A Report
to the
Montana
Legislature

Financial-Compliance Audit

Teachers' Retirement System

For the Two Fiscal Years Ended June 30, 2008

December 2008

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Division

08-09A

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LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor
Monica Huyg, Legal Counsel

Deputy Legislative Auditors
James Gillett
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December 2008

The Legislative Audit Committee
of the Montana State Legislature:

This report, along with our financial audit report (07-09), constitutes our financial-compliance audit report on the Teachers' Retirement System (system), a component unit of the state of Montana, for the two fiscal years ended June 30, 2008. In both audits we tested compliance with laws that have a direct and material effect on the financial statements. This report contains recommendations related to the actuarial soundness of the system and improving internal controls.

We issued an unqualified opinion on the system's financial statements for the fiscal years ended June 30, 2008, and 2007. Our opinion on the system's financial statements is also contained in the Teachers' Retirement System annual report. The annual report contains additional background, statistical, and actuarial information not included in this audit report, which may be of interest to legislators or the public. Copies of the annual report can be obtained from the Teachers' Retirement System or accessed on its website. The annual report for fiscal year 2008 is expected to be available in December 2008.

The system's written response to the audit is included at the end of the audit report. We thank the Executive Director and his staff for their assistance and cooperation throughout the audit.

Respectfully submitted,

/s/ Tori Hunthausen

Tori Hunthausen, CPA
Legislative Auditor

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Appointed and Administrative Officials

			Term Expires
Teachers' Retirement Board	Tim Ryan, Chair	Big Fork	7/1/09
	Kari Peiffer, Vice Chair	Kalispell	7/1/12
	Scott Dubbs	Lewistown	7/1/13
	Mona Bilden	Miles City	7/1/11
	Darrell Laymen	Glendive	7/1/11
	James Turcotte	Helena	7/1/10

Administrative Officials

David L. Senn, Executive Director

Tammy Rau, Deputy Executive Director

Dan Gaughan, Accounting/Fiscal Manager

For additional information concerning the Teachers' Retirement System, contact:

David L. Senn, Executive Director
1500 Sixth Avenue
P.O. Box 200139
Helena, MT 59620-0139
e-mail: dsenn@mt.gov

Report Summary

Teachers' Retirement System

This report documents the results of our financial-compliance audit of the Teachers' Retirement System (system) for the two fiscal years ended June 30, 2008. This report contains recommendations related to the actuarial soundness of the system and improving internal controls. The financial audit of the system for the two fiscal years ended June 30, 2007, was issued in a separate report (07-09).

System personnel prepare the financial statements from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) with adjustment. We issued an unqualified opinion on the financial statements presented in this report, which means the reader can rely on the financial information presented.

The listing below serves as a means of summarizing the recommendations contained in the report, the system's response thereto, and a reference to the supporting comments.

Recommendation #1 4

We recommend the Teachers' Retirement System take necessary measures to ensure the system is funded on an actuarially sound basis as required by the Montana Constitution.

System Response: Concur B-3

Recommendation #2 4

We recommend the Teachers' Retirement System document procedures to monitor and test internal controls in accordance with state policy.

System Response: Concur B-3

Chapter I – Introduction

Introduction

We performed a financial-compliance audit of the Teachers' Retirement System (system) for the two fiscal years ended June 30, 2008. The objectives of our audit were to:

- Determine the system's compliance with applicable laws and regulations.
- Obtain an understanding of the system's control processes, and if appropriate, make recommendations for improvement in the internal and management controls of the system.
- Determine if the financial statements prepared by system personnel fairly present the fiduciary net assets of the system as of June 30, 2008 and 2007, and the changes in fiduciary net assets for the fiscal years then ended, in conformity with generally accepted accounting principles.

Our financial audit of the system for the two fiscal years ended June 30, 2007, was issued in a separate report (07-09).

The financial statements are prepared by system personnel from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) with adjustment. Adjustments are made to correct errors in the accounting records and to accurately present financial activity to the readers of the statements in accordance with generally accepted accounting principles (GAAP). As such, a reader should not expect these financial statements to agree in all instances to the state's primary accounting records.

This report contains recommendations regarding the unfunded actuarial liability and improving internal controls. Other areas of concern deemed not to have a significant effect on the successful operations of the system are not specifically included in the report, but have been discussed with management. In accordance with section 5-13-307, MCA, we analyzed the cost of implementing the recommendation contained in this report and determined it was significant; this is discussed in the report section beginning on page 3.

Background

The system is a component unit of the state of Montana. A component unit is a legally separate organization for which the state of Montana is financially accountable. The system, established by state law in 1937, had more than 18,000 active members not yet receiving benefits at July 1, 2008. Approximately 11,300 retirees or their beneficiaries were receiving retirement, disability, or survivor benefits as of July 1, 2008.

A six-member board, appointed by the Governor for five-year terms, governs the system. In addition to providing oversight to system personnel, the board's responsibilities include:

- Establishing rules and regulations necessary for the proper administration and operation of the retirement system.
- Determining the eligibility of a person who is applying for membership in the system.
- Designating an actuary to provide consultation on the technical actuarial aspects of the retirement system.

The Executive Director and system personnel are responsible for the daily administration of the system. At June 30, 2008, 17 full-time equivalent (FTE) positions were authorized for the system.

