   | BKD,LLP<br>Decatur, Illinois                            |
| Investments        | Illinois State Board of Investment<br>Chicago, Illinois |

Certificate of  
Achievement  
for Excellence  
in Financial  
Reporting

Presented to

Judges' Retirement System  
of Illinois

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
June 30, 2011

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



*Christopher P. Moynell*

President

*Jeffrey R. Emery*

Executive Director

# FINANCIAL SECTION



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P.O. Box 1580  
Decatur, IL 62525-1580  
217.429.2411 Fax 217.429.6109 www.bkd.com

## Independent Auditors' Report

The Honorable William G. Holland  
Auditor General  
State of Illinois

and

Board of Trustees  
Judges' Retirement System of the State of Illinois  
Springfield, Illinois

As Special Assistant Auditors for the Auditor General, we have audited the accompanying financial statements of the Judges' Retirement System of the State of Illinois (System), as of and for the years ended June 30, 2012 and 2011 as listed in the table of contents. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the 2012 and 2011 financial statements of the Illinois State Board of Investment, an internal investment pool of the State of Illinois, which statements represent 96 percent, 97 percent, and (.19) percent, respectively in 2012, and 96 percent, 97 percent, and 57 percent, respectively, in 2011 of total assets, net assets held in trust for pension benefits, and total additions of the System. Those financial statement were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Illinois State Board of Investment is based solely on the report of the other auditors.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the plan net assets of the System as of June 30, 2012 and 2011, and the changes in its plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued, under separate cover, our report dated January 9, 2013 on our consideration of the System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, the schedule of funding progress, the schedule of employer contributions and notes to required supplementary information listed in the table of contents be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board 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 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 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.

Our audits were conducted for the purpose of forming an opinion on the System's basic financial statements as a whole. The supplementary financial information in the financial section and the accompanying introductory, investment, actuarial, statistical and plan summary and legislative sections, as listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The supplementary financial information as noted in the table of contents has been subjected to the auditing procedures applied in the audits of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America by us and other auditors. In our opinion, based on our audits, the procedures performed as described previously, and the report of the other auditors, the supplementary financial information as noted in the table of contents is fairly stated in all material respects in relation to the basic financial statements as a whole. The introductory, investment, actuarial, statistical and plan summary and legislative sections have not been subjected to the auditing procedures applied in the audits of the basic financial statements and, accordingly, we express no opinion on them.

BKD, LLP

January 9, 2013

*This financial report is designed to provide a general overview of the Judges' Retirement System's finances for all those with an interest in the System's finances.*

This section presents management's discussion and analysis of the financial position and performance of the Judges' Retirement System of Illinois (System) for the years ended June 30, 2012 and 2011. It is presented as a narrative overview and analysis. Readers are encouraged to consider the information presented here in conjunction with the Letter of Transmittal included in the Introductory Section, of the Comprehensive Annual Financial Report.

The System is a defined benefit, single-employer public employee retirement system. It provides services to 968 active judges and 1,056 benefit recipients. Throughout this discussion and analysis units of measure (i.e. billions, millions, thousands) are approximate, being rounded up or down to the nearest tenth of the respective unit value.

## OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the System's financial reporting which is comprised of the following components:

**1. Basic Financial Statements.** For the fiscal years ended June 30, 2012 and 2011, basic financial statements are presented for the System. This information presents the net assets held in trust for pension benefits for the System as of June 30, 2012 and 2011. This financial information also summarizes the changes in net assets held in trust for pension benefits for the years then ended.

**2. Notes to the Financial Statements.** The notes to the financial statements provide additional informa-

tion that is essential to achieve a full understanding of the data provided in the basic financial statements.

**3. Required Supplementary Information.** The required supplementary information consists of two schedules and related notes concerning actuarial information, funded status and required contributions for the System.

**4. Other Supplementary Schedules.** Other supplementary schedules include more detailed information pertaining to the System, including schedules of revenues by source, cash receipts and disbursements, and payments to consultants.

## FINANCIAL HIGHLIGHTS

- The System's net assets decreased by \$28.0 million and increased by \$82.7 million during fiscal years 2012 and 2011, respectively. These changes were primarily due to a \$28.7 million decrease in investments (excluding securities lending collateral) offset by a \$0.7 million increase in cash and receivables during fiscal year 2012 and a \$1.4 million increase in cash and a \$81.3 million increase in investments (excluding securities lending collateral) during fiscal year 2011.
- The System was actuarially funded at 29.7% as of June 30, 2012 a decrease from 31.5% as of June 30, 2011. For fiscal years 2012 and 2011, the actuarial value of assets equals the fair value of assets adjusted for any actuarial gains or losses from investment return incurred in the fiscal year recognized in equal amounts over the five year period following that fiscal year.
- The overall rate of return for the Illinois State Board of Investment (ISBI) Commingled Fund was 0.1% for fiscal year 2012 compared to 21.7% for fiscal year 2011.

*The condensed Statements of Plan Net Assets reflect the resources available to pay benefits to members, including retirees and beneficiaries, at the end of the years reported. A summary of the System's Plan Net Assets is presented below.*

|                              | Condensed Statements of Plan Net Assets<br>(in thousands) |              |              | Increase/(Decrease)<br>from |                 |
|------------------------------|---|--------------|--------------|-----------------------------|-----------------|
|                              | As of June 30,  |              |              | 2011 to<br>2012             | 2010 to<br>2011 |
|                              | 2012  | 2011         | 2010         |                             |                 |
| Cash                         | \$ 10,690.6   | \$ 18,015.8  | \$ 16,644.5  | \$ (7,325.2)                | \$ 1,371.3      |
| Receivables                  | 8,211.6   | 221.3        | 261.5        | 7,990.3                     | (40.2)          |
| Investments, at fair value * | 565,084.3   | 595,055.6    | 512,705.5    | (29,971.3)                  | 82,350.1        |
| Equipment, net               | 9.3   | 3.3          | 3.9          | 6.0                         | (0.6)           |
| Total assets                 | 583,995.8   | 613,296.0    | 529,615.4    | (29,300.2)                  | 83,680.6        |
| Liabilities*                 | 6,019.4   | 7,335.8      | 6,339.2      | (1,316.4)                   | 996.6           |
| Total plan net assets        | \$ 577,976.4  | \$ 605,960.2 | \$ 523,276.2 | \$ (27,983.8)               | \$ 82,684.0     |

\* Including securities lending collateral

## ADDITIONS TO PLAN NET ASSETS

Additions to Plan Net Assets include employer and participant contributions and net income from investment activities. Participant contributions were \$16.4 million and \$16.7 million for the years ended June 30, 2012 and 2011, respectively. Participant contribution rates are set by statute as a percentage of gross salary. Employer contributions increased to \$63.6 million in 2012 from \$62.7 million in 2011. This increase was the result of the State's funding plan.

## DEDUCTIONS FROM PLAN NET ASSETS

Deductions from Plan Net Assets are primarily benefit payments. During 2012 and 2011, the System paid out \$107.2 million and \$101.4 million, respectively, in benefits and refunds, an increase of approximately 5.8%. These higher payments were mainly due to an increase in the number of annuitants as well as a 3% automatic annuity increase paid each year. The administrative costs of the System represented less than 1% of total deductions in both 2012 and 2011.

## FUNDED RATIO

The funded ratio of the plan measures the ratio of the actuarial value of assets against actuarially determined liabilities and is one indicator of the fiscal strength of a pension fund's ability to meet obligations to its members. An annual actuarial valuation is required by statute. The most recent available valuation showed the funded status of the System on June 30, 2012 decreased to 29.7% from 31.5% on June 30, 2011. The major reason for the decline was the lingering effect of prior investment performance on the smoothed market value of assets. The amount by which actuarially determined liabilities exceeded the actuarial value of assets was \$1,420.5 million on June 30, 2012 compared to \$1,337.9 million on June 30, 2011.

## INVESTMENTS

Investments of the System are combined in a commingled investment pool with the State Employees'

Retirement System and the General Assembly Retirement System. Each system owns an equity position in the pool and receives proportionate investment income from the pool in accordance with respective ownership percentage. Investment gains or losses are reported in the Statement of Changes in Plan Net Assets of each retirement system.

The net investment income of the total ISBI Commingled Fund was approximately \$5.0 million during fiscal year 2012, versus \$2.0 billion during fiscal year 2011, resulting in returns of 0.1% and 21.7%, respectively. The actual rate of return earned by the System will vary from the return earned on the total ISBI Commingled Fund as a result of overall market conditions at the time of additional investments in or withdrawals from the ISBI Commingled Fund. For the three, five, and ten year period ended June 30, 2012, the ISBI Commingled Fund earned a compounded rate of return of positive 10.0%, negative 0.1%, and positive 5.2%, respectively.

The ISBI is exposed to general market risk. This general market risk is reflected in asset valuations fluctuating with market volatility. Any impact from market volatility on the ISBI's investment portfolio depends in large measure on how deep the market downturn is, how long it lasts, and how it fits within fiscal year reporting periods. The resulting market risk and associated realized and unrealized gains and losses could significantly impact the ISBI's financial condition.

*Questions concerning any of the information provided in this report or requests for additional financial information should be sent to the Judges' Retirement System of Illinois, Accounting Division, 2101 S. Veterans Parkway, P. O. Box 19255, Springfield, Illinois 62794*

*The condensed Statements of Changes in Plan Net Assets reflect the changes in the resources available to pay benefits to members, including retirees and beneficiaries.*

|  | For the Year Ended June 30, |                   |                   | Increase/(Decrease)<br>from |                    |
|--|-----------------------------|-------------------|-------------------|-----------------------------|--------------------|
|  | 2012                        | 2011              | 2010              | 2011 to<br>2012             | 2010 to<br>2011    |
| <b>Additions</b>                           |                             |                   |                   |                             |                    |
| Participant contributions                  | \$ 16,444.8                 | \$ 16,725.2       | \$ 16,001.6       | \$ (280.4)                  | \$ 723.6           |
| Employer contributions                     | 63,644.1                    | 62,694.4          | 78,509.8          | 949.7                       | (15,815.4)         |
| Investment income/(loss)                   | (69.1)                      | 105,253.4         | 42,532.3          | (105,322.5)                 | 62,721.1           |
| Other                                      | -                           | 5.0               | -                 | (5.0)                       | 5.0                |
| Total additions                            | <u>80,019.8</u>             | <u>184,678.0</u>  | <u>137,043.7</u>  | <u>(104,658.2)</u>          | <u>47,634.3</u>    |
| <b>Deductions</b>                          |                             |                   |                   |                             |                    |
| Benefits                                   | 106,653.1                   | 100,719.8         | 91,569.7          | 5,933.3                     | 9,150.1            |
| Refunds                                    | 586.4                       | 652.2             | 510.5             | (65.8)                      | 141.7              |
| Administrative expenses                    | 764.1                       | 622.0             | 563.4             | 142.1                       | 58.6               |
| Total deductions                           | <u>108,003.6</u>            | <u>101,994.0</u>  | <u>92,643.6</u>   | <u>6,009.6</u>              | <u>9,350.4</u>     |
| Net increase/(decrease) in plan net assets | <u>\$ (27,983.8)</u>        | <u>\$82,684.0</u> | <u>\$44,400.1</u> | <u>\$(110,667.8)</u>        | <u>\$ 38,283.9</u> |

# FINANCIAL STATEMENTS

## JUDGES' RETIREMENT SYSTEM OF ILLINOIS

Statements of Plan Net Assets

June 30, 2012 and 2011

|   | 2012                  | 2011                  |
|---|-----------------------|-----------------------|
| Assets  |                       |                       |
| Cash  | \$ 10,690,635         | \$ 18,015,766         |
| Receivables:  |                       |                       |
| Employer contributions  | 7,953,510             | -                     |
| Participants' contributions   | 186,463               | 148,637               |
| Refundable annuities  | 1,485                 | 8,895                 |
| Interest on cash balances   | 4,155                 | 8,261                 |
| Due from General Assembly Retirement System   | 65,961                | 55,523                |
| Total Receivables   | <u>8,211,574</u>      | <u>221,316</u>        |
| Investments - held in the Illinois State Board of<br>Investment Commingled Fund at fair value | <u>559,139,279</u>    | <u>587,794,578</u>    |
| Securities lending collateral with State Treasurer  | <u>5,945,000</u>      | <u>7,261,000</u>      |
| Equipment, net of accumulated depreciation  | <u>9,326</u>          | <u>3,377</u>          |
| Total Assets  | <u>583,995,814</u>    | <u>613,296,037</u>    |
| Liabilities   |                       |                       |
| Benefits payable  | 711                   | 5,331                 |
| Refunds payable   | -                     | 527                   |
| Administrative expenses payable   | 73,736                | 68,971                |
| Securities lending collateral   | <u>5,945,000</u>      | <u>7,261,000</u>      |
| Total Liabilities   | <u>6,019,447</u>      | <u>7,335,829</u>      |
| Net assets held in trust for pension benefits   | <u>\$ 577,976,367</u> | <u>\$ 605,960,208</u> |
| <i>See accompanying notes to financial statements.</i>  |                       |                       |

# FINANCIAL STATEMENTS

## JUDGES' RETIREMENT SYSTEM OF ILLINOIS

Statements of Changes in Plan Net Assets

Years Ended June 30, 2012 and 2011

|   | 2012                  | 2011                  |
|---|-----------------------|-----------------------|
| <b>Additions:</b>   |                       |                       |
| Contributions:  |                       |                       |
| Participants  | \$ 16,444,796         | \$ 16,725,191         |
| Employer  | 63,644,099            | 62,694,460            |
| Total contributions   | <u>80,088,895</u>     | <u>79,419,651</u>     |
| Investments:  |                       |                       |
| Net investment income   | 13,408,141            | 12,025,283            |
| Interest earned on cash balances                                | 86,203                | 109,280               |
| Net appreciation (depreciation)<br>in fair value of investments | <u>(13,563,440)</u>   | <u>93,118,822</u>     |
| Total investment income (loss)                                  | <u>(69,096)</u>       | <u>105,253,385</u>    |
| Other:  |                       |                       |
| Miscellaneous   | -                     | 5,000                 |
| Total Additions   | <u>80,019,799</u>     | <u>184,678,036</u>    |
| <b>Deductions:</b>  |                       |                       |
| Benefits:   |                       |                       |
| Temporary disability  | -                     | 72,613                |
| Retirement annuities  | 87,161,263            | 82,076,983            |
| Survivors' annuities  | <u>19,491,832</u>     | <u>18,570,146</u>     |
| Total benefits  | 106,653,095           | 100,719,742           |
| Refunds of contributions  | 586,455               | 652,193               |
| Administrative expenses   | <u>764,090</u>        | <u>622,045</u>        |
| Total Deductions  | <u>108,003,640</u>    | <u>101,993,980</u>    |
| Net Increase (Decrease)   | <u>(27,983,841)</u>   | <u>82,684,056</u>     |
| Net assets held in trust for pension benefits:                  |                       |                       |
| Beginning of year   | <u>605,960,208</u>    | <u>523,276,152</u>    |
| End of year   | <u>\$ 577,976,367</u> | <u>\$ 605,960,208</u> |
| <i>See accompanying notes to financial statements.</i>          |                       |                       |

## JUDGES' RETIREMENT SYSTEM OF ILLINOIS

Notes to Financial Statements June 30, 2012 and 2011

### 1. Reporting Entity

Generally accepted accounting principles require that the financial reporting entity include (1) the primary government (2) organizations for which the primary government is financially accountable and (3) other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.

The Judges' Retirement System of Illinois (System) is administered by a Board of Trustees consisting of five persons, which include the State Treasurer, the Chief of the Supreme Court, ex officio, and three participating judges appointed by the Supreme Court.

Based on the criteria of the Governmental Accounting Standards Board Statement No. 14, there are no other state agencies, boards or commissions, or other organizations required to be combined with the System, however, the System is considered to be part of the State of Illinois financial reporting entity, and is to be combined and included in the State of Illinois' comprehensive annual financial report.

Pursuant to federal tax law and regulations governing the administration of public employee pension plans, the System has established a separate fund for the sole purpose of paying benefits in accordance with Section 415 of the Internal Revenue Code. The receipts and disbursements from the fund for fiscal

years 2012 and 2011 were each less than \$760,000. Due to the immaterial nature of the separate fund, these receipts and disbursements have been included in the System's financial statements.

### 2. Plan Description

The System is the administrator of a single-employer defined benefit public employee retirement system (PERS) established and administered by the State of Illinois to provide pension benefits for its participants. The plan is comprised of two tiers of contribution requirements and benefit levels. Tier 1 pertains to participants who first became a participant of the System prior to January 1, 2011. Tier 2 pertains to participants who first became a participant of the System on or after January 1, 2011.

#### a. Eligibility and Membership

The Judges' Retirement System covers Judges, Associate Judges and, under certain conditions, the Administrative Director of the Illinois courts. Participation by Judges, either appointed or elected, is mandatory unless the Judge files an election not to participate within thirty days of receipt of notice of this option.

#### b. Contributions

In accordance with Chapter 40, Section 5/18-133 of the Illinois Compiled Statutes, participants contribute specified percentages of their salaries for retirement annuities, survivors' annuities, and annual increases. Tier 1 participants contribute based on total annual compensation. Beginning January 1, 2011, Tier 2 participants contribute based on an annual compensation not to exceed \$106,800 with limitations for future years increased by the lesser of 3% or the annual percentage increase in the Consumer Price Index. The calendar year 2012 rate is \$110,004. Contributions are excluded from gross income for Federal and State income tax purposes.

Participants who are eligible to receive the maximum rate of annuity may irrevocably elect to discontinue contributions and have their benefits "frozen" based upon the applicable salary in effect immediately prior to the effective date of such election.

Participants who have attained age 60 and are eligible to receive the maximum rate of annuity and have not elected to discontinue contributing to the System may irrevocably elect to have their contributions based only on the salary increases received on or after the effective date of such election rather than on the total salary received.

At June 30, 2012 and 2011, the System membership consisted of:

|   | 2012  | 2011  |
|---|-------|-------|
| Retirees and beneficiaries currently receiving benefits:              |       |       |
| Retirement annuities  | 725   | 720   |
| Survivors' annuities  | 331   | 327   |
|   | 1,056 | 1,047 |
| Inactive participants entitled to benefits but not yet receiving them | 15    | 16    |
| Total   | 1,071 | 1,063 |
| Current participants:   |       |       |
| Vested  | 627   | 633   |
| Nonvested   | 341   | 335   |
| Total   | 968   | 968   |

*Operation of the System and the direction of its policies are the responsibility of the Board of Trustees.*

The total contribution rate is 11% if the participants elect to contribute for their spouse and dependents as shown below:

|       |                            |
|-------|----------------------------|
| 7.5%  | Retirement annuity         |
| 2.5%  | Survivors' annuity         |
| 1.0%  | Automatic annual increases |
| 11.0% |                            |

The statutes governing the Judges' Retirement System provide for optional contributions by participants, with interest at prescribed rates, to retroactively establish service credits for periods of prior creditable service.

The Board of Trustees has adopted the policy that interest payments by a participant, included in optional contributions to retroactively establish service credits, shall be considered an integral part of the participant's investment in annuity expectancies and, as such, shall be included as a part of any refund payable.

The payment of (1) the required State contributions, (2) all benefits granted under the System and (3) all expenses in connection with the administration and operation thereof are the obligations of the State to the extent specified in Chapter 40, Article 5/18 of the Illinois Compiled Statutes.

### c. Benefits

#### Retirement Annuity: Tier 1

Participants have vested rights to full retirement benefits beginning at age 60 with at least 10 years of credited service or reduced retirement benefits beginning at age 55. Participants also have vested rights to full retirement benefits at age 62 upon completing 6 years of credited service or at age 55 upon completing 26 years of credited service.

The retirement annuity provided is 3-1/2% for each of the first 10 years of service, plus 5% for each year of service in excess of 10, based upon the applicable final salary. The maximum retirement annuity is 85% of the applicable final salary. Annual automatic increases of 3% of the current amount of retirement annuity are provided.

#### Retirement Annuity: Tier 2

Participants have vested rights to full retirement benefits at age 67 with at least 8 years of credited service or reduced retirement benefits at age 62 with at least 8 years of credited service.

The retirement annuity provided is 3% for each year of service based upon the applicable final average salary. The maximum retirement annuity is 60% of the applicable final average salary. Annual automatic increases equal to the lesser of 3% or the annual change in the Consumer Price Index are provided.

### Other Benefits:

The Judges' Retirement System also provides survivors' annuity benefits, temporary and/or total disability benefits and, under certain specified conditions, lump-sum death benefits.

Participants who terminate service and are not eligible for an immediate annuity may receive, upon application, a refund of their total contributions. Participants or annuitants who are not married are entitled to refunds of their contributions for survivors.

## 3. Summary of Significant Accounting Policies & Plan Asset Matters

### a. Basis of Accounting

The financial transactions of the System are maintained and these financial statements have been prepared using the accrual basis of accounting in conformity with generally accepted accounting principles.

Participant and employer contributions are recognized as revenues when due pursuant to statutory requirements. Benefits and refunds are recognized as expenses when due and payable in accordance with the terms of the plan.

### b. Cash

The System retains all of its available cash in a commingled investment pool managed by the Treasurer of the State of Illinois (Treasurer). All deposits are fully collateralized by the Treasurer.

"Available cash" is determined to be that amount which is required for the current operating expenditures of the System. The excess of available cash is transferred to the Illinois State Board of Investment (ISBI) for purposes of long-term investment for the System.

### c. Implementation of New Accounting Standard

GASB Statement No. 64, "Derivative Instruments: Application of Hedge Accounting Termination Provisions - An Amendment to GASB Statement No. 53", was established to enhance comparability and improve financial reporting by clarifying the circumstances in which hedge accounting should continue when a swap counterparty, or a swap counterparty's credit support provider, is replaced. The ISBI implemented this Statement for the year ending June 30, 2012.

### d. General Litigation

The System is subject to claims and lawsuits that arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the plan net assets or the changes in plan net assets of the System.

## e. Methods Used to Value Investments

Investments are managed by the ISBI pursuant to Chapter 40, Article 5/22A of the Illinois Compiled Statutes (ILCS) and are maintained in the ISBI Commingled Fund.

Investments owned are reported at fair value as follows: (1) U.S. Government and Agency, Foreign and Corporate Obligations, Convertible Bonds – prices quoted by a major dealer in such securities; (2) Common Stock and Equity Funds, Preferred Stock, Foreign Equity Securities, Forward Foreign Currency Contracts and Options: (a) Listed – closing prices as reported on the composite summary of national securities exchanges; (b) Over-the-counter – bid prices; (3) Money Market Instruments – average cost which approximates fair values; (4) Real Estate Investments – fair values as determined by the ISBI and its investment managers; (5) Alternative Investments (Private Equity, Hedge Funds, Bank Loans, and Infrastructure Funds) – fair values as determined by the ISBI and its investment managers; and (6) Commingled Funds – fair values as determined by the ISBI and its investment managers.

Units of the ISBI Commingled Fund are issued to the member systems on the last day of the month based on the unit net asset value calculated as of that date. Net investment income of the ISBI Commingled Fund is allocated to each of the member systems on the last day of the month on the basis of percentage of accumulated units owned by the respective systems. Management expenses are deducted monthly from income before distribution.

The investment authority of the ISBI is provided in Chapter 40, Section 5/22A-112 of the ILCS. Such investment authority requires that all opportunities be undertaken with care, skill, prudence and diligence given prevailing circumstances that a prudent person acting in like capacity and experience would undertake.

## f. Actuarial Experience Review

In accordance with Illinois Compiled Statutes, an actuarial experience review is to be performed at least once every five years to determine the adequacy of actuarial assumptions regarding the mortality, retirement, disability, employment, turnover, interest and earnable compensation of the members and beneficiaries of the System. An experience review was last performed as of June 30, 2010 resulting in the adoption of new assumptions as of June 30, 2011.

## g. Administrative Expenses

Expenses related to the administration of the System are financed through investment earnings and employer retirement contributions. These expenses are budgeted and approved by the System's Board of Trustees.

For fiscal year 2012, administrative expenses common to the Judges' Retirement System and the General Assembly Retirement System are allocated 75% to the Judges' Retirement System and 25% to the General Assembly Retirement System. For fiscal year 2011, administrative expenses common to the Judges' Retirement System and the General Assembly Retirement System were allocated 70% to the Judges' Retirement System and 30% to the General Assembly Retirement System. Invoices/vouchers covering common expenses incurred are paid by the Judges' Retirement System, and the appropriate amount is allocated to and reimbursed by the General Assembly Retirement System. Administrative expenses allocated to and reimbursed by the General Assembly Retirement System as of June 30, 2012 and 2011, were \$224,439 and \$226,995, respectively.

## h. Risk Management

The System, as part of the primary government of the State, provides for risks of loss associated with workers' compensation and general liability through the State's self-insurance program. The System obtains commercial insurance for fidelity, surety, and property. There have been no commercial insurance claims in the past three fiscal years.

## i. Use of Estimates

In preparing financial statements in conformity with U.S. generally accepted accounting principles, the System makes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates and assumptions.

## j. Reclassifications

Certain fiscal year 2011 amounts have been reclassified to conform to the fiscal year 2012 presentation. These reclassifications have not changed the fiscal year 2011 results.

## 4. Investments

### *Summary of the ISBI Fund's investments at fair value by type*

|                                    | June 30, 2012                  | June 30, 2011                  |
|------------------------------------|--------------------------------|--------------------------------|
| U.S. govt. and agency obligations  | \$ 958,131,279                 | \$ 1,367,098,751               |
| Foreign obligations                | 385,628,617                    | 37,951,769                     |
| Corporate obligations              | 656,977,663                    | 762,833,382                    |
| Common stock & equity funds        | 3,253,103,566                  | 3,380,198,858                  |
| Commingled funds                   | 225,608,712                    | 256,817,374                    |
| Foreign equity securities          | 2,012,774,573                  | 2,195,201,185                  |
| Foreign preferred stock            | 592,156                        | 40,032                         |
| Hedge funds                        | 1,026,725,785                  | 1,075,584,754                  |
| Real estate funds                  | 967,346,450                    | 780,336,465                    |
| Private equity                     | 679,423,383                    | 629,256,286                    |
| Money market instruments           | 255,922,180                    | 303,501,465                    |
| Real assets                        | 507,019,665                    | 455,984,316                    |
| Bank loans                         | 328,593,596                    | 253,447,070                    |
| Forward foreign currency contracts | (43,859)                       | (353)                          |
| <b>Total investments</b>           | <b><u>\$11,257,803,766</u></b> | <b><u>\$11,498,251,354</u></b> |

### Deposits

Custodial credit risk for deposits is the risk that, in the event of a financial institution failure, the System's and ISBI's deposits may not be returned. All non-investment related bank balances at year-end are insured or collateralized with securities held by the Illinois State Treasurer or agents in the name of the State Treasurer. As of June 30, 2012 and 2011, the ISBI had non-investment related bank balances of \$25,096,663 and \$119,804, respectively. Of the June 30, 2012 cash balance, \$24,854,573 represents the transfer of the Illinois Power Agency Trust funds. This cash was held by the State Treasurer pending transfer to State Street Bank and Trust Company for investment. The transfer of these funds to State Street Bank and Trust for investment occurred on July 19, 2012. During fiscal year 2007, a Credit Risk Policy was implemented by the ISBI staff and formally adopted by the ISBI Board in July of 2007. The policy outlines the control procedures used to monitor custodial credit risk. These assets are under the custody of State Street Bank and Trust Company. State Street Bank and Trust Company has an AA- Long-term Deposit/Debt rating by Standard & Poor's and an Aa2 rating by Moody. Certain investments of the ISBI with maturities of 90 days or less would be considered cash equivalents; these consist of short-term investment

funds and U.S. Treasury bills with maturities of 90 days or less, which are not subject to the custodial credit risk. For financial statement presentation and investment purposes, the ISBI reports these types of cash equivalents as Money Market Instruments within their investments. As of June 30, 2012 and 2011, the ISBI had investment related bank balances of \$20,601,170 and \$12,234,333, respectively. These balances include USD and foreign cash balances. The USD cash balances had no exposure to custodial credit risk as a result of the passage of the Dodd Frank Wall Street Reform and Consumer Protection Act ("Dodd Frank Act") in July, 2010. The FDIC must provide unlimited deposit insurance coverage for balances held in US dollar non-interest bearing transaction accounts (DDAs) for a period of two years, beginning on December 31, 2010 and ending on December 31, 2012. At any given point and time, the foreign cash balances may be exposed to custodial credit risk.

## Investment Commitments

The ISBI's real estate and private equity investment portfolios consist of passive interests in limited partnerships. The ISBI had outstanding commitments to these limited partnerships of approximately \$478 million and \$344 million, as of June 30, 2012 and 2011, respectively. Also, at the end of fiscal year 2012 and 2011, the ISBI had outstanding commitments of \$196 million and \$321 million, respectively, to separate real estate accounts. Also at the end of fiscal year 2012 and 2011, the ISBI had outstanding amounts of \$63 million and \$102 million, respectively, committed to real assets. The ISBI would fund outstanding commitments by utilizing available cash and then selling liquid securities in the portfolio as necessary.

## Investment Liquidity

The ISBI holds investments in hedge funds, real estate funds, private equity funds and real assets that are considered illiquid by the very nature of the investment. Market risk exists with respect to these investments as the ISBI may not be able to exit from the investments during periods of significant market value declines.

## Alternative Investments

The ISBI's investments in hedge funds are structured to achieve a diversified hedged equity fund-of-funds portfolio. Capital is allocated to a select group of hedge fund managers that invest predominately in equity securities, both long and short. The investments shall be managed with the intent of preserving capital in a declining market and in a rising market they will generate a smaller return than the overall equity market.

The ISBI's investments in Private Equity and Real Estate funds represent investment vehicles used for making investments in various equity and debt securities according to the investment strategies as determined by the fund managers at the commencement of the fund.

Investment strategies of Private Equity funds include, but are not limited to, leveraged buyouts, venture capital, growth capital and mezzanine capital.

Investment strategies of Real Estate investments include, but are not limited to, the purchase, development, ownership, management, rental and/or sale of real estate for profit. In May, 2011, RLJ Lodging Fund II, a limited partnership investment, was exchanged by the ISBI for 1,035,092 shares of restricted common stock as a result of an initial public offering (IPO) transaction conducted by RLJ Lodging Trust. Due to the fact that this holding is

currently restricted for sale as a result of a lock-up agreement in place that specifies that during the period that commences 180 days from the date of the initial IPO the holders of the shares will not, without prior written consent of the underwriting group, directly or indirectly offer, pledge, sell, contract to sell, sell any option or contract to purchase, purchase any option or contract to sell, grant any option, right or warrant for sale of, or otherwise dispose or transfer such shares. As of June 30, 2011, this holding is an illiquid asset as a result of this restriction. During fiscal year 2012, the restriction attached to these shares expired and 1,043,923 in RLJ Lodging Trust shares were sold in March 2012. This included an additional amount of 8,831 shares received by the ISBI during the fiscal year.

Certain real estate investments are leveraged whereby partnerships have been established to purchase properties through a combination of contributions from the ISBI and through acquisition of debt. At June 30, 2012, real estate equities of approximately \$967 million are reported at estimated fair value. Of this amount, \$795 million is equity and \$172 million is long term debt. At June 30, 2011 real estate equities of approximately \$780 million were reported at estimated market value. Of this amount, \$669 million was equity and \$111 million was long term debt.

Required repayment of real estate debt, which is non-recourse debt is as follows as of June 30, 2012 and 2011:

| Debt Maturities     |                      |                      |
|---------------------|----------------------|----------------------|
| Year Ending June 30 | 2012                 | 2011                 |
| 2013                | \$ 38,336,179        | \$ 37,099,137        |
| 2014                | -                    | -                    |
| 2015                | 39,603,847           | 40,070,463           |
| 2016                | 28,761,199           | 33,400,000           |
| 2017                | 64,845,576           | -                    |
|                     | <u>\$171,546,801</u> | <u>\$110,569,600</u> |

The ISBI's investments in Real Assets represent pooled investment vehicles used to seek capital appreciation and current income by acquiring, holding, financing, refinancing and disposing of infrastructure investments and farmland assets. Real Assets include various public works (e.g. bridges, tunnels, toll roads, airports, public transportation and other public works) that are made typically as a part of a privatization initiative on the part of a government entity.

## FINANCIAL STATEMENTS

A Commingled fund is a kind of mutual fund or common trust fund which consists of multiple kinds of assets from several accounts combined together. 'Commingling' these separate assets mitigates risk for the trader through investment diversification and reduces the cost of managing each account separately. Commingled funds are also called "pooled funds" and "master trusts".

### Concentration of Credit Risk and Credit Risk for Investments

The ISBI's portfolio of investments is managed by professional investment management firms. These investment management firms are required to maintain diversified portfolios. Each investment manager must comply with risk management guidelines individually assigned to them as part of their investment management agreement. The ISBI did not have any single issuer investment that exceeded 5% of the total net assets of the fund as of June 30, 2012 and 2011. At June 30, 2012, Commingled funds totaled approximately \$226 million. Of this amount, approximately \$165 million is invested in fixed income securities. At June 30, 2011, Commingled funds totaled approximately \$257 million. Of this amount, approximately \$215 million is invested in fixed income securities. These securities are not rated. The table to the right presents the quality ratings of debt securities held by the ISBI as of June 30, 2012 and 2011.

|  | Moody's<br>Quality Rating        | 2012                  | 2011                    |
|--|----------------------------------|-----------------------|-------------------------|
| U.S. Government and<br>Agency obligations        | AAA                              | \$ 955,072,566        | \$ 1,355,098,991        |
|  | AA                               | 3,054,072             | -                       |
|  | Not Rated                        | 4,641                 | 11,999,760              |
| <b>Total U.S. govt. and agency obligations</b>   |                                  | <b>\$ 958,131,279</b> | <b>\$ 1,367,098,751</b> |
| Foreign Obligations                              | AAA                              | \$ 186,587,716        | \$ -                    |
|  | AA                               | 70,836,832            | 2,972,737               |
|  | A                                | 38,941,615            | 9,187,174               |
|  | BAA                              | 17,922,423            | -                       |
|  | BA                               | 13,976,279            | 7,107,320               |
|  | B                                | 16,044,688            | 17,263,610              |
|  | CAA                              | 1,411,638             | -                       |
|  | Not rated                        | 39,907,426            | 1,420,928               |
|  | <b>Total Foreign Obligations</b> |                       | <b>\$ 385,628,617</b>   |
| Corporate Obligations<br>Bank and Finance        | AAA                              | \$ -                  | \$ 7,075,122            |
|  | AA                               | 6,229,998             | 46,441,423              |
|  | A                                | 65,118,722            | 110,462,063             |
|  | BAA                              | 46,729,424            | 14,653,097              |
|  | BA                               | 13,870,851            | 8,808,672               |
|  | B                                | 17,295,104            | 17,167,398              |
|  | Not Rated                        | 1,045                 | 802                     |
|  | <b>Total Bank and Finance</b>    |                       | <b>\$ 149,245,144</b>   |
| Collateralized Mortgage Obligations              | AAA                              | \$ 1,076,456          | \$ 10,711,049           |
|  | Not Rated                        | -                     | 2,781,477               |
| <b>Total Collateralized Mortgage Obligations</b> |                                  | <b>\$ 1,076,456</b>   | <b>\$ 13,492,526</b>    |
| Industrial                                       | AA                               | \$ 36,473,262         | \$ 36,746,537           |
|  | A                                | 29,602,573            | 50,163,160              |
|  | BAA                              | 75,478,624            | 81,696,395              |
|  | BA                               | 59,680,342            | 62,382,115              |
|  | B                                | 193,691,505           | 167,590,259             |
|  | CAA                              | 10,775,593            | 9,516,061               |
|  | Not Rated                        | 6,530,791             | 17,752,514              |
| <b>Total Industrial</b>                          |                                  | <b>\$ 412,232,690</b> | <b>\$ 425,847,041</b>   |
| Other  | AA                               | \$ 1,127,225          | \$ 2,941,058            |
|  | A                                | 22,075,563            | 12,003,588              |
|  | BAA                              | 7,428,269             | 7,027,751               |
|  | BA                               | 19,369,553            | 36,360,024              |
|  | B                                | 43,572,387            | 51,094,875              |
|  | CAA                              | -                     | 5,582,749               |
|  | Not rated                        | 850,376               | 3,875,193               |
| <b>Total Other</b>                               |                                  | <b>\$ 94,423,373</b>  | <b>\$ 118,885,238</b>   |
| <b>Total Corporate Obligations</b>               |                                  | <b>\$ 656,977,663</b> | <b>\$ 762,833,382</b>   |
| Money Market                                     | Not Rated                        | \$ 255,922,180        | \$ 303,501,465          |
| <b>Total Money Market</b>                        |                                  | <b>\$ 255,922,180</b> | <b>\$ 303,501,465</b>   |

## FINANCIAL STATEMENTS

### Custodial Credit Risk for Investments

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the ISBI will not be able to recover the value of investments or collateral securities that are in the possession of a counterparty. As of June 30, 2012 and 2011, there were no investments that were uninsured and unregistered, securities held by the counterparty or by its trust department or agent but not in the ISBI's name.

### Interest Rate Risk

The ISBI manages its exposure to fair value losses arising from interest rate risk by diversifying the debt securities portfolio and maintaining the debt securities portfolio to an effective weighted duration between 80% and 120% of the benchmark index.