All full-time members of the public teaching profession, except for eligible employees of the Montana University System hired after July 1, 1993, are required by law to be members in the retirement system. All contributions are exempt from income tax to the employees until benefits are drawn against those contributions. The system implemented a Guaranteed Annual Benefit Adjustment (GABA) effective in January 2000. Retirees are eligible for GABA once they have received at least 36 monthly retirement benefit payments prior to January 1 of the year in which the adjustment is to be made. GABA provides eligible retirees with a guaranteed 1.5 percent increase in retirement benefits on an annual basis.

In fiscal years 2006 and 2007 the legislature authorized a $100 million and $50 million general fund transfer to the system respectively to address funding shortfalls. The 2007 Legislature also increased General Fund employer and general fund contributions. The Montana Board of Investments is responsible for investing the system's assets.

Chapter II – Findings and Recommendations

System Not Actuarially Sound

The results of the July 1, 2008, actuarial valuation show the Teachers' Retirement System (system) is not actuarially sound.

Article VIII, Section 15, of the Constitution of the State of Montana, requires public retirement systems be funded on an actuarially sound basis. To be actuarially sound, government accounting standards provide that the maximum amortization period for an unfunded actuarial accrued liability (UAAL) is 30 years.

The most recent actuarial valuation, performed as of July 1, 2008, indicates the system is not actuarially sound and the period required to amortize UAAL is 31.3 years. The actuarial valuation as of July 1, 2007, found the system to be actuarially sound with a UAAL amortization period of 28.6 years. The legislature provided supplemental cash contributions of $50 million in fiscal year 2007 and $100 million in fiscal year 2006. Those supplemental cash contributions, increased state general fund contributions, and positive investment returns helped make the system actuarially sound at July 1, 2007. In addition, the 2007 Legislature increased funding contributions as noted below.

Contributions as a Percent of Pay

	Members	Participating Employers	State General Fund Contribution*	Total
Prior to July 1, 2007	7.15%	7.47%	0.11%	14.73%
July 1, 2007 to June 30, 2009	7.15%	7.47%	2.11%	16.73%
July 1, 2009 and after	7.15%	7.47%	2.49%	17.11%

*The general fund contribution is for members employed by a school district or community college. Other member employers will contribute 9.47 percent from July 1, 2007, until June 30, 2009, and 9.85 percent after July 1, 2009.

The funding policy of the systems' board (Board) provides that… "whenever the amortization period of the unfunded liabilities for two consecutive valuations are projected to exceed 30 years based on the market value of assets, or the funded ratio is less than 85 percent, and the Board cannot reasonably anticipate that the amortization period would decline or the funded ratio improve without an increase in funding sources, it is the obligation of the Board to recommend to the legislature that funding be increased and/or liabilities be reduced.'' The funding ratio refers to the portion of the UAAL that can be satisfied with the current level of contributions.

The actuarial valuation disclosed that the amortization period at July 1, 2008, is 31.3 years and the funded ratio is currently 79.9 percent. That valuation also notes that, assuming experience follows actuarial assumptions, the amortization period is projected to remain above 30 years and notes that a contribution increase of .17 percent of pay (17.11 percent to 17.28 percent) as of July 1, 2009, is projected to maintain an amortization of the UAAL over 30 years.

Recommendation #1

We recommend the Teachers' Retirement System take necessary measures to ensure the system is funded on an actuarially sound basis as required by the Montana Constitution.

Internal Controls

The Teachers' Retirement System has not documented procedures for monitoring and testing of control procedures in accordance with state accounting policy.

State policy in the Montana Operations Manual (MOM), Volume II, Chapter 2-9900, outlines management's responsibility for establishing and maintaining internal controls. To assist agencies, the Department of Administration issued an Internal Control Guidebook contained in the MOM noted above. A section of this policy requires management to establish procedures to monitor and test internal controls to ensure they are working as management intends.

During the course of our audit we found that management has established internal controls but has not documented monitoring or testing of internal controls. Documented monitoring and testing procedures provide management with assurance that controls are working as designed. Management noted they have started documentation of monitoring and testing procedures.

Recommendation #2

We recommend the Teachers' Retirement System document procedures to monitor and test internal controls in accordance with state policy.

Independent Auditor's Report

LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor
Monica Huyg, Legal Counsel

Deputy Legislative Auditors
James Gillett
Angie Grove

Independent Auditor's Report

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Statement of Fiduciary Net Assets of the Teachers' Retirement System (system), a component unit of the state of Montana, as of June 30, 2008 and 2007, and the related Statement of Changes in Fiduciary Net Assets for each of the fiscal years then ended. These financial statements are the responsibility of the Teachers' Retirement Board. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Teachers' Retirement System as of June 30, 2008 and 2007, and the changes in fiduciary net assets for each of the fiscal years then ended, in conformity with accounting principles generally accepted in the United States of America.

Management's Discussion and Analysis, the Schedule of Funding Progress, the Schedule of Contributions from the Employer and Other Contributing Entities and Other Postemployment Benefits Plan Information-Schedule of Funding Progress, are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements of the Teachers' Retirement System. The Supporting Schedule of Administrative Expenses and the Schedule of

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Payments to Consultants are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

At July 1, 2008, the system was not actuarially sound. The amortization period for the Unfunded Actuarially Accrued Liability (UAAL) was 31.3 years at July 1, 2008. The maximum allowable amortization period is 30 years.