Duration is the measure of a debt investment's exposure to fair value changes arising from changing interest rates. It uses the present value of cash flows, weighted for those cash flows as a percentage of the investment's fair value. The effective duration measures the sensitivity of market price to parallel shifts in the yield curve. As of June 30, 2012 and 2011, the ISBI benchmarked its debt security portfolio to Barclay's Capital Intermediate U.S. Government/Credit Bond Index. At June 30, 2012 and 2011, the effective duration of the Barclay's Capital Intermediate U.S. Government/Credit Bond Index was 3.9 years. At the same point in time, the effective duration of the ISBI debt security portfolio at June 30, 2012 and 2011 was 4.6 years. The table below shows the detail of the duration by investment type as of June 30, 2012 and 2011.

| Investment Type                     | 2012                    |                                   | 2011                    |                                   |
|-------------------------------------|-------------------------|-----------------------------------|-------------------------|-----------------------------------|
|                                     | Fair Value              | Effective Weighted Duration Years | Fair Value              | Effective Weighted Duration Years |
| U.S. Govt. and Agency Obligations   |                         |                                   |                         |                                   |
| U.S. Government                     | \$ 383,122,214          | 6.7                               | \$ 479,422,631          | 6.9                               |
| Agency                              | 575,009,065             | 2.7                               | 887,676,120             | 3.6                               |
| Foreign Obligations                 | 385,628,617             | 6.1                               | 37,951,769              | 4.3                               |
| Corporate Obligations               |                         |                                   |                         |                                   |
| Bank & Finance                      | 149,245,144             | 3.9                               | 204,608,577             | 4.2                               |
| Collateralized Mortgage Obligations | 1,076,456               | 2.2                               | 13,492,526              | 2.1                               |
| Industrials                         | 412,232,690             | 4.0                               | 425,847,041             | 4.4                               |
| Other                               | 94,423,373              | 4.2                               | 118,885,238             | 4.2                               |
| Total                               | <u>\$ 2,000,737,559</u> |                                   | <u>\$ 2,167,883,902</u> |                                   |

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### Foreign Currency Risk

The ISBI's international portfolio is constructed on the principles of diversification, quality growth, and value. Risk of loss arises from changes in currency exchange rates. International managers may also engage in transactions to hedge currency at their discretion.

Certain investments held in infrastructure funds trade in a reported currency of Euro-based dollars valued at \$53,539,234 and \$50,878,191 as of June 30, 2012 and 2011, respectively. The table below presents the foreign currency risk by type of investment as of June 30, 2012 and 2011.

| Currency   | 2012  |                       | 2011  |                      |
|--|---|-----------------------|---|----------------------|
|  | Foreign Equity Securities & Foreign Preferred Stock | Foreign Obligations   | Foreign Equity and Foreign Preferred Securities | Foreign Obligations  |
| Australian Dollar                                  | \$ 82,314,617                                       | \$ 16,469,771         | \$ 109,809,451                                  | \$ -                 |
| Brazilian Real                                     | 49,364,844  | -                     | 62,981,703                                      | -                    |
| Canadian Dollar                                    | 126,199,484   | 27,179,367            | 144,335,493                                     | -                    |
| Chilean Peso                                       | 1,098,684   | 2,308,184             | -   | -                    |
| Czech Koruna                                       | 536,589   | 2,520,227             | -   | -                    |
| Danish Krone                                       | 27,321,050  | 4,165,438             | 25,279,264                                      | -                    |
| Egyptian Pound                                     | 1,810,173   | -                     | 1,549,693                                       | -                    |
| English Pound Sterling                             | 374,618,002   | 32,868,184            | 388,163,730                                     | -                    |
| Euro Currency                                      | 394,894,819   | 103,642,653           | 550,189,912                                     | -                    |
| Hong Kong Dollar                                   | 127,339,809   | 2,384,108             | 83,691,016                                      | -                    |
| Hungarian Forint                                   | 1,457,562   | -                     | 1,711,349                                       | -                    |
| Indonesian Rupian                                  | 9,446,308   | -                     | 1,735,957                                       | -                    |
| Israeli Shekel                                     | 2,619,603   | 28,742                | 4,293,903                                       | -                    |
| Japanese Yen                                       | 191,615,229   | 65,481,682            | 249,633,309                                     | -                    |
| Malaysian Ringgit                                  | 7,106,044   | 2,848,977             | -   | -                    |
| Mexican Peso                                       | 20,566,508  | 13,648,235            | 10,577,337                                      | -                    |
| Moroccan Dirham                                    | 219,512   | -                     | -   | -                    |
| New Zealand Dollar                                 | 5,008,123   | 1,783,525             | 4,812,384                                       | -                    |
| Norwegian Krone                                    | 24,657,161  | 6,403,137             | 25,479,679                                      | -                    |
| Philippine Peso                                    | 2,219,444   | -                     | -   | -                    |
| Polish Zloty                                       | 2,949,201   | 8,408,688             | -   | -                    |
| Singapore Dollar                                   | 42,090,664  | 3,813,610             | 51,977,284                                      | -                    |
| South African Rand                                 | 25,078,599  | 4,116,002             | 11,571,713                                      | -                    |
| South Korean Won                                   | 71,317,427  | 13,526,890            | 62,696,222                                      | -                    |
| Swedish Krona                                      | 27,254,280  | 10,680,201            | 35,264,901                                      | -                    |
| Swiss Franc  | 138,838,635   | 7,455,551             | 154,181,296                                     | -                    |
| Thailand Baht                                      | 3,954,203   | 4,274,188             | -   | -                    |
| Turkish Lira                                       | 2,811,622   | -                     | -   | -                    |
| Foreign investments<br>denominated in U.S. Dollars | 248,658,533   | 51,621,257            | 215,305,621                                     | 37,951,769           |
| Total  | <u>\$ 2,013,366,729</u>                             | <u>\$ 385,628,617</u> | <u>\$ 2,195,241,217</u>                         | <u>\$ 37,951,769</u> |

## Securities Lending

The ISBI participates in a securities lending program with Credit Suisse AG, New York Branch who acts as securities lending agent. Securities are loaned to brokers and, in return, the ISBI receives cash and non-cash collateral. All of the securities are eligible for the securities lending program. Collateral consists solely of cash and government securities having a fair value equal to or exceeding 102% of the value of the loaned securities (105% for non-U.S. securities). In the event of borrower default, Credit Suisse AG, New York Branch provides the ISBI with counterparty default indemnification. Investments in the cash collateral account represent securities that were distributed to the ISBI in connection with the in-kind redemption of the ISBI's ownership in the State Street Bank and Trust Company Quality Funds for Short-Term Investment ("Quality D"). Credit Suisse is not responsible for any losses with regards to these legacy investments. This arrangement subjects the ISBI to credit risk as the credit quality of these investments may decline over time. The credit risk on the legacy investments is the risk of a possible loss arising from the inability of a counterparty to meet its obligations. These losses could include the loss of principal, interest and/or decreased expected cash flows in any of the investments held in the ISBI's cash collateral account. In the event a counterparty defaults on its obligations, the ISBI would need to credit the cash collateral account with the amount of the default to make the account whole so that once loaned securities are returned, the cash pledged by borrowers is returned to them. As of June 30, 2012 and 2011, respectively, the collateral received exceeded the fair value of the securities loaned. As of June 30, 2012 and 2011, there were outstanding loaned investment securities having fair values of \$115,655,166 and \$221,448,333, respectively; against which collateral was received with a fair value of \$120,556,697 and \$230,083,146, respectively. Collateral received at June 30, 2012 and 2011 consisted of \$72,452,520 and \$216,717,213, respectively, in cash and \$48,104,177 and \$13,987,903, respectively, in securities for which the ISBI does not have the ability to pledge or sell.

The cash collateral received is invested in a short-term investment pool having a fair value of \$67,901,315 and \$211,162,204 as of June 30, 2012 and 2011, respectively. This investment pool had an average duration of 32.42 days and 31.18 days as of June 30, 2012 and 2011, respectively. Any decrease in the fair value of invested cash collateral is recorded by the ISBI as unrealized losses and reported as a component of the investment income/loss on the ISBI's Statement of Changes in Net Assets.

Cash and cash equivalents included in the System's Statement of Plan Net Assets consist of deposits held in the State Treasury. The Illinois Office of the Treasurer

invests the deposits held and allocates investment income on a monthly basis.

The State Treasurer lends securities to broker-dealers and other entities for collateral that will be returned for the same securities in the future. The State Treasurer has, through a Securities Lending Agreement, authorized Deutsche Bank Group to lend the State Treasurer's securities to broker-dealers and banks pursuant to a form of loan agreement.

During fiscal years 2012 and 2011, Deutsche Bank Group lent U.S. Treasury and U.S. Agency securities and received as collateral U.S. dollar denominated cash. Borrowers were required to deliver collateral for each loan equal to at least 100% of the aggregated market value of the loaned securities. Loans are marked to market daily. If the market value of collateral falls below 100%, the borrower must provide additional collateral to raise the market value to 100%.

The State Treasurer did not impose any restrictions during fiscal years 2012 and 2011 on the amount of the loans of available, or the eligible securities. In the event of borrower default, Deutsche Bank Group provides the State Treasurer with counterparty default indemnification. In addition, Deutsche Bank Group is obligated to indemnify the State Treasurer if the Deutsche Bank Group loses any securities, collateral or investments of the State Treasurer in Deutsche Bank Group's custody. Moreover, there were no losses during the fiscal years 2012 and 2011 resulting from a default of the borrowers or Deutsche Bank Group.

During fiscal years 2012 and 2011, the State Treasurer and borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested in repurchase agreements with approved counterparties collateralized with securities approved by Deutsche Bank Group and marked to market daily at no less than 102%. Because the loans are terminable at will, their duration did not generally match the duration of the investments made with the cash collateral. The State Treasurer had no credit risk as a result of its securities lending program as the collateral held exceeded the fair value of the securities lent. The securities lending collateral invested in repurchase agreements and the fair value of securities on loan for the State Treasurer as of June 30, 2012 were \$4,556,511,251 and \$4,551,829,732, respectively. The securities lending collateral invested in repurchase agreements and the fair value of securities on loan for the State Treasurer as of June 30, 2011 were \$3,456,373,500 and \$3,446,138,880, respectively. The System's portion of securities lending collateral that was invested in repurchase agreements as of June 30, 2012 and June 30, 2011 were \$5,945,000 and \$7,261,000, respectively.

## Derivative Securities

In fiscal year 2010, the ISBI implemented GASB Statement No. 53 Accounting and Financial Reporting for Derivative Instruments with respect to investments held in derivative securities. A derivative security is an investment whose payoff depends upon the value of other assets such as commodity prices, bond and stock prices, or a market index. The ISBI invests in derivative instruments including forward foreign currency contracts, futures, rights and warrants. The ISBI's derivatives are considered investment derivatives.

Foreign currency forward contracts (FX forwards) are used to protect against the currency risk in the ISBI's foreign equity portfolio. A foreign currency forward contract is an agreement to buy or sell a specific amount of a foreign currency at a specified delivery or maturity date for an agreed-upon price. Fluctuations in the market value of foreign currency forward contracts are marked to market on a daily basis. These investments are reported at fair value in the investment section of the ISBI's Statement of Net Assets. The gain or loss arising from the difference between the original contracts and the closing of such contracts is recognized in the net increase/decrease in the fair value of investments in the ISBI's Statement of Changes in Net Assets. In May 2011, the ISBI removed language from the investment management agreements allowing managers to hedge foreign currencies and/or to hedge equity positions.

The ISBI's investment managers use financial futures to replicate an underlying security they wish to hold (sell) in the portfolio. In certain instances, it may be beneficial to own a futures contract rather than the underlying security (arbitrage). Additionally, financial futures are used in the ISBI's fixed income portfolio to adjust portfolio strategy and overall portfolio duration. A financial futures contract is an agreement to buy or sell a specific amount at a specified delivery or maturity date for an agreed-upon price. As the fair values of the futures contract vary from the original contract price, a gain or loss is recognized and paid to or received from the clearinghouse. The gain or loss is recognized in the net increase/decrease in the fair value of investments in the ISBI's Statement of Changes in Net Assets. Financial futures represent an off-balance sheet obligation, as there are no balance sheet assets or liabilities associated with those contracts. The cash or securities to meet these obligations are held in the ISBI's investment portfolio.

The ISBI's investment managers use options in an attempt to add value to the portfolio (collect premiums)

or protect (hedge) a position in the portfolio. Financial options are an agreement that gives one party the right, but not the obligation, to buy or sell a specific amount of an asset for a specified price, called the strike price, on or before a specified expiration date. As a writer of financial options, the ISBI receives a premium at the outset of the agreement and bears the risk of an unfavorable change in the price of the financial instrument underlying the option. All written financial options are recognized as a liability in the ISBI's Statement of Net Assets. As a purchaser of financial options, the ISBI pays a premium at the outset of the agreement and the counterparty bears the risk of an unfavorable change in the price of the financial instrument underlying the option. The gain or loss associated with options is recognized in the net increase/decrease in the fair value of investments in the ISBI's Statement of Changes in Net Assets.

Rights and warrants allow the ISBI's investment managers to replicate an underlying security they wish to hold (sell) in the portfolio. Rights and warrants provide the holder with the right, but not the obligation, to buy or sell a company's stock at a predetermined price. Rights usually expire after a few weeks and warrants can expire from one to several years. Under certain circumstances, a type of warrant called Participatory Notes (P-Notes) are used in the portfolio by the ISBI's investment managers that are not registered to trade in domestic Indian Capital Markets. P-Notes are issued by Indian-based brokerage firms against an underlying Indian security permitting holders to get a share in the income from the security. These investments are reported at fair value in the investment section of the ISBI's Statement of Net Assets within the common stock and foreign equity classifications. The gain or loss associated with rights and warrants is recognized in the net increase/decrease in the fair value of investments in the ISBI's Statement of Changes in Net Assets.

The fair values of the forward contracts are estimated based on the present value of their estimated future cash flows. Futures contracts are exchange traded instruments where the fair value is determined by the equilibrium between the forces of supply and demand. The fair value of a right or warrant closely tracks the intrinsic value of the underlying stock and can be determined either by formulaic methodology (most commonly Black-Scholes) or intrinsic value methodology.

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The table below presents the investment derivative instruments aggregated by type that were held by the ISBI as of June 30, 2012 and 2011.

|             | Changes in Fair Value |                     | Fair Value at Year End |                      | Notional Amount<br>Number of Shares |                  |
|-------------|-----------------------|---------------------|------------------------|----------------------|-------------------------------------|------------------|
|             | 2012                  | 2011                | 2012                   | 2011                 | 2012                                | 2011             |
| FX Forwards | \$ (1,693,910)        | \$(15,460,385)      | \$ (43,859)            | \$ (353)             | n/a                                 | n/a              |
| Futures     | n/a                   | n/a                 | n/a                    | n/a                  | (16,717,412)                        | 65,250           |
| Options     | 2,744,205             | -                   | 2,811,004              | -                    | 27,000                              | -                |
| Rights      | (166,937)             | 840,746             | 30,249                 | 162,133              | 153,435                             | 901,548          |
| Warrants    | (9,022,293)           | 16,898,459          | 68,676,781             | 66,421,545           | 7,663,933                           | 5,272,322        |
|             | <u>\$ (8,138,935)</u> | <u>\$ 2,278,820</u> | <u>\$ 71,474,175</u>   | <u>\$ 66,583,325</u> | <u>(8,873,044)</u>                  | <u>6,239,120</u> |

The table below shows the futures positions held by the ISBI as of June 30, 2012 and 2011.

|                                | 2012                   |                        | 2011                   |                        |
|--------------------------------|------------------------|------------------------|------------------------|------------------------|
|                                | Number of<br>Contracts | Contract<br>Principal* | Number of<br>Contracts | Contract<br>Principal* |
| Equity Futures Purchased       | 1,410                  | \$92,997,500           | 1,305                  | \$85,836,375           |
| Fixed Income Futures Purchased | 382                    | 48,411,940             | -                      | -                      |
| Fixed Income Futures Sold      | 421                    | 63,940,695             | -                      | -                      |

\* Contract principal amounts shown represent the market value of the underlying assets the contracts control. These are shown to present the volume of the transactions but do not reflect the extent to which positions may offset one another. These amounts do not represent the much smaller amounts potentially subject to risk. Contract principal values also do not represent actual recorded values reported in the ISBI's Statement of Net Assets.

Derivative transactions involve, to varying degrees, credit risk and market risk. Credit risk is the possibility that a loss may occur because a party to a transaction fails to perform according to terms. Derivatives which are exchange traded are not subject to credit risk. No derivatives held are subject to custodial credit risk. Market risk is the possibility that a change in interest (interest rate risk) or currency rates (foreign currency risk) will cause the value of a financial instrument to decrease or become more costly to settle. The market risk associated with derivatives, the prices of which are constantly fluctuating, is regulated by imposing strict

limits as to the types, amounts and degree of risk that investment managers may undertake. These limits are approved by the Board of Trustees and management of the ISBI and the risk positions of the investment managers are reviewed on a periodic basis to monitor compliance with the limits. As of June 30, 2012, the ISBI held futures contracts whose underlying instruments were exposed to interest rate risk but there were no GASB 53 reportable elements. As of June 30, 2011, the ISBI held no derivatives subject to interest rate risk. The ISBI has not adopted a formal policy specific to master netting arrangements.

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The ISBI's derivative investments in foreign currency forward contracts are held with counterparties. The credit ratings and net exposure as of June 30, 2012 and 2011 for the counterparties are as follows:

| Moody's Rating | 2012              |                   |                            | 2011                |                     |                            |
|----------------|-------------------|-------------------|----------------------------|---------------------|---------------------|----------------------------|
|                | Fair Value        | Net Exposure      | Percentage of Net Exposure | Fair Value          | Net Exposure        | Percentage of Net Exposure |
| Aa3            | \$ 45,189         | \$ 45,189         | 11.50%                     | \$ 188              | \$ 188              | 0.01%                      |
| Aa2            | 46,885            | 46,885            | 12.00%                     | -                   | -                   | -                          |
| A3             | 84,367            | 84,367            | 21.59%                     | 2,736,018           | 2,736,018           | 99.99%                     |
| A2             | 64,971            | 64,971            | 16.62%                     | -                   | -                   | -                          |
| A1             | 3,119             | 3,119             | 0.80%                      | -                   | -                   | -                          |
| Baa1           | 146,228           | 146,228           | 37.42%                     | -                   | -                   | -                          |
|                | <u>\$ 390,759</u> | <u>\$ 390,759</u> | <u>100.00%</u>             | <u>\$ 2,736,206</u> | <u>\$ 2,736,206</u> | <u>100.00%</u>             |

The following table presents the fair value of derivative investments exposed to foreign currency risk as of June 30, 2012 and 2011:

| Currency                                | 2012               |                  |                      |                     | 2011            |                   |                      |             |
|---|--------------------|------------------|----------------------|---------------------|-----------------|-------------------|----------------------|-------------|
|   | FX Forwards        | Rights           | Warrants             | Options             | FX Forwards     | Rights            | Warrants             | Options     |
| Australian Dollar                       | \$ (85,578)        | \$ -             | \$ -                 | \$ -                | \$ -            | \$ -              | \$ -                 | \$ -        |
| Brazilian Real                          | 1,589              | -                | -                    | -                   | -               | -                 | -                    | -           |
| Canadian Dollar                         | (13,256)           | 10,733           | -                    | -                   | -               | -                 | -                    | -           |
| Chilean Peso                            | 1,450              | 1,296            | -                    | -                   | -               | -                 | -                    | -           |
| Columbian Peso                          | (15,312)           | -                | -                    | -                   | -               | -                 | -                    | -           |
| Czech Koruna                            | 9,411              | -                | -                    | -                   | -               | -                 | -                    | -           |
| Danish Krone                            | (30)               | -                | -                    | -                   | -               | -                 | -                    | -           |
| Egyptian Pound                          | (148)              | -                | -                    | -                   | -               | -                 | -                    | -           |
| English Pound Sterling                  | 49,917             | -                | -                    | -                   | -               | -                 | -                    | -           |
| Euro Currency                           | 118,889            | 18,220           | 6,103                | -                   | (391)           | 153,078           | -                    | -           |
| Hong Kong Dollar                        | 234                | -                | -                    | -                   | -               | 9,055             | -                    | -           |
| Indonesian Rupiah                       | (619)              | -                | -                    | -                   | -               | -                 | -                    | -           |
| Japanese Yen                            | (19,071)           | -                | -                    | -                   | 38              | -                 | -                    | -           |
| Malaysian Ringgit                       | (1,234)            | -                | -                    | -                   | -               | -                 | -                    | -           |
| Mexican Peso                            | 27,008             | -                | -                    | -                   | -               | -                 | -                    | -           |
| New Zealand Dollar                      | 46,885             | -                | -                    | -                   | -               | -                 | -                    | -           |
| Norwegian Krone                         | 4,157              | -                | -                    | -                   | -               | -                 | -                    | -           |
| Polish Zloty                            | (32,461)           | -                | -                    | -                   | -               | -                 | -                    | -           |
| Singapore Dollar                        | (13,207)           | -                | -                    | -                   | -               | -                 | -                    | -           |
| South African Rand                      | 14,798             | -                | -                    | -                   | -               | -                 | -                    | -           |
| South Korean Won                        | 23,502             | -                | -                    | -                   | -               | -                 | -                    | -           |
| Swedish Krona                           | (154,835)          | -                | -                    | -                   | -               | -                 | -                    | -           |
| Swiss Franc                             | (5,251)            | -                | -                    | -                   | -               | -                 | -                    | -           |
| Thailand Baht                           | (697)              | -                | -                    | -                   | -               | -                 | -                    | -           |
| Investments denominated in U.S. dollars | <u>-</u>           | <u>-</u>         | <u>68,670,678</u>    | <u>2,806,363</u>    | <u>-</u>        | <u>-</u>          | <u>66,421,545</u>    | <u>-</u>    |
|   | <u>\$ (43,859)</u> | <u>\$ 30,249</u> | <u>\$ 68,676,781</u> | <u>\$ 2,806,363</u> | <u>\$ (353)</u> | <u>\$ 162,133</u> | <u>\$ 66,421,545</u> | <u>\$ -</u> |

## Other Information

The System owns approximately 5% of the net investment assets of the ISBI Commingled Fund as of June 30, 2012 and 2011. A schedule of investment expenses is included in the ISBI's annual report.

For additional information on ISBI's investments, please refer to their Annual Report as of June 30, 2012. A copy of the report can be obtained from the ISBI at 180 North LaSalle Street, Suite 2015, Chicago, Illinois 60601.

## 5. Administrative Expenses

A summary of the administrative expenses for the Judges' Retirement System for fiscal years 2012 and 2011 are listed below.

### Administrative expenses for fiscal years 2012 and 2011

|  | 2012                    | 2011                    |
|--|-------------------------|-------------------------|
| Personal services                                  | \$366,182               | \$306,465               |
| Employee retirement contributions paid by employer | 6,582                   | 7,769                   |
| Employer retirement contributions                  | 125,275                 | 85,811                  |
| Social security contributions                      | 27,118                  | 22,786                  |
| Group insurance                                    | 83,480                  | 57,549                  |
| Contractual services                               | 127,216                 | 115,903                 |
| Travel   | 3,585                   | 4,514                   |
| Printing   | 3,025                   | 3,555                   |
| Commodities  | 713                     | 752                     |
| Telecommunications                                 | 2,705                   | 2,696                   |
| Information technology                             | 8,367                   | 5,446                   |
| Automotive   | 2,871                   | 1,979                   |
| Depreciation                                       | 1,766                   | 922                     |
| Change in accrued compensated absences             | 5,064                   | 5,898                   |
| Loss on disposal of equipment                      | 141                     | -                       |
| <b>Total</b>                                       | <b><u>\$764,090</u></b> | <b><u>\$622,045</u></b> |

## 6. Funding - Statutory Contributions Required & Contributions Made

On an annual basis, a valuation of the liabilities and reserves of the System is performed by the System's actuarial consultants in order to determine the amount of contributions statutorily required from the State of Illinois. For fiscal years 2012 and 2011, the actuary used the projected unit credit actuarial method for determining the proper employer contribution amount.

For fiscal years 2012 and 2011, the required employer contribution was computed in accordance with the State's funding plan. This funding legislation provides for a systematic 50-year funding plan with an ultimate goal to fund the cost of maintaining and administering the System at an actuarial funded ratio of 90%.

In addition, the funding plan provides for a 15 year phase-in period to allow the state to adapt to the increased financial commitment. Since the 15-year phase-in period ended June 30 2010, the state's contribution will remain at a level percentage of payroll for the next 35 years until the 90% funded level is achieved.

The total amount of statutorily required employer contributions for fiscal years 2012 and 2011 was \$63,628,000 and \$62,377,000, respectively. The total amount of employer contributions received from the state during fiscal years 2012 and 2011 was \$63,628,000 and \$62,428,783, respectively.

The schedule of funding progress, presented as required supplementary information (RSI) following the notes to the financial statements, presents multiyear trend information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the AALs for benefits.

The funded status of the System as of June 30, 2012, the most recent actuarial valuation date, is listed below:

| Actuarial<br>Value of<br>Assets<br>(a) | Actuarial Accrued<br>Liability (AAL)<br>Projected Unit<br>Credit (b) | Unfunded<br>AAL<br>(UAAL)<br>(b-a) | Funded<br>Ratio<br>(a/b) | Covered<br>Payroll<br>(c) | UAAL as a<br>Percentage of<br>Covered Payroll<br>([(b-a)/c]) |
|--|--|------------------------------------|--------------------------|---------------------------|--|
| \$601,219,999                          | \$2,021,715,796  | \$1,420,495,797                    | 29.7%                    | \$171,498,000             | 828.3%   |

Additional information on the latest actuarial valuation is as follows.

|   |  |
|---|--|
| Valuation date: June 30, 2012   |  |
| Actuarial cost method: Projected Unit Credit  |  |
| Amortization method:  |  |
| a.  | For GASB Statement No. 25 reporting purposes: Level percent of payroll   |
| b.  | Per state statute: 15-year phase-in to a level percent of payroll until a 90% funding level is achieved  |
| Remaining amortization period:  |  |
| a.  | For GASB Statement No. 25 reporting purposes: 30 years, open   |
| b.  | Per state statute: 33 years, closed  |
| Asset valuation method:   |  |
| Fair value, adjusted for any actuarial gains or losses from investment return incurred in the fiscal year recognized in equal amounts over the five year period following that fiscal year. |  |
| Actuarial assumptions:  |  |
| Investment rate of return:  | 7.0 percent per year, compounded annually  |
| Projected salary increases:   | 4.0 percent per year (consisting of an inflation component of 3.0% per year and a seniority/ merit component of 1.0% per year), compounded annually                        |
| Assumed inflation rate:   | 3.0 percent  |
| Group size growth rate:   | 0.0 percent  |
| Post-retirement increase:   | Tier 1: 3.0 percent per year, compounded annually<br>Tier 2: 3.0 percent per year or the annual change in the Consumer Price Index, whichever is less, compounded annually |
| Mortality Rates:  |  |
| Active and retired members: The UP-1994 Mortality Table for Males, rated down 3 years.  |  |
| Survivors: The UP-1994 Mortality Table for Females, rated down 2 years.   |  |

## 7. Pension Plan & Other Post-Employment Benefits

**Plan Description.** All of the System's full-time employees who are not eligible for participation in another state-sponsored retirement plan participate in the State Employees' Retirement System (SERS), which is a pension trust fund in the State of Illinois reporting entity.

The SERS is a single-employer defined benefit public employee retirement system (PERS) in which state employees participate, except those covered by the State Universities, Teachers', General Assembly, and Judges' Retirement Systems.

The financial position and results of operations of the SERS for fiscal years 2012 and 2011 are included in the State of Illinois' Comprehensive Annual Financial Report (CAFR) for the years ended June 30, 2012 and 2011, respectively. The SERS also issues a separate CAFR that may be obtained by writing to the SERS, 2101 South Veterans Parkway, Springfield, Illinois, 62794-9255 or by calling 217-785-7202.

The State of Illinois' CAFR may be obtained by writing to the State Comptroller's Office, Financial Reporting Department, 325 West Adams St., Springfield, Illinois, 62704-1858 or by calling 217-782-2053.

A summary of SERS' benefit provisions, changes in benefit provisions, employee eligibility requirements including eligibility for vesting, and the authority under which benefit provisions are established, are included as an integral part of the SERS' CAFR. Also included is a discussion of employer and employee obligations to contribute, and the authority under which those obligations are established.

**Funding Policy.** The System pays employer retirement contributions based upon an actuarially determined percentage of its payrolls. For fiscal years 2012, 2011, and 2010 the employer contribution rates were 34.190%, 27.988%, and 28.377%, respectively. The System's contributions to SERS for fiscal years 2012, 2011, and 2010 were \$125,275, \$85,811, and \$79,061, respectively, and were equal to the required contributions for each fiscal year.

**Other Post-Employment Benefits.** The State provides health, dental, vision, and life insurance benefits for retirees and their dependents in a program administered by the Department of Healthcare and Family Services along with the Department of Central Management Services. Substantially all State employees become eligible for post-employment

benefits if they eventually become annuitants of one of the State sponsored pension plans. Health, dental, and vision benefits include basic benefits for annuitants and dependents under the State's self-insurance plan and insurance contracts currently in force. Annuitants may be required to contribute towards health, dental, and vision benefits with the amount based on factors such as date of retirement, years of credited service with the State, whether the annuitant is covered by Medicare, and whether the annuitant has chosen a managed health care plan. Annuitants who retired prior to January 1, 1998, and who are vested in the State Employee's Retirement System do not contribute towards health, dental, and vision benefits. For annuitants who retired on or after January 1, 1998, the annuitant's contribution amount is reduced five percent for each year of credited service with the State allowing those annuitants with twenty or more years of credited service to not have to contribute towards health, dental, and vision benefits.

However, Public Act 97-0695, effective June 30, 2012, alters the contributions to be paid by the State, annuitants, survivors and retired employees under the State Employees Group Insurance Act. This Act requires the Director of Central Management Services to, on an annual basis, determine the amount that the State should contribute. The remainder of the cost of coverage shall be the responsibility of the annuitant, survivor or retired

employee. Annuitants also receive life insurance coverage equal to the annual salary of the last day of employment until age 60, at which time the benefit becomes \$5,000.

The State pays the System's portion of employer costs for the benefits provided. The total cost of the State's portion of health, dental, vision, and life insurance benefits of all members, including post-employment health, dental, vision, and life insurance benefits, is recognized as an expenditure by the State in the Illinois Comprehensive Annual Financial Report. The State finances the costs on a pay-as-you-go basis. The total costs incurred for health, dental, vision, and life insurance benefits are not separated by department or component unit for annuitants and their dependents nor active employees and their dependents.

A summary of post-employment benefit provisions, changes in benefit provisions, employee eligibility requirements including eligibility for vesting, and the authority under which benefit provisions are established are included as an integral part of the financial statements of the Department of Healthcare and Family Services. A copy of the financial statements of the Department of Healthcare and Family Services may be obtained by writing to the Department of Healthcare and Family Services, 201 South Grand Ave., Springfield, Illinois, 62763-3838.

**8. Analysis of Changes in Reserve Balances**

The funded statutory reserves of the Judges' Retirement System are composed of the following:

**a. Reserve for Participants' Contributions**

This reserve consists of participants' accumulated contributions for retirement annuities, survivors' annuities and automatic annual increases.

**b. Reserve for Future Operations**

This reserve is the balance remaining in the Judges' Retirement System from State of Illinois contributions and revenue from investments after consideration of charges for payouts by the Judges' Retirement System.

**9. Accrued Compensation Absences**

Employees of the Judges' Retirement System are entitled to receive compensation for all accrued but unused vacation time and one-half of all unused sick leave earned after December 31, 1983 and prior to January 1, 1998 upon termination of employment. These accrued compensated absences as of June 30, 2012 and 2011 total \$59,615 and \$54,551, respectively and are included in administrative expenses payable.

**Statements of Changes in Reserve Balances  
Years Ended June 30, 2012 and 2011**

|  | Participants'<br>Contributions | Future<br>Operations  | Total<br>Reserve<br>Balances |
|--|--------------------------------|-----------------------|------------------------------|
| Balance at June 30, 2010   | \$ 166,360,698                 | \$ 356,915,454        | \$ 523,276,152               |
| Add (deduct):  |                                |                       |                              |
| Excess of revenues over expenses   | 16,338,675                     | 66,345,381            | 82,684,056                   |
| Reserve transfers:   |                                |                       |                              |
| Accumulated contributions of participants<br>who retired or died with eligible<br>survivor during the year | <u>(15,131,713)</u>            | <u>15,131,713</u>     | <u>-</u>                     |
| Balance at June 30, 2011   | \$ 167,567,660                 | \$ 438,392,548        | \$ 605,960,208               |
| Add (deduct):  |                                |                       |                              |
| Excess of revenues over (under) expenses   | 15,858,341                     | (43,842,182)          | (27,983,841)                 |
| Reserve transfers:   |                                |                       |                              |
| Accumulated contributions of participants<br>who retired or died with eligible<br>survivor during the year | <u>(5,879,351)</u>             | <u>5,879,351</u>      | <u>-</u>                     |
| Balance at June 30, 2012   | <u>\$ 177,546,650</u>          | <u>\$ 400,429,717</u> | <u>\$ 577,976,367</u>        |

### 10. Equipment

Capital assets over \$100 are capitalized at their cost at the time of acquisition. Depreciation is computed using the straight-line method over the estimated useful life of the asset. The estimated useful lives are as follows: (1) office furniture - 10 years, (2) equipment - 6 years, and (3) certain electronic data processing equipment - 3 years.

### 11. New Accounting Pronouncement

GASB Statement No. 67, "Financial Reporting for Pension Plans", was established to provide improved financial reporting by state and local governmental pension plans. The scope of the Statement addresses accounting and financial reporting for the activities of pension plans that are administered through trusts that have the specific characteristics. For defined benefit pension plans, the Statement establishes stan-

Summary of the changes in equipment for fiscal years 2012 and 2011

|                          | Beginning Balance | 2012            |                 | Ending Balance  |
|--------------------------|-------------------|-----------------|-----------------|-----------------|
|                          |                   | Additions       | Deletions       |                 |
| Equipment                | \$ 30,838         | \$ 7,856        | \$ (9,399)      | \$ 29,295       |
| Accumulated depreciation | (27,461)          | (1,766)         | 9,258           | (19,969)        |
| Equipment, net           | <u>\$ 3,377</u>   | <u>\$ 6,090</u> | <u>\$ (141)</u> | <u>\$ 9,326</u> |
|                          |                   | 2011            |                 |                 |
|                          | Beginning Balance | Additions       | Deletions       | Ending Balance  |
| Equipment                | \$ 33,468         | \$ 458          | \$ (3,088)      | \$ 30,838       |
| Accumulated depreciation | (29,627)          | (922)           | 3,088           | (27,461)        |
| Equipment, net           | <u>\$ 3,841</u>   | <u>\$ (464)</u> | <u>\$ -</u>     | <u>\$ 3,377</u> |

dards of financial reporting for separately issued financial reports and specifies the required approach to measuring the pension liability for benefits provided through the pension plan. The System is required to implement this Statement for the year ending June 30, 2014.

# REQUIRED SUPPLEMENTARY INFORMATION

## SCHEDULE OF FUNDING PROGRESS

| Actuarial Valuation Date | Actuarial Value of Assets * (a) | Actuarial Accrued Liability (AAL) Projected Unit Credit (b) | Unfunded AAL (UAAL) (b-a) | Funded Ratio (a/b) | Covered Payroll (c) | UAAL as a Percentage of Covered Payroll ([b-a]/c) |
|--------------------------|---------------------------------|---|---------------------------|--------------------|---------------------|---|
| 6/30/07                  | \$670,090,950                   | \$1,385,339,573   | \$715,248,623             | 48.4%              | \$142,900,000       | 500.5%  |
| 6/30/08                  | 612,680,574                     | 1,457,336,054   | 844,655,480               | 42.0               | 143,700,000         | 587.8   |
| 6/30/09                  | 616,849,071                     | 1,548,509,535   | 931,660,464               | 39.8               | 155,645,000         | 598.6   |
| 6/30/10                  | 619,925,786                     | 1,819,447,826   | 1,199,522,040             | 34.1               | 161,164,000         | 744.3   |
| 6/30/11                  | 614,596,203                     | 1,952,539,400   | 1,337,943,197             | 31.5               | 169,155,000         | 791.0   |
| 6/30/12                  | 601,219,999                     | 2,021,715,796   | 1,420,495,797             | 29.7               | 171,498,000         | 828.3   |

\* For fiscal years prior to 2009, the actuarial value of assets was equal to the fair value of assets. Beginning in fiscal year 2009, the actuarial value of assets was equal to the fair value of assets adjusted for any actuarial gains or losses from investment return incurred in the fiscal year recognized in equal amounts over the five year period following that fiscal year.

## SCHEDULE OF EMPLOYER CONTRIBUTIONS

| Year Ended June 30 | Annual Required Contribution per GASB Statement No. 25 | Percentage Contributed | Annual Required Contribution per State Statute | Percentage Contributed |
|--------------------|--|------------------------|--|------------------------|
| 2007               | \$ 73,371,653  | 48.0%                  | \$ 35,236,800                                  | 100.0%                 |
| 2008               | 75,134,070   | 62.4                   | 46,872,500                                     | 100.0                  |
| 2009               | 78,386,597   | 76.5                   | 59,983,000                                     | 100.0                  |
| 2010               | 86,916,418   | 90.3                   | 78,832,000                                     | 99.6                   |
| 2011               | 95,490,182   | 65.4                   | 62,377,000                                     | 100.1                  |
| 2012               | 110,923,357  | 57.4                   | 63,628,000                                     | 100.0                  |

### Notes to Required Supplementary Information

Valuation date: June 30, 2012

Actuarial cost method: Projected Unit Credit

Amortization method:

- a. For GASB Statement No. 25 reporting purposes: Level percent of payroll
- b. Per state statute: 15-year phase-in to a level percent of payroll until a 90% funding level is achieved

Remaining amortization period:

- a. For GASB Statement No. 25 reporting purposes: 30 years, open
- b. Per state statute: 33 years, closed

Asset valuation method: Fair value, adjusted for any actuarial gains or losses from investment return incurred in the fiscal year recognized in equal amounts over the five year period following that fiscal year.

Actuarial assumptions:

Investment rate of return: 7.0 percent per year, compounded annually

Projected salary increases: 4.0 percent per year (consisting of an inflation component of 3.0% per year and a seniority/ merit component of 1.0% per year), compounded annually

Assumed inflation rate: 3.0 percent

Group size growth rate: 0.0 percent

Post-retirement increase: Tier 1: 3.0 percent per year, compounded annually  
Tier 2: 3.0 percent per year or the annual change in the Consumer Price Index, whichever is less, compounded annually

Mortality Rates:

Active and retired members: The UP-1994 Mortality Table for Males, rated down 3 years.

Survivors: The UP-1994 Mortality Table for Females, rated down 2 years.