Respectfully submitted,

/s/ James Gillett

James Gillett, CPA
Deputy Legislative Auditor

November 14, 2008

Teachers' Retirement System
Management's Discussion and Analysis,
Financial Statements, Required Supplementary Information,
and Supplemental Information

TEACHERS' RETIREMENT SYSTEM
MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion and analysis provides a financial activity overview of the Montana Teachers' Retirement System (TRS) for the fiscal year ended June 30, 2008 with comparative totals for the fiscal years ended June 30, 2007 and 2006. Please read this in conjunction with the financial statements, accompanying footnotes, required supplementary information with notes, and supporting schedules.

Overview of the Financial Statements

Because of the long-term nature of a defined benefit pension plan, financial statements alone cannot provide sufficient information to properly reflect the System's ongoing plan perspective.

This presentation consists of two financial statements with footnotes, two schedules of historical trend information with footnotes, and two supporting schedules. The Statement of Fiduciary Net Assets reflects the resources available to pay benefits to retirees and beneficiaries. The Statement of Changes in Fiduciary Net Assets presents the changes that occurred in those resources for the fiscal year ended.

The Schedule of Funding Progress presents historical trend information about the actuarially funded status for the TRS plan from a long-term, ongoing perspective and the progress made in accumulating sufficient assets to pay benefits when due. The Schedule of Contributions from the Employer and Other Contributing Entities displays historical trend data of the annual required employer contributions and the actual contributions made by employers in relation to the requirement.

The Schedule of Administrative Expenses is a presentation of what comprises the administrative expense item as reported on the Statement of Changes in Fiduciary Net Assets. The Schedule of Payments to Consultants represents our fees paid to outside professionals.

Financial Highlights

- The 2007 Legislature increased the employer contribution rate from 7.47% to 9.47% for fiscal year 2008.
- The TRS plan net assets decreased by $215.9 million in 2008 and increased $463.4 million in 2007 representing a 6.7% decrease and a 16.9% increase respectively.
- Net investment income (fair value of investments plus investment income less investment expense) decreased in 2008 by $131.6 million and increased $115.1 million in 2007 representative of the volatility of the stock market.
- Pension benefits paid to beneficiaries and plan members increased 7.3% and 6.3% for the last two fiscal years respectively.

Condensed Financial Information (in millions)

Fiduciary Net Assets	FY2008	FY2007	FY2006	2008 Percent Inc/(Dec)	2007 Percent Inc/(Dec)
Cash/Short-term Investments	$ 31.8	$ 88.4	$ 71.8	(64.0)	23.1
Receivables	29.5	21.5	21.0	37.2	2.4
Investments (fair value)	3,113.1	3,256.3	2,704.4	(4.4)	20.4
Capital Assets (net)	0.3	0.3	0.7	0	(57.1)
Total Assets	3,174.7	3,366.6	2,797.9	(5.7)	20.3
Liabilities	181.3	157.3	52.2	15.3	201.3
Net Assets	**$2,993.4**	**$3,209.3**	**$2,745.8**	**(6.7)**	**16.9**

Changes in Fiduciary Net Assets	FY2008	FY2007	FY2006	2008 Percent Inc/(Dec)	2007 Percent Inc/(Dec)
Additions:					
Employer Contributions	$ 67.9	$ 61.9	$ 58.3	9.7	6.2
Plan Member Contributions	59.6	56.5	53.3	5.5	6.0
Other Contributions	13.5	0.7	0.7	1,828.6	0.0
Payment from State of Montana	0	50.0	100.0	(100.0)	(50.0)
Net Investment Income	(153.3)	484.5	224.8	(131.6)	115.5
Total Additions	(12.3)	653.7	437.0	(101.9)	49.6
Deductions:					
Benefit Payments	196.1	182.8	172.0	7.3	6.3
Withdrawals	5.7	5.6	4.9	1.8	14.3
Administrative Expenses	1.8	1.4	1.6	28.6	(12.5)
Loss on Intangible Asset	0	0.5	0.0	(100.0)	NA
Total Deductions	203.6	190.4	178.4	6.9	6.7
Net Inc/(Dec) in Net Assets	**$ (215.9)**	**$ 463.4**	**$ 258.6**	**(146.6)**	**79.2**

Financial Analysis

- The increase/decrease from year-to-year in cash/short-term investments is due mostly to the change in the number of shares held in the Short Term Investment Pool.
- The significant increase in receivables for 2008 reflects the supplemental payment due at fiscal year end from the general fund in relation to the 2% increase in the employer contribution rate for school districts that was effective July 1, 2007.
- The decrease/increase in investments for 2008 and 2007 respectively is due primarily to the change in the fair market value of our investment holdings.
- The decrease in capital assets in 2007 is due to the depreciation and amortization of the assets and a loss on the write-off of previously capitalized software costs in 2007.
- The significant fluctuation in liabilities is due to the security lending collateral activity conducted by the Montana Board of Investments.
- The significant decrease in net investment income in 2008 was due to a $590.7 million drop in the fair value of investments and $40.8 million less in investment earnings as compared to the $200.6 million increase in the fair value of our investments and a $62.7 million increase in investment earnings in 2007 and a $40.8 million increase in the unrealized net appreciation in the fair value of our investments for 2006.
- The increase in benefit payments from year-to-year reflects an increase in the number of retirees and beneficiaries plus the 1.5% guaranteed annual benefit adjustment.

Overview of the Actuarial Funding

The TRS plan experienced an asset loss over the last year. The market assets had a negative return of 4.9% net of investment and operating expenses. The actuarial assets earned 7.22% which is 0.57% below the actuarial assumption of 7.75%. Actuarial gains or losses result when the return on the actuarial value of assets differs from the actuarial investment return assumption. The following table compares the annual returns for the past six years.