SUPPLEMENTARY FINANCIAL INFORMATION

SUMMARY OF REVENUES BY SOURCE

Years Ended June 30, 2012 and 2011

|   | 2012                 | 2011                  |
|---|----------------------|-----------------------|
| Contributions:  |                      |                       |
| Participants:   |                      |                       |
| Participants  | \$ 16,305,260        | \$ 16,428,912         |
| Interest paid by participants                                   | 63,644               | 217,575               |
| Receipts from reciprocal systems                                | 75,892               | -                     |
| Repayment of refunds  | -                    | 78,704                |
| Total participant contributions                                 | <u>16,444,796</u>    | <u>16,725,191</u>     |
| Employer:   |                      |                       |
| Pension Contribution Fund                                       | -                    | 47,386,951            |
| General Revenue Fund  | 63,628,000           | 15,041,832            |
| Received from reciprocal systems                                | 16,099               | -                     |
| Paid by participants  | -                    | 265,677               |
| Total employer contributions                                    | <u>63,644,099</u>    | <u>62,694,460</u>     |
| Total contributions revenue                                     | <u>80,088,895</u>    | <u>79,419,651</u>     |
| Investments:  |                      |                       |
| Net investment income   | 13,408,141           | 12,025,283            |
| Interest earned on cash balances                                | 86,203               | 109,280               |
| Net appreciation (depreciation) in<br>fair value of investments | <u>(13,563,440)</u>  | <u>93,118,822</u>     |
| Total investment revenue (loss)                                 | <u>(69,096)</u>      | <u>105,253,385</u>    |
| Other:  |                      |                       |
| Miscellaneous   | -                    | 5,000                 |
| Total revenues  | <u>\$ 80,019,799</u> | <u>\$ 184,678,036</u> |

SCHEDULE OF PAYMENTS TO CONSULTANTS

Years Ended June 30, 2012 and 2011

|                   | 2012             | 2011             |
|-------------------|------------------|------------------|
| Actuary           | \$ 26,000        | \$ 31,000        |
| Audit fees        | 39,932           | 23,994           |
| Legal services    | 2,012            | 2,126            |
| Financial planner | 703              | 1,468            |
| Medical services  | 94               | 199              |
| Total             | <u>\$ 68,741</u> | <u>\$ 58,787</u> |

SUPPLEMENTARY FINANCIAL INFORMATION

SUMMARY SCHEDULE OF CASH RECEIPTS AND DISBURSEMENTS  
Years Ended June 30, 2012 and 2011

|  | 2012                 | 2011                 |
|--|----------------------|----------------------|
| Cash balance, beginning of year                        | \$ 18,015,766        | \$ 16,644,537        |
| Receipts:  |                      |                      |
| Participant contributions                              | 16,312,068           | 16,582,220           |
| Employer contributions:                                |                      |                      |
| Pension Contribution Fund                              | -                    | 47,386,951           |
| General Revenue Fund                                   | 55,674,490           | 15,041,832           |
| Received from reciprocal systems                       | 16,099               | -                    |
| Paid by participants                                   | -                    | 265,677              |
| Interest income on cash balances                       | 90,309               | 114,412              |
| Reimbursements from General Assembly Retirement System | 214,000              | 236,884              |
| Transfers from reciprocal systems                      | 75,892               | -                    |
| Cancellation of annuities, net of overpayments         | 33,538               | 82,924               |
| Cancellation of administrative expenses                | -                    | 5,888                |
| Tax-deferred installment payments                      | 19,010               | 16,261               |
| Repayment of refunds                                   | -                    | 139,470              |
| Transfers from Illinois State Board of Investment      | 28,500,000           | 71,200,000           |
| Miscellaneous  | 100                  | 5,345                |
| Total cash receipts                                    | <u>100,935,506</u>   | <u>151,077,864</u>   |
| Disbursements:   |                      |                      |
| Benefit payments:                                      |                      |                      |
| Temporary disability                                   | -                    | 72,613               |
| Retirement annuities                                   | 87,184,592           | 82,140,890           |
| Survivors' annuities                                   | 19,499,251           | 18,571,448           |
| Refunds  | 586,981              | 686,156              |
| Transfer to Illinois State Board of Investment         | -                    | 47,386,951           |
| Administrative expenses                                | 989,813              | 848,577              |
| Total cash disbursements                               | <u>108,260,637</u>   | <u>149,706,635</u>   |
| Cash balance, end of year                              | <u>\$ 10,690,635</u> | <u>\$ 18,015,766</u> |

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# INVESTMENT SECTION

### INVESTMENT REPORT

By state law, the System's investment function is managed by the Illinois State Board of Investment (ISBI). The ISBI was created in 1969 to provide a means of centralizing the investment management function for public employee pension funds and retirement systems operating in the state.

In addition to the assets of the Judges' Retirement System, the ISBI also manages the investment function for the General Assembly and State Employees' Retirement Systems. All ISBI investments are accounted for in a commingled fund (ISBI Fund).

As of June 30, 2012, total net assets under management valued at market, amounted to \$11.284 billion. Of the total market value of assets under management, \$559.1 million or approximately 5% represented assets of the Judges' Retirement System.

A summary of the portfolio's largest holdings, as well as the complete listing of the ISBI portfolio, are included in the ISBI Annual Report. A schedule of fees and commissions paid by brokerage firms and a listing of transactions executed, including transaction value, are also contained in the ISBI Annual Report. The following investment information and analysis has been prepared from information provided by the ISBI. Investment performance returns are prepared by State Street Bank. Investment activities are presented on a trade date basis and measurements are calculated using time weighted rates of return consistent with investment industry standards.

### INVESTMENT POLICY

The ISBI operates under a strategic investment policy. The investment objective of the total portfolio is to maximize the rate of return on investments within a prudent level of risk. To achieve this objective, the ISBI invests in different types of assets and uses multiple managers to ensure diversification.

### EMERGING & MINORITY PARTICIPATION

In accordance with Public Act 96-006, the ISBI Board continues to put forth best efforts to comply with the goals outlined in the ISBI's following policies: the Emerging and Minority Investment Manager and Minority and Illinois Broker Policy, the Fiduciary Diversification Policy, and the Minority Contract/Service Utilization Policy. The aforementioned policies exemplify the ISBI Board's commitment to providing opportunities for

businesses owned by minorities, females and persons with disabilities, as well as increasing the racial, ethnic and gender diversity of its fiduciaries.

As of fiscal year 2012, the ISBI allocated 21.6% of its assets to minority and female-owned firms, of which 10.3% was allocated to emerging firms. 18.0% of ISBI's assets were allocated to minority-owned investment firms, and 4.4% to female-owned investment firms. Some investment firms qualify as both female-owned and minority-owned. Within asset classes, the ISBI has allocated 30.1% of equities, 17.6% of fixed income and 1.4% of alternatives to minority and female-owned firms. Alternatives include allocations to Real Estate funds and Private Equity funds.

The ISBI Board has established a goal of allocating 20% of brokerage commissions to broker dealers owned by females, minorities, or persons with disabilities. Investment firms are required to execute trades directly with disadvantaged broker dealers and are prohibited from utilizing step-outs. During fiscal year 2012, utilization of such broker dealers by the ISBI Board's investment advisers exceeded the Policy goals: approximately 44.9% utilization for domestic equity advisers, 28.9% utilization for fixed income advisers (based on par value) and 28.3% utilization for international equity advisers. The ISBI Board's investment advisers also exceeded the Policy goal to direct 25% of trades to Illinois-based broker/dealers: approximately 51.4% utilization by domestic and international equity advisers and 27.6% utilization by fixed income advisers (based on par value).

In monitoring the utilization of disadvantaged broker dealers, the ISBI has retained a third party transaction cost analysis service provider to ensure the ISBI Board's investment managers operate in a manner consistent with best execution practices.

### ASSET ALLOCATION

The investment policy of the ISBI establishes asset allocation targets and ranges for each asset class, selected to achieve overall risk and return objectives. This policy is implemented by allocations to investment managers with assignments to invest in specific asset classes, with defined security selection styles and methodologies.

The asset allocation policy for fiscal year 2012 is set forth on page 39.

## INVESTMENT SECTION

|                         | Actual Asset Allocation | Policy Target |
|-------------------------|-------------------------|---------------|
| U.S. Equity             | 29%                     | 30%           |
| U.S. Equity Hedge Funds | 9                       | 10            |
| International Equity    | 18                      | 20            |
| Commingled Funds        | 2                       | -             |
| Fixed Income            | 18                      | 17            |
| Bank Loans              | 3                       | 3             |
| Real Estate             | 9                       | 10            |
| Private Equity          | 6                       | 5             |
| Real Assets             | 4                       | 5             |
| Cash                    | 2                       | -             |
| <b>Total</b>            | <b>100%</b>             | <b>100%</b>   |

### U. S. EQUITIES

In fiscal year 2012, the Russell 3000 Index, a broad representation of the U.S. market, was up 3.8%. Growth stocks exceeded value stocks with the Russell 3000 Growth Index up 5.1%, compared to the Russell 3000 Value Index up 2.6%. Large capitalization stocks outperformed small capitalization stocks with the S&P 500 up 5.5%, compared to a negative 2.1% return for the Russell 2000. The ISBI's U.S. equity portfolio was up 1.3% for fiscal year 2012, 2.5% below the Russell 3000. The

### INVESTMENT RESULTS

In fiscal year 2012, investors benefitted from positive returns in U.S. equity, fixed income, real estate and private equity as measured by market indices. The ISBI's total fund was up 0.1% for fiscal year 2012, net of expenses. This follows positive returns of 21.7% and 9.1% for fiscal year 2011 and fiscal year 2010, respectively, with negative returns of 20.1% and 6.2% for fiscal year 2009 and fiscal year 2008, respectively.

The ISBI Board continues to be concerned with the under-performance of specific managers; however, most of the ISBI's current managers have exceeded their individual benchmarks since inception.

portfolio's exposure to small and middle capitalization stocks detracted from overall performance. Through structure analysis, rebalancing and risk management, the domestic equity portfolio continues to track the market with predictable consistency to achieve its objective.

### REAL ESTATE

In fiscal year 2012, the ISBI's Real Estate portfolio earned a return of 5.3%. The NFI-ODCE (NCREIF Fund Index Open-End Diversified Core Equity), a measure of core, leveraged, open-end real estate funds, earned a return of 11.3%. In the last 12 months, the ISBI has rebalanced its portfolio to meet the 80% Core/20% Non-Core real estate strategy.

New investing is planned for fiscal year 2013 as additional capital remains within the core separate accounts. The downturn in the real estate market slowed the separate account investment pace; however, the real estate portfolio is scheduled to be fully funded by end of calendar year 2013. The ISBI's Real Estate portfolio is invested primarily through interests in separate accounts, limited partnerships, trusts, and other forms of pooled investments.

|                          | REAL ESTATE |         |         |
|--------------------------|-------------|---------|---------|
|                          | 1 Year      | 3 Years | 5 Years |
| ISBI                     | 5.3%        | 4.2%    | (4.6)%  |
| NCREIF Real Estate Index | 11.3        | 7.4     | (1.8)   |

### U.S. EQUITIES

|                    | 1 Year | 3 Years | 5 Years |
|--------------------|--------|---------|---------|
| ISBI               | 1.3%   | 16.8%   | 0.8%    |
| Russell 3000 Index | 3.8    | 16.7    | 0.4     |

### INTERNATIONAL EQUITIES

The Morgan Stanley ACWI ex US Index is a broad index of global equities, including emerging markets but excluding the United States. In fiscal year 2012 that index returned a negative 14.4%, or 18.2% below the U.S. index. The ISBI's International Equity portfolio was down 10.7%, 3.7% above the ACWI ex US Index.

### INTERNATIONAL EQUITIES

|                 | 1 Year  | 3 Years | 5 Years |
|-----------------|---------|---------|---------|
| ISBI            | (10.7)% | 10.3%   | (3.1)%  |
| MSCI-EAFE Index | (14.4)  | 7.8     | (4.0)   |

### FIXED INCOME

In fiscal year 2012 the ISBI Fixed Income portfolio had a return of 6.8%, compared to the 7.4% return for the Barclay's Capital Universal Bond Index. Exposure to the lower volatility Government Credit Intermediate sector detracted from the performance of the overall fixed income portfolio.

## FIXED INCOME

|                                  | 1 Year | 3 Years | 5 Years |
|----------------------------------|--------|---------|---------|
| ISBI                             | 6.8%   | 6.0%    | 4.2%    |
| Barclays Capital Universal Index | 7.4    | 7.6     | 6.8     |

## U. S. EQUITY HEDGE FUNDS

The ISBI U.S. Equity Hedge Fund portfolio had a return of negative 4.3% for fiscal year 2012, compared to the negative 10.7% return for the HFRX Equity Hedge Index.

Besides monitoring hedged equity performance, the ISBI Board looked critically at how the hedged equity portfolio is structured and the level of fees paid. The consequence was a higher level of confidence in the existing portfolio structure, and an aggressive re-negotiation of, and reduction in, fees.

Although this process continued through the end of the fiscal year and concluded early in fiscal year 2013, the consequence will constitute total savings exceeding \$5 million annually going forward.

## U.S. EQUITY HEDGE FUNDS

|                   | 1 Year | 3 Years | 5 Years |
|-------------------|--------|---------|---------|
| ISBI              | (4.3)% | 4.1%    | (0.6)%  |
| HFRX Equity Hedge | (10.7) | (1.6)   | (6.3)   |

## PRIVATE EQUITY

In fiscal year 2012, the ISBI's Private Equity portfolio return was 7.6%. On average, the ISBI invests \$100M each year among five to six private equity opportunities.

The Private Equity portfolio consists of interests in limited partnerships and other commingled vehicles that invest in management buyouts, venture capital, and other private placement equity strategy activities. The Private Equity asset class has recovered from previous market disruptions and continues to be one of the best performing asset classes since its inception date. Although the asset class is recovering, in fiscal year 2012, the ISBI's portfolio did not keep up with the portfolio benchmark return of 9.5%.

## INVESTMENT SECTION

### ADMINISTRATIVE EXPENSES

The ISBI's total expenses for fiscal year 2012, based on \$11.3 billion in total assets, were \$36.4 million, compared to \$37.2 million based on \$11.5 billion in total assets for fiscal year 2011. The resulting expense ratio (expenses divided by average fair value of assets) was .33% for fiscal year 2012, as compared to .35%

for fiscal year 2011. Decreased aggregate expenses in fiscal year 2012 were mainly a result of reduced fees paid to investment managers. The ISBI's fees paid to investment advisory firms are aggressively managed which has contributed to the reduction in the cost of investment advisory services.

### INVESTMENT PORTFOLIO SUMMARY

|                                      | June 30, 2012            |               | June 30, 2011            |                |
|--------------------------------------|--------------------------|---------------|--------------------------|----------------|
| Investments, at fair value           |                          |               |                          |                |
| U.S. Govt. and Agency Obligations    | \$ 958,131,279           | 8.49%         | \$ 1,367,098,751         | 11.86%         |
| Foreign Obligations                  | 385,628,617              | 3.42          | 37,951,769               | 0.33           |
| Corporate Obligations                | 656,977,663              | 5.82          | 762,833,382              | 6.62           |
| Domestic Common Stock & Equity Funds | 3,253,103,566            | 28.83         | 3,380,198,858            | 29.32          |
| Commingled Funds                     | 225,608,712              | 2.00          | 256,817,374              | 2.23           |
| Foreign Equity Securities            | 2,012,774,573            | 17.84         | 2,195,201,185            | 19.04          |
| Foreign Preferred Stock              | 592,156                  | 0.01          | 40,032                   | 0.00           |
| Hedge Funds                          | 1,026,725,785            | 9.10          | 1,075,584,754            | 9.33           |
| Real Estate Funds                    | 967,346,450              | 8.57          | 780,336,465              | 6.77           |
| Private Equity                       | 679,423,383              | 6.02          | 629,256,286              | 5.46           |
| Money Market Instruments             | 255,922,180              | 2.27          | 303,501,465              | 2.63           |
| Real Assets                          | 507,019,665              | 4.49          | 455,984,316              | 3.96           |
| Bank Loans                           | 328,593,596              | 2.91          | 253,447,070              | 2.20           |
| Foreign Currency Forward Contracts   | (43,859)                 | 0.00          | (353)                    | 0.00           |
|                                      | <u>11,257,803,766</u>    | <u>99.77</u>  | <u>11,498,251,354</u>    | <u>99.75</u>   |
| Other Assets, Less Liabilities       | 26,132,919               | .23           | 29,373,670               | 0.25           |
| Net Assets, at Fair Value            | <u>\$ 11,283,936,685</u> | <u>100.0%</u> | <u>\$ 11,527,625,024</u> | <u>100.00%</u> |

## INVESTMENT SECTION

### ANALYSIS OF INVESTMENT PERFORMANCE

|  | 2012   | 2011  | 2010  | 2009    | 2008    |
|--|--------|-------|-------|---------|---------|
| Total Return* - Past 3 years   | 10.0%  |       |       |         |         |
| Total Return* - Past 5 years   | (0.1)% |       |       |         |         |
| Total Return* - year by year   | 0.1%   | 21.7% | 9.1%  | (20.1)% | (6.2)%  |
| System's Actuarial Assumed Rate of Return  | 7.0%   |       | 8.0%  |         |         |
| Comparative rates of return on fixed income securities   |        |       |       |         |         |
| Total fixed income - ISBI  | 6.8%   | 5.7%  | 5.5%  | (2.4)%  | 5.3%    |
| Comparison index:  |        |       |       |         |         |
| Barclays Capital Universal Index   | 7.4%   | 4.8%  | 10.6% | 4.9%    | 6.2%    |
| Comparative rates of return on equities  |        |       |       |         |         |
| U.S. equities - ISBI   | 1.3%   | 33.9% | 17.3% | (25.1)% | (12.7)% |
| Comparison index:  |        |       |       |         |         |
| Russell 3000 Index   | 3.8%   | 32.4% | 15.7% | (26.6)% | (12.5)% |
| State Street Bank and Trust, the ISBI's master custodian, provides performance rates of return by portfolio, portfolio aggregation and the respective indices. |        |       |       |         |         |
| Time weighted methodology, based upon market values, is used when calculating performance.   |        |       |       |         |         |
| * Total return is the combined effect of income earned and market appreciation (depreciation).   |        |       |       |         |         |

### ADDITIONAL INVESTMENT INFORMATION

The following table shows a comparison of ISBI investment operations of the System for fiscal years 2012 and 2011:

|                                       | 2012           | 2011           | Increase/(Decrease) |            |
|---------------------------------------|----------------|----------------|---------------------|------------|
|                                       |                |                | Amount              | Percentage |
| Balance at beginning of year,         |                |                |                     |            |
| at fair value                         | \$ 587,794,578 | \$ 506,463,522 | \$ 81,331,056       | 16.1%      |
| Cash transferred (from) ISBI, net     | (28,500,000)   | (23,813,049)   | (4,686,951)         | (19.7)     |
| Net ISBI investment revenue:          |                |                |                     |            |
| ISBI Commingled Fund income           | 15,223,558     | 13,926,694     | 1,296,864           | 9.3        |
| Less ISBI expenses                    | (1,815,417)    | (1,901,411)    | 85,994              | 4.5        |
| Net ISBI investment income            | 13,408,141     | 12,025,283     | 1,382,858           | 11.5       |
| Net apprec/deprec in fair value       |                |                |                     |            |
| of ISBI investments                   | (13,563,440)   | 93,118,822     | (106,682,262)       | (114.6)    |
| Net ISBI investment revenue           | (155,299)      | 105,144,105    | (105,299,404)       | (100.1)    |
| Balance at end of year, at fair value | \$ 559,139,279 | \$ 587,794,578 | \$ (28,655,299)     | (4.9)%     |

In addition, interest on the average balance in the System's cash account in the State Treasury for FY 2012 was \$86,203 compared to \$109,280 during FY 2011.