Fiscal Year	Market Return	Actuarial Return	Actuarial Return over 7.75 % Assumption (8.00% prior to 7/1/04)
7/1/2002 to 6/30/2003	6.2%	1.6%	(6.4)%
7/1/2003 to 6/30/2004	13.3%	2.1%	(5.9)%
7/1/2004 to 6/30/2005	8.0%	2.7%	(5.0)%
7/1/2005 to 6/30/2006	8.9%	8.5%	0.7%
7/1/2006 to 6/30/2007	17.6%	10.2%	2.5%
7/1/2007 to 6/30/2008	(4.9)%	7.2%	(0.6)%

The chart above shows the actuarial return on assets has under performed the assumption more than it has exceeded the assumption in the last six years. These losses plus other actuarial gains and losses led to the need for the legislature to provide one-time contributions of $50 million in fiscal year 2007 and $100 million in fiscal year 2006. Those one time contributions and positive investment returns in fiscal year 2007 helped make the system actuarially sound at July 1, 2007. In addition, the 2007 legislature also increased funding contributions as noted below.

Contributions as a Percent of Pay

	Members	Participating Employers	State General Fund Contribution*	Total
Prior to July 1, 2007	7.15%	7.47%	0.11%	14.73%
July 1, 2007 to June 30, 2009	7.15%	7.47%	2.11%	16.73%
July 1, 2009 and after	7.15%	7.47%	2.49%	17.11%

*The General Fund contribution is for members employed by a school district or community college. Other member employers will contribute 9.47 percent from July 1, 2007 until June 30, 2009, and 9.85 percent after July 1, 2009.

The July 1, 2007 actuarial valuation calculated a 28.6 year amortization period for the Unfunded Actuarial Accrued Liability. If there were no assumption changes, or experience gains and losses, the amortization period would have been expected to decrease by 1.0 years to 27.6 at July 1, 2008. The new assumptions adopted in May 2008 increased the expected July 1, 2008 amortization period by 2.7 years to 30.3. The experience gains and losses from the year ending June 30, 2008 increased the amortization period by another 1.0 years. The resulting amortization period at July 1, 2008 is 31.3 years. The net funded ratio is currently 79.9%.

MCA 19-20-201 requires the actuarial report to show how market performance is affecting the actuarial funding of the Retirement System. The July 1, 2008 market value of assets is $166 million less than the actuarial value of assets due to a negative 4.88% market return in the year ended June 30, 2008. If the market value of assets was used, the amortization period would be 44.7 years, and the net Funded Ratio would be 75.7%. Based on market assets, a contribution increase of 1.57% of pay (17.11% to 18.68%) as of July 1, 2009 is projected to maintain an amortization of the unfunded actuarial accrued liability over the 30 years beginning July 1, 2008.

TEACHERS' RETIREMENT SYSTEM
A COMPONENT UNIT OF THE STATE OF MONTANA
STATEMENT OF FIDUCIARY NET ASSETS
JUNE 30, 2008 AND 2007

	2008	2007
ASSETS		
Cash/Cash Equivalents-Short Term		
Investment Pool (Note B)	$ 31,811,457	$ 88,435,655
Receivables:		
Accounts Receivable	18,946,006	15,159,435
Interest Receivable	7,292,299	6,214,473
Due from Primary Government	3,241,381	170,489
Total Receivables	$ 29,479,686	$ 21,544,397
Investments, at fair value (Note B):		
Mortgages	$ 27,120,606	$ 31,399,861
Investment Pools	2,893,544,962	3,059,618,387
Other Investments	11,426,652	8,236,796
Securities Lending Collateral (Note B)	180,987,059	157,024,527
Total Investments	$ 3,113,079,279	$ 3,256,279,571
Assets Used in Plan Operations:		
Land and Buildings	$ 193,844	$ 193,844
Less: Accumulated Depreciation	(143,645)	(139,880)
Equipment	63,662	147,087
Less: Accumulated Depreciation	(48,999)	(131,200)
Prepaid Expense	647	9,812
Intangible Assets, net of amortization	252,351	246,113
Total Other Assets	$ 317,860	$ 325,776
TOTAL ASSETS	$ 3,174,688,282	$ 3,366,585,399
LIABILITIES		
Accounts Payable	$ 88,004	$ 128,299
Due to Primary Government	14,434	17,363
Securities Lending Liability (Note B)	180,987,059	157,024,527
Compensated Absences (Note B)	158,675	139,888
OPEB Implicit Rate Subsidy	47,478	0
TOTAL LIABILITIES	$ 181,295,650	$ 157,310,077
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS	$ 2,993,392,632	$ 3,209,275,322

The accompanying Notes to the Financial Statements are an integral part of this financial statement.