# ACTUARIAL SECTION



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October 26, 2012

Board of Trustees and Executive Secretary  
Judges' Retirement System of Illinois  
P. O. Box 19255  
2101 S. Veterans Parkway  
Springfield, Illinois 62794-9255

**CONFIDENTIAL**

**Re: Actuarial Certification**

At your request, we have performed the annual actuarial valuation of the assets and liabilities of the Judges' Retirement System of Illinois ("JRS") as of June 30, 2012. This valuation has been performed to measure the funding status of the System and determine the employer statutory contribution rate for the year beginning July 1, 2013, and ending June 30, 2014. In addition, it includes disclosure information required under GASB Statement No. 25 and Statement No. 27.

The required statutory contribution rate has been determined under the Projected Unit Credit Cost Method, providing for a 90 percent funding of total actuarial liabilities by fiscal year 2045 as required by 40 ILCS Section 5/18-131(c). Contribution rates are determined according to P.A. 93-0589 reflecting the infusion of the proceeds from the sale of general obligation bonds. The contribution rates reflect the impact of P.A. 96-0889, which created a second tier for future members of JRS hired after December 31, 2010.

The required statutory contribution rates and amounts for fiscal year beginning July 1, 2013, as determined in the June 30, 2012, actuarial valuation are shown below.

|                       | <b>Total</b> |
|-----------------------|--------------|
| Required Rate         | 74.091%      |
| Required Contribution | 126,808,000  |

The system's current funding plan satisfies the requirements for amortizing the unfunded liability provided under GASB Statement No. 25 for the fiscal year ending June 30, 2014. The assumptions and methods used to develop the normal cost and actuarial accrued liability meet the requirements of GASB Statement No. 25.

Pursuant to P.A. 96-0043, for purposes of determining statutory contribution rates for fiscal year 2013 an actuarial value of the System's assets was used. The actuarial value of assets is assumed to earn a rate of return equal to the System's actuarially assumed rate of return. The liabilities have been valued based on financial and employee data, which is supplied by the administrative staff of the System and verified by the System's auditor. We did not audit this data, but have reviewed the statistical support and concluded that the data is reasonable and consistent with the prior year's data.

**Gabriel Roeder Smith & Company**

# ACTUARY'S CERTIFICATION LETTER

Board of Trustees and Executive Secretary  
October 26, 2012  
Page 2

For the actuarial valuation as of June 30, 2012, the assumed rate of return used to discount liabilities and project assets was 7.0 percent.

In our opinion, the calculations also comply with the requirements of Illinois state law and, where applicable, the Internal Revenue Code, ERISA, and the Statements of the Governmental Accounting Standards Board except as noted above. All of our work conforms with generally accepted actuarial principles and practices, and to the Actuarial Standards of Practice issued by the Actuarial Standards Board.

We certify that the information presented herein is accurate and fairly portrays the actuarial position of JRS as of June 30, 2012. We prepared the accompanying Summary of Actuarial Cost Method and Major Actuarial Assumptions, but the JRS staff prepared the other supporting schedules in this section and the trend tables in the financial section, based on information supplied in our report.

The undersigned are Members of the American Academy of Actuaries (MAAA) as indicated, and meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion contained herein.

Respectfully submitted,

**Gabriel, Roeder, Smith & Company**

By:   
Alex Rivera, FSA, EA, MAAA  
Senior Consultant

By:   
David Kausch, FSA, EA, MAAA  
Senior Consultant

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**Gabriel Roeder Smith & Company**

## INTRODUCTION

Annually, the System's actuarial consultants perform a valuation of the liabilities and reserves of the System in order to make a determination of the amount of contributions required from the state. These results are then certified to the Board.

The Board, in turn, has the duty of certifying an employer contribution amount, required to be paid to the System by the state during the succeeding fiscal year.

The employers' contribution amount, together with participants' contributions, income from investments and any other income received by the System, shall be sufficient to meet the cost of maintaining and administering the System on a funded basis in accordance with actuarial requirements, pursuant to Chapter 40, Section 5/18-131 of the Illinois Compiled Statutes.

In August, 1994, Senate Bill 533 was signed into law as Public Act 88-0593. This funding legislation, which became effective July 1, 1995, provides that:

- For fiscal years 1996 through 2010, the contribution to the System, as a percentage of the payroll, shall be increased in equal annual increments so that by fiscal year 2010 the contribution rate is at the same level as the contribution rate for fiscal years 2011 through 2045.
- For fiscal years 2011 through 2045, the minimum contribution to the System for each fiscal year shall be an amount determined to be sufficient to bring the total actuarial value of assets of the System up to 90% of the total actuarial liabilities of the System by the end of fiscal year 2045. In making these determinations, the required contribution shall be calculated each year as a level percentage of payroll over the years remaining to and including fiscal year 2045 and shall be determined under the projected unit credit actuarial cost method.
- Beginning in fiscal year 2045, the minimum contribution to the System for each fiscal year shall be the amount needed to maintain the total actuarial value of assets of the System at 90% of the total actuarial liabilities of the System.

The funding legislation also provides for the establishment of a continuing appropriation of the required state contributions to the System. This has, in effect, removed the appropriation of these funds from the annual budgetary process.

The amortization period required by the state's funding plan, as described above, meets the parameters of GASB Statement No. 25.

In April, 2003, House Bill 2660 was signed into law as Public Act 93-0002. This legislation authorized the sale of \$10 billion of General Obligation bonds for the purpose of making contributions to the five state-financed retirement systems. This legislation also modified the funding plan by mandating that, beginning in fiscal year 2005, the required state contribution for each fiscal year not exceed the state contributions that would have been required had the General Obligation bond program not been in effect, reduced by the total debt service for each year for the System's portion of the General Obligation bond proceeds.

In June, 2005, Senate Bill 0027 was signed into law as Public Act 94-0004. This legislation further modified the funding plan by reducing the amount of required employer contributions for fiscal years 2006 and 2007 that would have otherwise been required under Public Act 88-0593, as modified by Public Act 93-0002. The required state contributions for fiscal years 2008 through 2010 were then to be increased incrementally as a percentage of the participant payroll so that by fiscal year 2011 the state would be contributing at the required level contribution rate to achieve the financing objective of a 90% funded status by the end of fiscal year 2045.

The total amount of statutorily required employer contributions for fiscal years 2012 and 2011 was \$63,628,000 and \$62,377,000, respectively. The total amount of employer contributions received from the state during fiscal years 2012 and 2011 was \$63,628,000 and \$62,428,783, respectively.

## ACTUARIAL COST METHOD AND SUMMARY OF MAJOR ACTUARIAL ASSUMPTIONS

The System utilizes the projected unit credit actuarial cost method. Under this method, the actuarial liability is the actuarial present value or that portion of a participant's projected benefit that is attributable to service to date on the basis of future compensation projected to retirement. The normal cost represents the actuarial present value of the participant's projected benefit that is attributable to service in the current year, again based on future compensation projected to retirement.

Actuarial gains and losses are recognized in the unfunded actuarial liability of the System. However, for purposes of determining future employer contributions, the actuarial gains and losses are amortized in accordance with the funding plan as previously described.

## ACTUARIAL SECTION

A description of the actuarial assumptions utilized for fiscal years 2012 and 2011 follows:

**Dates of Adoption:** The Projected Unit Credit Actuarial Cost Method was adopted June 30, 1987; the interest rate assumption was adopted June 30, 2010; all other assumptions were adopted June 30, 2011.

**Asset Valuation Method:** The actuarial value of assets is equal to the fair value of assets adjusted for any actuarial gains or losses from investment return incurred in the fiscal year recognized in equal amounts over the five year period following that fiscal year.

**Mortality Rates:** Active and retired members: The UP-1994 Mortality Table for Males, rated down 3 years. Survivors: The UP-1994 Mortality Table for Females, rated down 2 years. No adjustment is made for post-disabled mortality. The mortality table used is a static table with no provision for future mortality improvement.

**Salary Increase:** A salary increase assumption of 4.0% per year (consisting of an inflation component of 3.0% per year and a seniority/merit component of 1.0% per year), compounded annually, was used. In determining total covered payroll, the size of the active group is assumed to remain constant.

**Interest Rate:** An interest rate assumption of 7.0% per year compounded annually, was used.

**Marital Status:** It was assumed that 75% of active participants are married. Actual marital status at benefit commencement is used for retirees.

**Spouse's Age:** The age of the spouse was assumed to be 4 years younger than the age of the participant/retiree.

**Termination Rates:** Termination rates based on the recent experience of the System were used. Above is a sample of the termination rates that were used:

| Age | Rate of Termination | Age | Rate of Termination |
|-----|---------------------|-----|---------------------|
| 30  | .0128               | 50  | .0058               |
| 35  | .0110               | 55  | .0042               |
| 40  | .0094               | 60  | .0024               |
| 45  | .0076               | 65  | .0007               |

It is assumed that terminated participants will not be rehired. The rates apply only to participants who have not fulfilled the service requirement necessary for retirement at any given age.

**Disability Rates:** Disability rates based on the recent experience of the System as well as on published disability rate tables were used. The following is a sample of the disability rates that were used:

| Age | Rate of Disability | Age | Rate of Disability |
|-----|--------------------|-----|--------------------|
| 30  | .00057             | 45  | .00115             |
| 35  | .00064             | 50  | .00170             |
| 40  | .00083             | 55  | .00000             |

**Retirement Rates:** Tier 1 rates of retirement for each age from 55 to 80 and Tier 2 rates of retirement for each age from 62 to 80 based on the recent experience of the System were used. The following are samples of the rates of retirement that were used:

| Tier 1 |                    | Tier 2 |                    |
|--------|--------------------|--------|--------------------|
| Age    | Rate of Retirement | Age    | Rate of Retirement |
| 55     | .080               | 62     | .300               |
| 60     | .220               | 65     | .160               |
| 65     | .110               | 67     | .300               |
| 70     | .110               | 70     | .120               |
| 75     | .200               | 75     | .200               |
| 80     | 1.000              | 80     | 1.000              |

The above retirement rates are equivalent to an average retirement age of 62.6 for Tier 1 and 67.6 for Tier 2.

**Experience Review:** Pursuant to state law, the System had the actuary's perform this review for the five year period ended June 30, 2010, which was updated for values as of June 30, 2011.

**NOTE:** The System retained the services of a new actuary for the fiscal year ended June 30, 2012. The actuarial assumptions have been recommended by the actuary and adopted by the System's Board of Trustees, at the dates indicated previously.

### SCHEDULE OF RETIRANTS AND SURVIVORS' ANNUITANTS ADDED TO AND REMOVED FROM ROLLS

| Fiscal Year | Annuitants |           |           |        | Survivors |           |           |        | Total |
|-------------|------------|-----------|-----------|--------|-----------|-----------|-----------|--------|-------|
|             | Beginning  | Additions | Deletions | Ending | Beginning | Additions | Deletions | Ending |       |
| 2003        | 517        | 51        | 29        | 539    | 321       | 19        | 15        | 325    | 864   |
| 2004        | 539        | 29        | 33        | 535    | 325       | 30        | 17        | 338    | 873   |
| 2005        | 535        | 51        | 24        | 562    | 338       | 24        | 24        | 338    | 900   |
| 2006        | 562        | 41        | 22        | 581    | 338       | 12        | 19        | 331    | 912   |
| 2007        | 581        | 67        | 28        | 620    | 331       | 19        | 24        | 326    | 946   |
| 2008        | 620        | 44        | 40        | 624    | 326       | 31        | 25        | 332    | 956   |
| 2009        | 624        | 60        | 37        | 647    | 332       | 19        | 16        | 335    | 982   |
| 2010        | 647        | 41        | 23        | 665    | 335       | 19        | 20        | 334    | 999   |
| 2011        | 665        | 83        | 28        | 720    | 334       | 14        | 21        | 327    | 1,047 |
| 2012        | 720        | 29        | 24        | 725    | 327       | 20        | 16        | 331    | 1,056 |

## ACTUARIAL SECTION

### SUMMARY OF AND CHANGES TO THE PLAN PROVISIONS

Please refer to the Plan Summary and Legislative Section for a summary of the plan provisions and legislative amendments that were evaluated and considered by the actuary.

### SHORT-TERM SOLVENCY TEST

A short-term solvency test is one means of checking a system's progress under its funding program. In a short-term solvency test, the plan's present assets

(primarily cash and investments) are compared with: 1) active and inactive participant contributions on deposit; 2) the liabilities for future benefits to present retired lives; and 3) the liabilities for service already rendered by active and inactive participants. In a system that has been following level percent of payroll financing, the liabilities for service already rendered by active and inactive participants (liability 3) should be partially covered by the remainder of present assets. If the system continues using level cost financing, the funded portion of liability 3 will increase over time, although it is very rare for a system to have its liability 3 fully funded.

### COMPUTED ACTUARIAL VALUES

| Fiscal Year | Aggregate Accrued Liabilities For                    |  |   |                            | Percentage of Accrued Liabilities Covered By Assets |       |      |
|-------------|--|--|---|----------------------------|---|-------|------|
|             | (1)<br>Active and Inactive Participant Contributions | (2)<br>Retirement and Survivor Annuity | (3)<br>Active and Inactive Participants (Employer Financed Portion) | Actuarial Value of Assets* | (1)   | (2)   | (3)  |
| 2003        | \$ 121,873,715                                       | \$ 607,038,789                         | \$ 347,319,461  | \$ 330,053,560             | 100.0%  | 34.3% | 0.0% |
| 2004        | 130,547,360  | 633,302,100                            | 392,243,491   | 534,579,823                | 100.0   | 63.8  | 0.0  |
| 2005        | 135,440,555  | 690,111,273                            | 410,960,328   | 564,999,447                | 100.0   | 62.2  | 0.0  |
| 2006        | 142,846,641  | 730,339,241                            | 418,208,979   | 599,234,149                | 100.0   | 62.5  | 0.0  |
| 2007        | 145,242,498  | 819,153,160                            | 420,943,915   | 670,090,950                | 100.0   | 64.1  | 0.0  |
| 2008        | 152,455,812  | 856,958,002                            | 447,922,240   | 612,680,574                | 100.0   | 53.7  | 0.0  |
| 2009        | 157,840,805  | 934,047,891                            | 456,620,839   | 616,849,071                | 100.0   | 49.1  | 0.0  |
| 2010        | 166,360,698  | 1,070,374,455                          | 582,712,673   | 619,925,786                | 100.0   | 42.4  | 0.0  |
| 2011        | 167,567,660  | 1,244,264,760                          | 540,706,980   | 614,596,203                | 100.0   | 35.9  | 0.0  |
| 2012        | 177,546,650  | 1,289,080,804                          | 555,088,342   | 601,219,999                | 100.0   | 32.9  | 0.0  |

\* For fiscal years prior to 2009, the actuarial value of assets was equal to the fair value of assets. Beginning in fiscal year 2009, the actuarial value of assets was equal to the fair value of assets adjusted for any actuarial gains or losses from investment return incurred in the fiscal year recognized in equal amounts over the five year period following that fiscal year.

### VALUATION RESULTS

|                                      | June 30, 2012           | June 30, 2011           |
|--------------------------------------|-------------------------|-------------------------|
| Actuarial Liability:                 |                         |                         |
| For Active Participants:             |                         |                         |
| Pension benefits                     | \$ 524,822,298          | \$ 446,333,592          |
| Cost-of-living adjustments           | 175,220,406             | 160,010,745             |
| Death benefits                       | 23,401,757              | -                       |
| Pre-retirement survivors' annuity    | -                       | 35,418,406              |
| Post-retirement survivors' annuity   | -                       | 53,628,273              |
| Withdrawal benefits                  | 1,976,773               | 5,353,553               |
| Disability benefits                  | 1,358,560               | 1,828,530               |
| Total                                | <u>726,779,794</u>      | <u>702,573,099</u>      |
| For Participants Receiving Benefits: |                         |                         |
| Retirement annuities                 | 1,108,702,441           | 1,076,051,387           |
| Survivor annuities                   | 180,378,363             | 168,213,373             |
| Total                                | <u>1,289,080,804</u>    | <u>1,244,264,760</u>    |
| For Inactive Participants            | <u>5,855,198</u>        | <u>5,701,541</u>        |
| Total Actuarial Liability            | <u>2,021,715,796</u>    | <u>1,952,539,400</u>    |
| Actuarial Value of Assets            | <u>601,219,999</u>      | <u>614,596,203</u>      |
| Unfunded Actuarial Liability         | <u>\$ 1,420,495,797</u> | <u>\$ 1,337,943,197</u> |

## ACTUARIAL SECTION

### SUMMARY OF ACCRUED AND UNFUNDED ACCRUED LIABILITIES (Analysis of Funding)

In an inflationary economy, the value of the dollar decreases. This environment results in employees' pay and retirement benefits increasing in dollar amounts resulting in unfunded accrued liabilities which increase in dollar amounts, all at a time when the actual substance of these items may be decreasing. Looking at just the dollar amounts of unfunded

accrued liabilities can be misleading. The ratio of the unfunded accrued liabilities to active employee payroll provides an index which clarifies understanding. The smaller the ratio of unfunded liabilities to active participant payroll, the stronger the system. Observation of this relative index over a period of years will give an indication of whether the system is becoming financially stronger or weaker.

| Fiscal Year | Total Actuarial Liability | Actuarial Value of Assets * | Actuarial Value of Assets as a % of Actuarial Liability | Total Unfunded Actuarial Liability | Annual Covered Payroll | Unfunded Actuarial Liability as a % of Annual Covered Payroll |
|-------------|---------------------------|-----------------------------|---|------------------------------------|------------------------|---|
| 2003        | \$ 1,076,231,965          | \$ 330,053,560              | 30.7%   | \$ 746,178,405                     | \$ 123,900,000         | 602.2%  |
| 2004        | 1,156,092,951             | 534,579,823                 | 46.2%   | 621,513,128                        | 127,200,000            | 488.6%  |
| 2005        | 1,236,512,156             | 564,999,447                 | 45.7%   | 671,512,709                        | 128,700,000            | 521.8%  |
| 2006        | 1,291,394,861             | 599,234,149                 | 46.4%   | 692,160,712                        | 135,400,000            | 511.2%  |
| 2007        | 1,385,339,573             | 670,090,950                 | 48.4%   | 715,248,623                        | 142,900,000            | 500.5%  |
| 2008        | 1,457,336,054             | 612,680,574                 | 42.0%   | 844,655,480                        | 143,700,000            | 587.8%  |
| 2009        | 1,548,509,535             | 616,849,071                 | 39.8%   | 931,660,464                        | 155,645,000            | 598.6%  |
| 2010        | 1,819,447,826             | 619,925,786                 | 34.1%   | 1,199,522,040                      | 161,164,000            | 744.3%  |
| 2011        | 1,952,539,400             | 614,596,203                 | 31.5%   | 1,337,943,197                      | 169,155,000            | 791.0%  |
| 2012        | 2,021,715,796             | 601,219,999                 | 29.7%   | 1,420,495,797                      | 171,498,000            | 828.3%  |