TEACHERS' RETIREMENT SYSTEM
A COMPONENT UNIT OF THE STATE OF MONTANA
STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
FISCAL YEARS ENDED JUNE 30, 2008 AND 2007

	2008	2007
ADDITIONS		
Contributions:		
Employer	$ 67,921,950	$ 61,943,986
Plan Member	59,552,619	56,508,585
Other	13,492,375	720,266
Total Contributions	$ 140,966,944	$ 119,172,837
Misc Income	$ 15,654	$ 15,633
Payment from Primary Government (Note C)	0	50,000,000
Investment Income:		
Net Appreciation/(Depreciation) in Fair Value of Investments	$ (236,359,446)	$ 354,302,356
Investment Earnings	96,731,693	137,540,095
Security Lending Income (Note B)	9,544,163	5,815,626
Investment Income/(Loss)	$ (130,083,590)	$ 497,658,077
Less: Investment Expense	15,425,847	7,616,254
Less: Security Lending Expense (Note B)	7,802,791	5,509,847
Net Investment Income/(Loss)	$ (153,312,228)	$ 484,531,976
Total Additions	$ (12,329,630)	$ 653,720,446
DEDUCTIONS		
Benefit Payments	$ 196,060,216	$ 182,826,747
Withdrawals	5,694,601	5,594,541
Administrative Expense	1,750,765	1,434,103
OPEB Expenses	47,478	0
Loss on Intangible Asset	0	501,575
Transfer out	0	205
Total Deductions	$ 203,553,060	$ 190,357,171
NET INCREASE (DECREASE) IN PLAN NET ASSETS	$ (215,882,690)	$ 463,363,275
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS BEGINNING OF YEAR	3,209,275,322	2,745,771,047
Prior Period Adjustment		141,000
END OF YEAR	$ 2,993,392,632	$ 3,209,275,322

The accompanying Notes to the Financial Statements are an integral part of this financial statement.

TEACHERS' RETIREMENT SYSTEM
A COMPONENT UNIT OF THE STATE OF MONTANA
NOTES TO THE FINANCIAL STATEMENTS
FISCAL YEARS ENDED JUNE 30, 2008 AND 2007

NOTE A. DESCRIPTION OF THE PLAN

The Teachers' Retirement Board is the governing body of a mandatory multiple-employer cost-sharing defined benefit pension plan, which provides retirement services to persons in Montana employed as teachers or professional staff of any public elementary or secondary school, community college or unit of the university system. The system was established by the State of Montana in 1937 to provide retirement, death and disability benefits and is governed by Title 19, chapter 20, of the MCA. TRS as an employer does not participate in the plan and acts only as the administrator of the plan.

At June 30, 2008, the number and type of reporting entities participating in the system were as follows:

Local School Districts	355
Community Colleges	3
University System Units	2
State Agencies	8
Total	368

At July 1, 2008, the date of the most recent actuarial valuation system membership consisted of the following:

Retirees and Beneficiaries Currently Receiving Benefits	11,788
Terminated Employees:	
Vested	1,649
Non-vested	9,574
Current Active Members:	
Vested	11,760
Non-vested	6,532
Total Membership	41,303

The pension plan provides retirement benefits and death and disability benefits. Employees with a minimum of 25 years of service or who have reached age 60 with 5 years of service are eligible to receive an annual retirement benefit equal to creditable service years divided by 60 times the average final compensation. Final compensation is the average of the highest three consecutive years of earned compensation. Benefits fully vest after 5 years of creditable service. Vested employees may retire at or after age 50 and receive reduced retirement benefits. A Guaranteed Annual Benefit Adjustment (GABA) of 1.5% is payable each January if the retiree has received at least 36 monthly retirement benefit payments prior to January 1 of the year in which the adjustment is to be made.

NOTE B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The TRS, a discretely presented component unit Pension Trust Fund of the State of Montana financial reporting entity, prepares its financial statements using the accrual basis of accounting. Employee and employer contributions are recognized as revenues in the period when due and investment income is recognized when earned. Benefit and withdrawal payments are recorded in the period in which the liabilities are due and payable.

Compensated Absences

Compensated absences represent 100 percent of accrued vacation and 25 percent of accrued sick leave for TRS personnel at June 30, 2008 and June 30, 2007.

Cash/Cash Equivalents and Investments

The Montana Board of Investments (BOI) manages the State's Unified Investment Program, which includes the TRS plan investments as required by Section 19-20-501, Montana Code Annotated. Per the Montana Constitution, Article VIII Section 13(3), investment of TRS assets shall be managed in a fiduciary capacity in the same manner that a prudent expert acting in a fiduciary capacity and familiar with the circumstances would use in the conduct of an enterprise of a similar character with similar aims. Information on investment policies, investment activity, investment management fees and a listing of specific investments owned by the pooled asset accounts can be obtained from Board of Investments at P.O. Box 200126, Helena, MT 59620-0126.

Information about the primary government's (State of Montana) investments, including credit risk classification, can be obtained from the Department of Administration, State Accounting Division, at P.O. Box 200102, Helena, MT 59620-0102.

Cash and cash equivalents consist of funds deposited in the State Treasurer's pooled cash account and cash invested in the Short-Term Investment Pool (STIP). Pool investments other than STIP are reported at the fair value of each unit times the number of units owned. STIP is recorded at $1 per unit for each unit held. The fair value of publicly traded stocks and bonds is determined by reference to market prices supplied by State Street Bank (the custodial bank). Because a public market does not exist for private equity and real estate investments, the fair value of these investments is the value reported in the most recent external managers' valuation reports.