*\* For fiscal years prior to 2009, the actuarial value of assets was equal to the fair value of assets. Beginning in fiscal year 2009, the actuarial value of assets was equal to the fair value of assets adjusted for any actuarial gains or losses from investment return incurred in the fiscal year recognized in equal amounts over the five year period following that fiscal year.*

### SCHEDULE OF ACTIVE MEMBER VALUATION DATA

| Active Members         |        |                |                    |                                      |
|------------------------|--------|----------------|--------------------|--------------------------------------|
| Valuation Date June 30 | Number | Annual Payroll | Annual Average Pay | % Increase/(decrease) In Average Pay |
| 2003                   | 920    | \$123,900,000  | \$134,674          | 3.1%                                 |
| 2004                   | 906    | 127,200,000    | 140,397            | 4.2%                                 |
| 2005                   | 928    | 128,700,000    | 138,685            | (1.2)%                               |
| 2006                   | 917    | 135,400,000    | 147,655            | 6.5%                                 |
| 2007                   | 957    | 142,900,000    | 149,321            | 1.1%                                 |
| 2008                   | 957    | 143,700,000    | 150,157            | 0.6%                                 |
| 2009                   | 968    | 155,645,000    | 160,790            | 7.1%                                 |
| 2010                   | 966    | 161,164,000    | 166,836            | 3.8%                                 |
| 2011                   | 968    | 169,155,000    | 174,747            | 4.7%                                 |
| 2012                   | 968    | 171,498,000    | 177,167            | 1.4%                                 |

## ACTUARIAL SECTION

### RECONCILIATION OF UNFUNDED ACTUARIAL LIABILITY

|  | FY 2012                 | FY 2011                 |
|--|-------------------------|-------------------------|
| Unfunded actuarial liability at beginning of fiscal year   | \$ 1,337,943,197        | \$ 1,199,522,040        |
| Contributions due  | 158,158,157             | 129,342,352             |
| Contributions paid   | <u>82,844,597</u>       | <u>62,694,460</u>       |
| Increase in unfunded liability due to contributions due being less than contributions paid       | 75,313,560              | 66,647,892              |
| Increase in unfunded liability due to investment return lower than assumed                       | 27,522,701              | 31,451,544              |
| Decrease in unfunded liability due to salary increases lower than assumed                        | (19,671,785)            | (17,743,557)            |
| Increase in unfunded liability due to changes in assumptions other than interest rate assumption | +                       | -                       |
|  | -                       | 15,622,518              |
| Increase in unfunded liability due to new actuary  | 1,124,270               | -                       |
| Increase (decrease) in unfunded liability due to other sources                                   | <u>(1,736,146)</u>      | <u>42,442,760</u>       |
| Total Actuarial Losses   | 7,239,040               | 71,773,265              |
| Net increase in unfunded liability for the year  | = 82,552,600            | 138,421,157             |
| Unfunded actuarial liability at end of fiscal year   | <u>\$ 1,420,495,797</u> | <u>\$ 1,337,943,197</u> |

# STATISTICAL SECTION

*The tables in this section present historical financial information as well as certain historical demographic information pertaining to participants and benefit recipients.*

***Financial Schedules:***

These schedules present information pertaining to assets, liabilities, reserves, and changes in net assets over a 10-year period.

Asset Balances: page 52

Liabilities & Reserve Balances: page 52

Changes in Net Assets: page 53

***Participant Demographic Schedules:***

These schedules present certain information pertaining to active and inactive participants over a 10-year period.

Number of Participants: page 52

Number on Active Payrolls: page 54

***Benefit Recipient Demographic Schedules:***

These schedules present certain information pertaining to benefit recipients, benefit types, average monthly benefits, ranges of monthly benefits, and location of retirees.

Number of Recurring Benefit Payments/  
Termination Refunds: page 54

Active Retirees by State: page 54

Retirement Annuitant Statistics and  
Average Monthly Benefits: page 55

Annuitants and Survivors by Monthly  
Benefit Range Amount: page 55

Schedule of Average Benefit Payments:  
page 56

## STATISTICAL SECTION

### ASSET BALANCES

| Fiscal Year Ended June 30 | Cash         | Receivables  | Investments    | Securities lending collateral with State Treasurer | Fixed Assets Net of Accumulated Depreciation | Total          |
|---------------------------|--------------|--------------|----------------|--|--|----------------|
| 2003                      | \$ 7,324,152 | \$ 5,362,571 | \$ 317,541,091 | \$ -   | \$ 2,306                                     | \$ 330,230,120 |
| 2004                      | 13,326,833   | 536,406      | 521,372,992    | -  | 1,704  | 535,237,935    |
| 2005                      | 11,788,710   | 2,945,326    | 550,350,071    | -  | 3,278  | 565,087,385    |
| 2006                      | 16,363,642   | 301,575      | 582,604,390    | -  | 4,289  | 599,273,896    |
| 2007                      | 11,697,990   | 262,335      | 658,193,724    | -  | 3,323  | 670,157,372    |
| 2008                      | 19,411,250   | 4,187,003    | 589,155,697    | -  | 3,895  | 612,757,845    |
| 2009                      | 17,991,016   | 25,372,085   | 435,604,601    | -  | 3,318  | 478,971,020    |
| 2010                      | 16,644,537   | 261,482      | 506,463,522    | 6,242,000  | 3,841  | 529,615,382    |
| 2011                      | 18,015,766   | 221,316      | 587,794,578    | 7,261,000  | 3,377  | 613,296,037    |
| 2012                      | 10,690,635   | 8,211,574    | 559,139,279    | 5,945,000  | 9,326  | 583,995,814    |

### LIABILITIES AND RESERVE BALANCES

| Fiscal Year Ended June 30 | Total Liabilities | Reserve for Participant Contributions | Reserve for Future Operations | Total Reserves | Total         |
|---------------------------|-------------------|---------------------------------------|-------------------------------|----------------|---------------|
| 2003                      | \$ 176,560        | \$121,873,715                         | \$208,179,845                 | \$330,053,560  | \$330,230,120 |
| 2004                      | 658,112           | 130,547,360                           | 404,032,463                   | 534,579,823    | 535,237,935   |
| 2005                      | 87,938            | 135,440,555                           | 429,558,892                   | 564,999,447    | 565,087,385   |
| 2006                      | 39,747            | 142,846,641                           | 456,387,508                   | 599,234,149    | 599,273,896   |
| 2007                      | 66,422            | 145,242,498                           | 524,848,452                   | 670,090,950    | 670,157,372   |
| 2008                      | 77,271            | 152,455,812                           | 460,224,762                   | 612,680,574    | 612,757,845   |
| 2009                      | 94,943            | 157,840,805                           | 321,035,272                   | 478,876,077    | 478,971,020   |
| 2010                      | 6,339,230         | 166,360,698                           | 356,915,454                   | 523,276,152    | 529,615,382   |
| 2011                      | 7,335,829         | 167,567,660                           | 438,392,548                   | 605,960,208    | 613,296,037   |
| 2012                      | 6,019,447         | 177,546,650                           | 400,429,717                   | 577,976,367    | 583,995,814   |

### NUMBER OF PARTICIPANTS

| At June 30 | Active | Inactive | Total |
|------------|--------|----------|-------|
| 2003       | 920    | 42       | 962   |
| 2004       | 906    | 35       | 941   |
| 2005       | 928    | 34       | 962   |
| 2006       | 917    | 30       | 947   |
| 2007       | 957    | 33       | 990   |
| 2008       | 957    | 25       | 982   |
| 2009       | 968    | 23       | 991   |
| 2010       | 966    | 20       | 986   |
| 2011       | 968    | 16       | 984   |
| 2012       | 968    | 15       | 983   |

CHANGES IN NET ASSETS

Fiscal Year

|  | 2003            | 2004           | 2005          | 2006          | 2007          | 2008            | 2009             | 2010          | 2011          | 2012            |
|--|-----------------|----------------|---------------|---------------|---------------|-----------------|------------------|---------------|---------------|-----------------|
| <b>Additions</b>                                     |                 |                |               |               |               |                 |                  |               |               |                 |
| Participant contributions                            | \$ 12,904,997   | \$ 13,720,911  | \$ 13,268,530 | \$ 13,833,096 | \$ 14,152,973 | \$ 15,443,114   | \$ 15,763,410    | \$ 16,001,619 | \$ 16,725,191 | \$ 16,444,796   |
| Employer contributions:                              |                 |                |               |               |               |                 |                  |               |               |                 |
| State of Illinois                                    | 31,373,000      | 178,481,483    | 31,991,000    | 29,189,400    | 35,236,800    | 46,872,500      | 59,983,000       | 78,509,810    | 62,428,783    | 63,628,000      |
| Other sources  | 67,103          | 111,612        | 52,009        | 148,511       | -             | 105,461         | -                | -             | 265,677       | 16,099          |
| Total employer contributions                         | 31,440,103      | 178,593,095    | 32,043,009    | 29,337,911    | 35,236,800    | 46,977,961      | 59,983,000       | 78,509,810    | 62,694,460    | 63,644,099      |
| Net investment income/(loss)                         | (226,117)       | 74,012,814     | 50,848,968    | 61,329,673    | 98,157,681    | (37,976,460)    | (122,716,471)    | 42,532,318    | 105,253,385   | (69,096)        |
| Miscellaneous  | -               | -              | -             | -             | -             | -               | -                | -             | -5,000        | -               |
| Total additions to/(deductions from) plan net assets | 44,118,983      | 266,326,820    | 96,160,507    | 104,500,680   | 147,547,454   | 24,444,615      | (46,970,061)     | 137,043,747   | 184,678,036   | 80,019,799      |
| <b>Deductions</b>                                    |                 |                |               |               |               |                 |                  |               |               |                 |
| Benefit Payments:                                    |                 |                |               |               |               |                 |                  |               |               |                 |
| Temporary disability                                 | -               | -              | -             | -             | -             | 47,643          | 81,674           | 139,775       | 72,613        | -               |
| Retirement annuities                                 | 4,507,057       | 47,965,512     | 50,718,643    | 54,553,869    | 60,911,363    | 64,863,585      | 68,876,522       | 73,439,970    | 82,076,983    | 87,161,263      |
| Survivors' annuities                                 | 2,207,505       | 12,947,383     | 13,820,917    | 14,443,234    | 14,704,503    | 15,601,364      | 16,861,343       | 17,990,012    | 18,570,146    | 19,491,832      |
| Total benefit payments                               | 56,714,562      | 60,912,895     | 64,539,560    | 68,997,103    | 75,615,866    | 80,512,592      | 85,819,539       | 91,569,757    | 100,719,742   | 106,653,095     |
| Refunds:   |                 |                |               |               |               |                 |                  |               |               |                 |
| Termination  | 57,588          | 44,569         | -             | 160,035       | 25,310        | 83,572          | 29,417           | -             | 81,210        | 55              |
| Other  | 524,881         | 395,006        | 740,497       | 661,602       | 595,267       | 758,431         | 419,892          | 510,555       | 570,983       | 586,400         |
| Total refunds  | 582,469         | 439,575        | 740,497       | 821,637       | 620,577       | 842,003         | 449,309          | 510,555       | 652,193       | 586,455         |
| Administrative expenses                              | 427,686         | 448,087        | 460,826       | 447,238       | 454,210       | 500,396         | 565,588          | 563,360       | 622,046       | 764,090         |
| Total deductions from plan net assets                | 57,724,717      | 61,800,557     | 65,740,883    | 70,265,978    | 76,690,653    | 81,854,991      | 86,834,436       | 92,643,672    | 101,993,980   | 108,003,640     |
| Change in net assets                                 | \$ (13,605,734) | \$ 204,526,263 | \$ 30,419,624 | \$ 34,234,702 | \$ 70,856,801 | \$ (57,410,376) | \$ (133,804,497) | \$ 44,400,075 | \$ 82,684,056 | \$ (27,983,841) |

# STATISTICAL SECTION

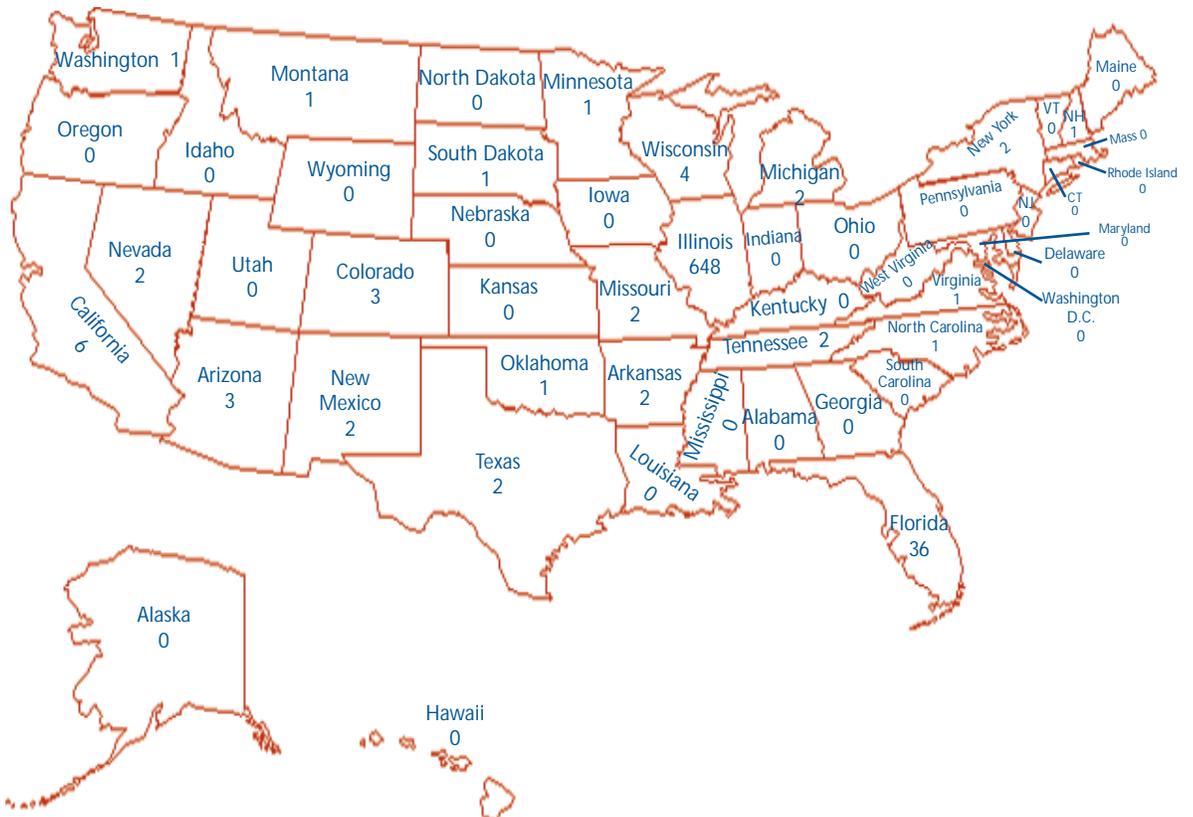
## NUMBER OF RECURRING BENEFIT PAYMENTS/ TERMINATION REFUNDS

| On June 30 | Retirement Annuities | Survivors' Annuities | Temporary Disability | Total Recurring Benefit Payments | Termination Refunds |
|------------|----------------------|----------------------|----------------------|----------------------------------|---------------------|
| 2003       | 539                  | 325                  | -                    | 864                              | 2                   |
| 2004       | 535                  | 338                  | -                    | 873                              | 3                   |
| 2005       | 562                  | 338                  | -                    | 900                              | -                   |
| 2006       | 581                  | 331                  | -                    | 912                              | 2                   |
| 2007       | 620                  | 326                  | -                    | 946                              | 3                   |
| 2008       | 624                  | 332                  | 1                    | 957                              | 4                   |
| 2009       | 647                  | 335                  | 1                    | 983                              | 1                   |
| 2010       | 665                  | 334                  | 2                    | 1,001                            | -                   |
| 2011       | 720                  | 327                  | -                    | 1,047                            | 3                   |
| 2012       | 725                  | 331                  | -                    | 1,056                            | 1                   |

## NUMBER ON ACTIVE PAYROLLS

| On June 30 | Supreme Court Justices | Appellate Court Justices | Circuit Court Judges | Retired Judges Recalled | Total |
|------------|------------------------|--------------------------|----------------------|-------------------------|-------|
| 2003       | 7                      | 42                       | 862                  | 12                      | 923   |
| 2004       | 7                      | 41                       | 847                  | 14                      | 909   |
| 2005       | 7                      | 40                       | 862                  | 21                      | 930   |
| 2006       | 7                      | 41                       | 852                  | 18                      | 918   |
| 2007       | 7                      | 41                       | 888                  | 22                      | 958   |
| 2008       | 7                      | 41                       | 885                  | 25                      | 958   |
| 2009       | 7                      | 40                       | 892                  | 30                      | 969   |
| 2010       | 7                      | 39                       | 894                  | 27                      | 967   |
| 2011       | 7                      | 38                       | 896                  | 27                      | 968   |
| 2012       | 7                      | 37                       | 903                  | 21                      | 968   |

### ACTIVE RETIREES BY STATE



## STATISTICAL SECTION

### RETIREMENT ANNUITANTS STATISTICS AND AVERAGE MONTHLY BENEFITS

| At Retirement             |             |                            |                     |                                 |
|---------------------------|-------------|----------------------------|---------------------|---------------------------------|
| Fiscal Year Ended June 30 | Average Age | Average Length of Service* | Average Current Age | Average Current Monthly Benefit |
| 2003                      | 63.8        | 17.8                       | 72.4                | \$ 7,107                        |
| 2004                      | 63.5        | 17.8                       | 72.3                | 7,418                           |
| 2005                      | 63.4        | 17.5                       | 72.3                | 7,730                           |
| 2006                      | 63.2        | 17.4                       | 72.3                | 8,015                           |
| 2007                      | 62.9        | 17.6                       | 71.9                | 8,443                           |
| 2008                      | 62.6        | 17.3                       | 71.7                | 8,685                           |
| 2009                      | 62.5        | 17.2                       | 71.4                | 9,098                           |
| 2010                      | 62.4        | 17.1                       | 71.5                | 9,379                           |
| 2011                      | 62.4        | 17.1                       | 71.2                | 9,797                           |
| 2012                      | 62.4        | 17.0                       | 71.6                | 10,118                          |

\* in years

| Annuitants by Benefit Range (Monthly)<br>on June 30, 2012 |       |                  |            |                       | Survivors by Benefit Range (Monthly)<br>on June 30, 2012 |       |                  |            |                       |
|---|-------|------------------|------------|-----------------------|--|-------|------------------|------------|-----------------------|
| Benefit Range   | Total | Cumulative Total | % of Total | Cumulative % of Total | Benefit Range  | Total | Cumulative Total | % of Total | Cumulative % of Total |
| \$1-1000  | 9     | 9                | 1.2%       | 1.2%                  | \$ 1-1000  | 32    | 32               | 9.7%       | 9.7%                  |
| 1001-2000   | 12    | 21               | 1.7        | 2.9                   | 1001-2000  | 27    | 59               | 8.1        | 17.8                  |
| 2001-3000   | 15    | 36               | 2.1        | 5.0                   | 2001-3000  | 28    | 87               | 8.5        | 26.3                  |
| 3001-4000   | 22    | 58               | 3.0        | 8.0                   | 3001-4000  | 21    | 108              | 6.3        | 32.6                  |
| 4001-5000   | 18    | 76               | 2.5        | 10.5                  | 4001-5000  | 32    | 140              | 9.7        | 42.3                  |
| 5001-6000   | 22    | 98               | 3.0        | 13.5                  | 5001-6000  | 50    | 190              | 15.1       | 57.4                  |
| 6001-7000   | 28    | 126              | 3.9        | 17.4                  | 6001-7000  | 54    | 244              | 16.3       | 73.7                  |
| 7001-8000   | 43    | 169              | 5.9        | 23.3                  | 7001-8000  | 40    | 284              | 12.1       | 85.8                  |
| 8001-9000   | 48    | 217              | 6.6        | 29.9                  | 8001-9000  | 40    | 324              | 12.1       | 97.9                  |
| 9001-10000  | 51    | 268              | 7.0        | 36.9                  | 9001-10000   | 6     | 330              | 1.8        | 99.7                  |
| 10001-11000   | 77    | 345              | 10.6       | 47.5                  | 10001-11000  | 1     | 331              | 0.3        | 100.0                 |
| 11001-12000   | 75    | 420              | 10.4       | 57.9                  |  |       |                  |            |                       |
| 12001-13000   | 186   | 606              | 25.7       | 83.6                  |  |       |                  |            |                       |
| 13001-14000   | 90    | 696              | 12.4       | 96.0                  |  |       |                  |            |                       |
| 14001-15000   | 22    | 718              | 3.0        | 99.0                  |  |       |                  |            |                       |
| 15001-16000   | 7     | 725              | 1.0        | 100.0                 |  |       |                  |            |                       |

## STATISTICAL SECTION

### Average Benefit Payments Fiscal Years 2003 through 2012

| Retirement Effective Dates      | Years Credited Service |           |           |           |           |           |           |
|---------------------------------|------------------------|-----------|-----------|-----------|-----------|-----------|-----------|
|                                 | 0-5                    | 5-10      | 10-15     | 15-20     | 20-25     | 25-30     | 30+       |
| <b>Period 7/1/02 to 6/30/03</b> |                        |           |           |           |           |           |           |
| Average monthly benefit         | \$ 7,815               | \$ 8,210  | \$ 5,069  | \$ 6,172  | \$ 9,332  | \$ 9,851  | \$ 10,019 |
| Average final average salary    | \$ 10,104              | \$ 11,378 | \$ 10,805 | \$ 11,632 | \$ 11,187 | \$ 11,590 | \$ 11,787 |
| Number of retired members*      | 3                      | 3         | 4         | 5         | 19        | 6         | 5         |
| <b>Period 7/1/03 to 6/30/04</b> |                        |           |           |           |           |           |           |
| Average monthly benefit         | \$ 9,181               | \$ 4,590  | \$ 5,531  | \$ 8,642  | \$ 9,002  | \$ 10,091 | \$ 9,617  |
| Average final average salary    | \$ 11,651              | \$ 11,694 | \$ 10,616 | \$ 11,815 | \$ 11,507 | \$ 11,872 | \$ 11,315 |
| Number of retired members*      | 4                      | 4         | 5         | 5         | 10        | 3         | 1         |
| <b>Period 7/1/04 to 6/30/05</b> |                        |           |           |           |           |           |           |
| Average monthly benefit         | \$ 9,175               | \$ 6,309  | \$ 6,586  | \$ 8,298  | \$ 9,985  | \$ 10,632 | \$ -      |
| Average final average salary    | \$ 11,960              | \$ 11,790 | \$ 11,158 | \$ 12,227 | \$ 11,747 | \$ 12,508 | \$ -      |
| Number of retired members*      | 10                     | 5         | 11        | 7         | 7         | 7         | -         |
| <b>Period 7/1/05 to 6/30/06</b> |                        |           |           |           |           |           |           |
| Average monthly benefit         | \$ 8,866               | \$ 7,057  | \$ -      | \$ 6,896  | \$ 9,468  | \$ 10,508 | \$ 10,650 |
| Average final average salary    | \$ 12,139              | \$ 12,744 | \$ -      | \$ 12,595 | \$ 12,194 | \$ 12,363 | \$ 12,744 |
| Number of retired members*      | 8                      | 2         | -         | 10        | 16        | 3         | 1         |
| <b>Period 7/1/06 to 6/30/07</b> |                        |           |           |           |           |           |           |
| Average monthly benefit         | \$ 9,421               | \$ 7,967  | \$ 7,254  | \$ 8,636  | \$ 10,491 | \$ 11,322 | \$ 11,179 |
| Average final average salary    | \$ 13,050              | \$ 13,152 | \$ 12,896 | \$ 12,752 | \$ 12,810 | \$ 13,320 | \$ 13,152 |
| Number of retired members*      | 6                      | 6         | 7         | 12        | 22        | 7         | 3         |
| <b>Period 7/1/07 to 6/30/08</b> |                        |           |           |           |           |           |           |
| Average monthly benefit         | \$ 6,171               | \$ 8,394  | \$ 7,169  | \$ 9,912  | \$ 10,005 | \$ -      | \$ 11,570 |
| Average final average salary    | \$ 9,595               | \$ 12,900 | \$ 12,512 | \$ 13,612 | \$ 12,880 | \$ -      | \$ 13,612 |
| Number of retired members*      | 2                      | 7         | 13        | 3         | 15        | -         | 1         |
| <b>Period 7/1/08 to 6/30/09</b> |                        |           |           |           |           |           |           |
| Average monthly benefit         | \$ 9,940               | \$ 9,313  | \$ 7,026  | \$ 7,699  | \$ 11,863 | \$ 12,369 | \$ 12,225 |
| Average final average salary    | \$ 13,429              | \$ 14,113 | \$ 13,894 | \$ 13,708 | \$ 14,135 | \$ 14,552 | \$ 14,383 |
| Number of retired members*      | 7                      | 9         | 6         | 4         | 23        | 6         | 5         |
| <b>Period 7/1/09 to 6/30/10</b> |                        |           |           |           |           |           |           |
| Average monthly benefit         | \$ 9,462               | \$ 9,855  | \$ 7,369  | \$ 7,372  | \$ 11,687 | \$ 9,670  | \$ 7,055  |
| Average final average salary    | \$ 13,408              | \$ 14,306 | \$ 13,328 | \$ 13,830 | \$ 14,183 | \$ 14,814 | \$ 14,525 |
| Number of retired members*      | 6                      | 4         | 6         | 6         | 15        | 2         | 2         |
| <b>Period 7/1/10 to 6/30/11</b> |                        |           |           |           |           |           |           |
| Average monthly benefit         | \$ 2,489               | \$ 4,922  | \$ 7,023  | \$ 11,074 | \$ 12,284 | \$ 12,760 | \$ 13,422 |
| Average final average salary    | \$ 14,158              | \$ 12,927 | \$ 13,404 | \$ 14,724 | \$ 14,619 | \$ 14,720 | \$ 15,373 |
| Number of retired members*      | 1                      | 4         | 10        | 25        | 29        | 9         | 5         |
| <b>Period 7/1/11 to 6/30/12</b> |                        |           |           |           |           |           |           |
| Average monthly benefit         | \$ 847                 | \$ 3,601  | \$ 7,891  | \$ 10,649 | \$ 12,140 | \$ 12,420 | \$ 12,166 |
| Average final average salary    | \$ 6,915               | \$ 13,897 | \$ 14,722 | \$ 14,825 | \$ 14,482 | \$ 14,612 | \$ 14,314 |
| Number of retired members*      | 1                      | 3         | 7         | 10        | 5         | 2         | 1         |

\* The number of retired members excludes new retirements with retroactive benefit start dates prior to the beginning of the period as well as resumptions of retirement benefits with original benefit start dates prior to the beginning of the period.

# PLAN SUMMARY AND LEGISLATIVE SECTION

## SUMMARY OF RETIREMENT SYSTEM PLAN (As of June 30, 2012)

### 1. Purpose

The purpose of the System is to establish an efficient method of permitting retirement, without hardship or prejudice, of judges who are aged or otherwise incapacitated, by enabling them to accumulate reserves for themselves and their dependents for old age, disability, death and termination of employment.

The Plan is comprised of two tiers of contribution requirements and benefit levels. Tier 1 pertains to participants who first became a participant of the System prior to January 1, 2011. Tier 2 pertains to participants who first became a participant of the System on or after January 1, 2011.

The provisions below apply to both Tier 1 and Tier 2 participants except where noted.

### 2. Administration

Responsibility for the operation of the System and the direction of its policies is vested in a Board of Trustees consisting of five members. The administration of the detailed affairs of the System is the responsibility of the Executive Secretary who is appointed by the Board of Trustees.

Administrative policies and procedures are designed to ensure an accurate accounting of funds of the System and prompt payment of claims for benefits within the applicable statute.

### 3. Employee Membership

All persons elected or appointed as a judge or associate judge of a Court become members of the System unless they file an election not to participate within 30 days of the date they are notified of this option.

### 4. Participant Contributions

Participants are required to contribute a percentage of salary as their share of meeting the various benefits at the rates shown below:

|                           |       |
|---------------------------|-------|
| Retirement Annuity        | 7.5%  |
| Automatic Annual Increase | 1.0%  |
| Survivors' Annuity        | 2.5%  |
| Total                     | 11.0% |

Tier 1 participants contribute based on total annual compensation. Tier 2 participants contribute based on a statutorily capped compensation amount which is increased each year by 3% or the annual percentage increase in the Consumer Price Index, whichever is less.

A judge who elects not to participate in the survivors' annuity benefit is not required to make contributions for the survivors' annuity benefit in which case the total participant contribution rate is 8 1/2% of salary. Contributions for survivors' annuity are not required to qualify an eligible child for a child's annuity.

Participants who are eligible to receive the maximum rate of annuity may irrevocably elect to discontinue contributions and have their benefits "frozen" based upon the applicable salary in effect immediately prior to the effective date of such election.

Participants who have attained age 60 and are eligible to receive the maximum rate of annuity and have not elected to discontinue contributing to the System may irrevocably elect to have their contributions based only on the salary increases received on or after the effective date of such election rather than on the total salary received.

### 5. Retirement Annuity

#### A. Qualification of Participant

Tier 1: Upon termination of service, a judge is eligible for an unreduced retirement annuity at:

1. Age 60 with at least 10 years of credit
2. Age 62 with at least 6 years of credit
3. Age 55 with at least 26 years of credit

The retirement annuity of a judge who retires between the ages of 55 and 60 with at least 10 years of credit shall be reduced 1/2 of 1% for each month the judge's age is under age 60.

However, for a judge who retires on or after December 10, 1999, the percentage reduction in retirement annuity shall be reduced by 5/12 of 1% for every month of service in the System in excess of 20 years.

Tier 2: Upon termination of service, a judge is eligible for an unreduced retirement annuity at:

1. Age 67 with at least 8 years of credit

The retirement annuity of a judge who retires between the ages of 62 and 67 with at least 8 years of credit shall be reduced 1/2 of 1% for each month the judge's age is under 67.

#### B. Amount of Annuity

Tier 1: The retirement annuity is determined according to the following formula based upon the applicable salary:

## PLAN SUMMARY

- 3.5% for each of the first 10 years of credit
- 5.0% for each year of credit above 10 years.

The maximum annuity is 85% of the applicable final average salary.

For participants who first serve as a judge before August 10, 2009 and terminate service on or after July 14, 1995, final average salary is the salary on the last day of employment as a judge or the highest salary received for employment as a judge in a position held for at least 4 consecutive years, whichever is greater.

For participants who first serve as a judge on or after August 10, 2009 and before January 1, 2011, final average salary is the average monthly salary during the 48 consecutive months of service within the last 120 months of service in which the total salary was the highest.

Tier 2: The retirement annuity is determined according to the following formula based upon the applicable final average salary:

- 3.0% for each year of credit

The maximum annuity is 60% of the applicable final average salary. The applicable final average salary is the average monthly salary during the 96 consecutive months of service within the last 120 months of service in which the total salary was the highest. The salary for any calendar year is capped in accordance with the statute governing the System. The cap is increased each year by 3% or the annual percentage increase in the Consumer Price Index, whichever is less.

### C. Annual Increases in Retirement Annuity

Tier 1: Post retirement increases of 3% of the current amount of annuity are granted to participants effective in January of the year next following the first anniversary of retirement and in January of each year thereafter.

Tier 2: Post retirement increases to the current amount of annuity in an amount equal to the lesser of 3% or the annual percentage increase in the Consumer Price Index for All Urban Consumers are granted to participants effective in January of the year next following the first anniversary of retirement and in January of each year thereafter, but in no event prior to age 67.

### D. Suspension of Retirement Annuity

Tier 1: The retirement annuity to any judge shall be suspended:

1. When the annuitant is employed for compensation by the State of Illinois as a judge, or
2. When the annuitant is employed for compensation by the State of Illinois in a permanent position other than legal counsel in the Office of the Governor or Chief

Deputy Attorney General (assuming the annuitant does not participate in any pension fund or retirement system under the Illinois Pension Code with respect to such service and, has filed prior to July 1, 2005, a written election with the System), or

3. After 75 working days in any calendar year in which the annuitant is employed for compensation by the State of Illinois in a temporary position other than a judge.

The retirement annuity to any judge shall not be suspended:

1. If the annuitant accepts employment in any teaching or non-teaching capacity with a state college or university as long as the annuitant did not elect the provisions of the Reciprocal Act upon retirement with the State Universities Retirement System, or
2. If the annuitant accepts employment in an administrative or teaching position with a secondary school district as long as the district level positions participate in the Teachers' Retirement System of Illinois and are not considered state positions which participate in the State Employees' Retirement System of Illinois, or
3. If the annuitant serves as a part-time employee (not required to work at least 35 hours per week) in any of the following positions and has not elected to participate in the State Employees' Retirement System of Illinois with respect to such service.

- Legislative Inspector General
- Special Legislative Inspector General
- Office of the Legislative Inspector General Employee
- Executive Director of the Legislative Ethics Commission
- Legislative Ethics Commission staff

Tier 2: The retirement annuity being paid is suspended when an annuitant is employed on a full time basis and becomes a member or participant of the Judges' Retirement System Article or any other Article of the Illinois Pension Code.

## 6. Survivor's Annuity

### A. Qualification of Survivor

If death occurs while in service as a judge, the judge must have established at least 1 1/2 years of credit. If death occurs after termination of service and prior to receipt of retirement annuity, the participant must have established at least 10 years of credit.

An eligible spouse, who has been married to the participant or annuitant for a continuous period of at least one year immediately preceding the date of death, qualifies at age 50, or at any age if there is in the care of the spouse any unmarried children of the member under age 18, over age 18 if mentally or physically disabled,

or under age 22 and a full-time student. Eligible surviving children would be entitled to benefits even though the participant did not contribute for the survivors' annuity benefit.

### B. Amount of Payment

If the participant's death occurs while in service, and assuming all payments have been made for full survivors' annuity credit, the surviving spouse would be eligible to 7 1/2% of salary or 66 2/3% of earned retirement annuity, whichever is greater. Eligible children of the participant would receive 5% of salary for each child with a maximum for all children of 20% of salary or 66 2/3% of earned retirement annuity, whichever is greater, regardless of whether full credit had been established for the survivors' annuity benefit.

If the participant's death occurs after termination of service or retirement, and assuming all payments have been made for full survivors' annuity credit, the surviving spouse would be eligible to 66 2/3% of earned retirement annuity. Eligible children would receive a survivors' annuity equal to the benefit of surviving children of a participant in service.

The benefit payment amount to a surviving spouse would be a prorated share of the full benefit amount noted above if the participant married or remarried after becoming a participant and elected to contribute for the survivors' annuity benefit prospectively from the date of marriage or remarriage.

### C. Annual Increases in Survivors' Annuity

Tier 1: Increases of 3% of the current amount of annuity are granted to survivors in each January occurring on or after the commencement of the annuity if the deceased participant died while receiving a retirement annuity.

In the event of an active participant's death, increases of 3% of the current amount of annuity are granted to survivors effective in January of the year next following the first anniversary of the commencement of the annuity and in January of each year thereafter.

Tier 2: Increases to the current amount of annuity in an amount equal to the lesser of 3% or the annual percentage increase in the Consumer Price Index for All Urban Consumers are granted to survivors. Such increases are payable on each January 1 occurring on or after the commencement of the annuity if the deceased participant died while receiving a retirement annuity or, in other cases, on each January 1 occurring on or after the first anniversary of the commencement of the annuity, but in no event prior to age 67.

### D. Duration of Payment

When all children, except for disabled children, are ineligible because of death, marriage or attainment of age 18 or age 22 in the case of a full-time student, the

spouse's benefit is suspended if the spouse is under age 50 until attainment of such age.

## 7. Death Benefit

The following lump sum death benefits are payable to the named beneficiaries or estate of the participant only if there are no eligible survivors' annuity beneficiaries surviving the deceased participant.

### A. Before Retirement

If the participant's death occurs before retirement, a refund of total contributions in the participant's account.

### B. After Retirement

If the participant's death occurs after retirement, a refund of the excess of contributions over annuity payments, if any.

The following lump sum death benefit is payable to the named beneficiaries or estate of the survivor.

### A. Death of Survivor Annuitant

Upon death of the survivor annuitant with no further survivors' annuity payable, a refund of excess contributions over total retirement and survivors' annuity payments, if any.

## 8. Disability Benefit

### A. Permanent Total Disability

A participant who becomes totally and permanently disabled while serving as a judge with at least 10 years of credit is eligible for an unreduced retirement annuity regardless of age. If disability is service-connected, the annuity is subject to reduction by amounts received by a participant under the Workers' Compensation Act and the Workers' Occupational Diseases Act.

### B. Temporary Total Disability

A participant with at least 2 years of service as a judge who becomes totally disabled and unable to perform the duties as a judge is entitled to a temporary disability benefit equal to 50% of salary payable during disability but not beyond the end of the term of office.

## 9. Refund of Contributions

A participant who terminates service as a judge may obtain a refund of total contributions made to the System, without interest, provided the participant is not immediately eligible to receive a retirement annuity. By accepting a refund, a participant forfeits all accrued rights and benefits in the System for his or herself and beneficiaries.

An unmarried participant or a married participant who becomes unmarried, either before or after retirement, is entitled to a refund of contributions made for the survivors' annuity benefit.

## LEGISLATIVE SECTION

### LEGISLATIVE AMENDMENTS

Legislative amendments with an effective date during fiscal year 2012 having an impact on the System.

***Senate Bill 1671 (P.A. 97-0530; effective August 23, 2011)***

Requires all pension funds and retirement systems to comply with the federal Heroes Earnings Assistance and Relief Tax Act of 2008 (P.L. 110-245).

***House Bill 3813 (P. A. 97-0651; effective January 5, 2012)***

Adds a requirement to the General Provisions of the Illinois Pension Code that any reasonable suspicion by an appointed trustee of a false statement or a falsified record being submitted or permitted by a person covered by the Illinois Pension Code shall be immediately referred to the board of trustees.

***Senate Bill 0179 (P. A. 97-0694; effective June 18, 2012)***

Amends the Illinois State Auditing Act. Authorizes the Auditor General to contract with or hire an actuary to serve as the State Actuary. Sets forth the duties of the State Actuary. Changes the manner in which the minimum required State contribution is certified. Provides for the State Actuary to provide input regarding the actuarial assumptions of the State-funded retirement systems.

### NEW LEGISLATION

There were no legislative amendments with an effective date subsequent to June 30, 2012 having an impact on the System.