The TRS investments include: STIP; Retirement Funds Bond Pool (RFBP); Montana Domestic Equity Pool (MDEP); Montana International Equity Pool (MTIP); Montana Private Equity Pool (MPEP), Montana Real Estate Pool (MTRP), mortgages and real estate. The TRS Investment Portfolio is listed below:

TRS Cash Equivalent and Investment Portfolio
June 30, 2008

Investment	Book Value	Fair Value
STIP	$ 32,943,654	$ 32,943,654
RFBP	768,059,943	760,319,056
MDEP	541,012,407	1,157,377,216
MTIP	311,631,000	561,647,715
MPEP	180,582,970	287,420,352
MTRP	122,873,000	126,780,622
Mortgages	27,466,653	27,120,607
Real Estate	8,224,902	8,351,430
Total	$ 1,992,794,529	$ 2,961,960,652

Securities Lending - Under the provisions of state statutes, BOI authorized the custodial bank to lend the BOI securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. The custodial bank is required to maintain collateral equal to 102 percent of the fair value of domestic securities and 105 percent of the fair value of international securities while the securities are on loan. The BOI and the custodial bank split the earnings on security lending activities. The securities lending collateral, securities lending collateral liability, securities lending income, and securities lending expense consist of allocations to TRS on a pro rata basis of its ownership share of each pool with securities lending activity. At June 30, 2008, and 2007, the BOI had no credit risk exposure to borrowers because the collateral pledged by the borrowers exceeded the value of the securities borrowed. The private equity and real estate Pools do not participate in securities lending.

Mortgages and Real Estate – The mortgages consist of a portfolio of Montana residential mortgages and the real estate holdings represent an equity interest in four real estate properties.

The investment risks for the pooled investments that TRS participates in are described in the following paragraphs.

Credit Risk – Credit risk is defined as the risk that an issuer or other counterparty to an investment will not fulfill its obligation.

Custodial Credit Risk - Custodial credit risk is the risk that, in the event of the failure of the counterparty to a transaction, the BOI may not be able to recover the value of the investment or collateral securities that are in the possession of an outside party.

Concentration of credit risk – Concentration of credit risk is the risk of loss attributed to the magnitude of an investor's investment in a single issuer.

Foreign Currency Risk – Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment.

Interest Rate Risk – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. In accordance with GASB Statement No. 40, the BOI selected the effective duration method to disclose interest rate risk.

All securities in pools are held in the name of the Montana BOI, or were registered in the nominee name for the Montana BOI and held in the possession of the BOI's custodial bank. MDEP, MTIP, MPEP, and MTRP do not invest in debt securities, so interest rate risk, credit risk, and concentration of credit risk do not apply to these holdings. MTIP, MPEP, and MTRP include assets subject to foreign currency risk. At June 30, 2008 approximately 36% of the combined portfolios are held in foreign currencies.

According to GASB Statement No. 40, interest rate disclosures are not required for STIP since STIP is a 2a7-like pool. RFBP has an effective duration of 4.63 and 5.27 for the pool at June 30, 2008, and 2007, respectively.

NOTE C. CONTRIBUTIONS

The TRS funding policy provides for monthly employee and employer contributions at rates specified by state law. Plan members are currently required to contribute 7.15% of their earned compensation and the current employer contribution rate is 9.47% of earned compensation. The State's General Fund contributes 2% of earned compensation by school district and community college members and an additional .11% of total earned compensation. Each employer in the Montana university system shall contribute to the TRS a supplemental employer contribution currently at a rate of 4.72% of the total compensation of employees participating in the Optional Retirement Program (ORP). An actuary determines the actuarial implications of the funding requirement in annual actuarial valuations. The actuarial method used to determine the implications of the statutory funding level is the entry age actuarial cost method, with both normal cost and amortization of the accrued liability determined as a level percentage of payroll.

The Montana State Legislature during the 2007 session infused $50 million from the State's General Fund into the TRS pension fund to help address the unfunded actuarial accrued liability of the system. The 2007 Legislature in going forward also addressed the funding status of the TRS pension fund to help ensure the unfunded actuarial accrued liability (UAAL) can be amortized over a period not exceeding 30 years. Per Governmental Accounting Standards Board (GASB) statement number 25 the maximum acceptable amortization period is 30 years. Effective July 1, 2007 the employer contribution rate increased 2% from 7.47% to 9.47%. Beginning July 1, 2009 the rate will increase another .38% to a total of 9.85%. Also the supplemental contribution to ensure university member benefits are funded by university employers was increased from 4.04% to 4.72% of Optional Retirement Plan (ORP) member pay effective July 1, 2007.

NOTE D. FUNDED STATUS and FUNDING PROGRESS

Our most recent actuarial valuation may be accessed on our website at:
www.trs.mt.gov/Board/ActuarialValuations/ActuarialValuations

The funded status of the TRS plan as of July 1, 2008 the most recent actuarial valuation date is as follows (dollar amounts in millions):

Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a) /c)
$3,159.1	$4,110.8	$794.6	79.9%	$689.5	115.2%

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

Valuation date	July 1, 2008
Actuarial cost method	Entry age
Amortization method	Level percent open
Remaining amortization period	31.3 years
Asset valuation method	4-year smoothed market
Actuarial assumptions:	
Investment rate of return	7.75%
Projected salary increases	4.50%
Guaranteed annual benefit adjustment	1.50%
Inflation rate	3.50%

The actuarial valuation prepared as of July 1, 2008, the most recent valuation date, indicates the statutory rate is insufficient to fund the normal cost and to amortize the unfunded accrued liability under the entry age actuarial cost method over 30 years.

On a market value basis the TRS earned $271 million more than anticipated by the 7.75% assumption for the year ended June 30, 2007 and $401 million less than anticipated by the 7.75% assumption for the year ended June 30, 2008. The net result as of July 1, 2008 is that the market value of assets is $166 million less than the actuarial value of assets. This $166 million in unrecognized asset losses, if not offset by future gains, will cause the contributions needed to amortize the UAAL in future valuations to increase even further. Therefore, to remain financially sound in the future, TRS will need either (1) future gains such as asset returns greater than the 7.75% assumption, or (2) an increase in contribution rates.

NOTE E. OTHER POSTEMPLOYMENT BENEFITS

For the fiscal year ending June 30, 2008, the TRS implemented the provisions of Governmental Accounting Standards Board (GASB) Statement No. 45 – Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions (OPEB). This statement requires disclosure of employer participation in defined benefit OPEB plans. The resulting TRS liability and expense for fiscal year 2008 has been reported in our financial statements.

Plan Description

TRS employees and dependents are eligible to receive health care through the State Group Benefits Plan administered by the Montana Department of Administration (MDOA). In accordance with section 2-18-704, MCA, the State provides optional post-employment medical, vision and dental health care benefits for retirees and their dependents and beneficiaries that elect to continue coverage and pay administratively established premiums. Plan coverage is on a calendar year basis. For GASB 45 reporting, the State Group Benefits Plan is considered an agent multiple-employer plan and TRS is considered to be a separate employer participating in the plan. Information about the State of Montana OPEB can be obtained from the Department of Administration, State Accounting Division, at P.O. Box 200102, Helena, MT 59620-0102.

Funding Policy

The contribution requirements of plan members are established and may be amended by the MDOA. The monthly premium for plan members ranges from $160 to $851 for 2008 depending on the medical plan selected, family coverage, and Medicare eligibility. The plan is financed on a pay-as-you-go basis.

GASB 45 requires the plan's employers to report each year the annual required contribution (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The 2008 ARC is calculated for all the plan's employers and then allocated to each participating employer. The TRS 2008 ARC is $47,478 and is based on the plan's current ARC rate of 7.99% percent of total annual covered payroll for all employers. The 2008 ARC is equal to an annual amount required each year to fully fund the liability over 30 years. The amount of the estimated OPEB actuarial accrued liability at transition was determined in accordance with the GASB Statement 45, and the liability for TRS is estimated at $548,418. (The actuarial accrued liability is the present value of future retiree benefits and expenses.)

Annual OPEB Cost

For fiscal year 2008, the TRS allocated annual OPEB cost (expense) of $47,478 was equal to the ARC. The TRS annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the net OPEB obligation for 2008 are as follows:

Fiscal Year Ended	Percentage of Annual OPEB Cost	Net Annual OPEB Cost Contributed	OPEB Obligation
6/30/08	0%	$47,478	$47,478

Funded Status and Funding Progress

The funded status of the TRS allocation of the plan as of January 1, 2007, the most recent valuation date was as follows:

Actuarial accrued liability (AAL)	$548,418
Actuarial value of plan assets	$ 0
Unfunded actuarial accrued liability (UAAL)	$548,418
Funded ratio (actuarial value of plan assets/AAL)	0
TRS Covered payroll (active plan members)	$634,670
UAAL as a percentage of covered payroll	86.41%

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions

As of January 1, 2007, the TRS actuarially accrued liability (AAL) for benefits was $548,418, with no actuarial value of assets, resulting in an unfunded actuarial accrued liability (UAAL) of $548,418, and the ratio of the UAAL to the covered payroll was 86.41%. The UAAL is being amortized as a level dollar amount over an open basis for 30 years.

In the January 1, 2007, actuarial valuation, the projected unit credit funding method was used for the State. The actuarial assumptions included a 4.25% discount rate and a 3.00% payroll growth rate. The projected annual healthcare cost trend rate is 7.00% for medical and 13.30% for prescription drugs, initially. Prescription drugs are reduced by decrements to a rate of 5.00% after eight years. Medical costs increase to 8.00% for the next three years. Then, these costs are reduced by decrements to a rate of 5.00% after five additional years.

TEACHERS' RETIREMENT SYSTEM
A COMPONENT UNIT OF THE STATE OF MONTANA
REQUIRED SUPPLEMENTARY INFORMATION

SCHEDULE OF FUNDING PROGRESS
(All dollar amounts in millions)

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liabilities (AAL)(1)	Present Value of Future University Supplemental Contributions	Unfunded Actuarial Accrued Liabilities (UAAL)(2)	Funded Ratio(3)	Covered Payroll(4)	UAAL as a Percentage of Covered Payroll
July 1, 2002	2,484.8	2,980.1	111.8	383.5	86.6	563.2	68.1
July 1, 2004	2,485.7	3,359.2	115.7	757.8	76.6	600.7	126.2
July 1, 2005	2,497.5	3,527.0	126.2	903.3	73.4	612.6	147.5
July 1, 2006	2,745.8	3,733.6	124.7	863.1	76.1	636.0	135.7
July 1, 2007	3,006.2	3,928.5	153.4	768.9	79.6	664.1	115.8
July 1, 2008	3,159.1	4,110.8	157.1	794.6	79.9	689.5	115.2

(1) Actuarial present value of benefits less actuarial present value of future normal costs based on entry age actuarial cost method.
(2) Actuarial accrued liabilities less actuarial value of assets and present value of future university supplemental contributions.
(3) Funded Ratio is the ratio of the actuarial value of assets over the actuarial accrued liabilities less the present value of future university supplemental contributions.
(4) Covered Payroll includes compensation paid to all active employees on which contributions are calculated.

TEACHERS' RETIREMENT SYSTEM
A COMPONENT UNIT OF THE STATE OF MONTANA
REQUIRED SUPPLEMENTARY INFORMATION

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYERS AND OTHER CONTRIBUTING ENTITIES

(All dollar amounts in thousands)

Fiscal Year Ending	Covered Employee Payroll[(1)]	Actual Employer Contributions[(2)]	Actual Employer Contribution %[(2)]	Annual Required Contribution (ARC) %[(3)]	Percentage of ARC Contributed[(4)]
June 30, 2003	597,131	53,277	7.58	7.58	100
June 30, 2004	600,728	55,774	7.58	7.58	100
June 30, 2005	612,622	57,150	7.58	7.58	100
June 30, 2006	635,997	158,962	7.58	10.45	223
June 30, 2007	664,140	112,664	7.58	11.64	130
June 30, 2008	689,460	81,423	9.58	9.58	100

(1) *Computed as the dollar amount of the actual employer contribution made as a percentage of payroll (less ORP and term pay contributions) divided by the contribution rate expressed as a percentage of payroll for fiscal years ending on or before June 30, 2007. For the fiscal year ending June 30, 2008 this figure is provided by the Retirement System.*

(2) *The actual and required employer contributions are expressed as a percentage of payroll. Contributions for termination pay of $6,585,334 and supplemental university contributions of $7,644,302 are included in the $81,422,610 actual employer dollar contribution, but are not made as a set percentage of payroll, and do not help to satisfy the ARC. Therefore, they are not included in the 9.58% employer contribution shown in this exhibit, or the calculation of the percentage of ARC contributed. The $50 million one time contribution made by the State in FYE 2007 and the $100 million one-time contribution made by the State in FYE 2006 are included in the employer dollar contribution, and the calculation of the percentage of ARC contributed, but are not included in the 7.58% employer contribution shown in this exhibit.*

(3) *The State makes employer contributions as a percentage of actual payroll. Thus, as long as the percentage equals the percentage required by the most recent actuarial valuation, the dollar amount of the Annual Required Contributions (ARC) is equal to the actual dollar amount of the required employer contributions. The 2008 ARC was determined in the July 1, 2006 valuation as the amount needed starting July 1, 2007 to maintain a 30 year amortization period.*

(4) *This is the Actual Employer Contribution expressed as a percentage of the product of the ARC percent and the Covered Employee Payroll.*

TEACHERS' RETIREMENT SYSTEM
A COMPONENT UNIT OF THE STATE OF MONTANA
NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION

Actuarial Cost Method

The actuarial valuation was prepared using the entry age actuarial cost method. Under this method, the actuarial present value of the projected benefits of each individual included in the valuation is allocated as a level percentage of the individual's projected compensation between entry age and assumed exit. The portion of this actuarial present value allocated to a valuation year is called the normal cost. The normal cost was first calculated for each individual member. The normal cost rate is defined to equal the total of the individual normal costs, divided by the total pay rate.

The portion of this actuarial present value not provided for at a valuation date by the sum of (a) the actuarial value of the assets and (b) the actuarial present value of future normal costs is called the unfunded actuarial accrued liability. The unfunded actuarial accrued liability is amortized as a level percentage of the projected salaries of present and future members of the System.

The ultimate cost of any pension program over time equals the benefits paid and expenses incurred while administering the program. The source of revenue used to pay for this cost is equal to the contribution from employers and employees to fund the program, plus investment return earned on contributions made through pre-funding the benefit payments.

Valuation of Assets - Actuarial Basis

Assets are valued based on their market value, with a four-year smoothing of all market value gains and losses. The expected return is determined for each year based on the beginning of year market value and actual cash flows during the year. Any difference between the expected market value return and the actual market value return is recognized evenly over a period of four years. The gains and losses are measured starting with the year ended June 30, 2007 (adopted 7/1/2007). The method of measuring the System's actuarial assets has changed since the prior valuation. Asset gains and losses are smoothed over a four-year period as of July 1, 2007, beginning with gains and losses over the year ending on June 30, 2007. As of July 1, 2006, the System's assets were measured on a market value basis, with immediate recognition of all gains and losses. Prior to 2006, asset gains and losses were smoothed over a five-year period.

Inflation Rate

The assumed inflation rate is 3.50% per annum, compounded annually (adopted 7/1/2004).

Investment Earnings

The annual rate of investment earnings of the assets of the System is assumed to be 7.75% per year, compounded annually. (Adopted July 1, 2004)

Guaranteed Annual Benefit Adjustment Increases
On January 1 of each year, the retirement allowance payable must be increased by 1.5% if the retiree's most recent retirement effective date is at least 36 months prior to January 1 of the year in which the adjustment is to be made.

Future Salaries
The rates of annual salary increases assumed for the purpose of the valuation include an assumed 4.5% annual rate of increase in the general wage level of the membership plus a variable merit and longevity rate from 0% to 4.51%. The merit and longevity increases for the Montana University System (MUS) members did not show a pattern of increasing or decreasing with service at the time of our most recent study. Therefore, the MUS members have a flat 1% merit and longevity assumption. The general wage increase assumption was adopted July 1, 2004 and the merit and longevity scales were adopted July 1, 2002.

MUS members are assumed to have a 0.63% higher average final compensation to account for the larger than average annual compensation increases observed in the years immediately preceding retirement.

Amortization Method
The unfunded actuarial accrued liability created by this method, including gains and losses, is amortized as a level percentage of the System's projected payroll.

Amortization Period
The amortization period of the unfunded actuarial liability over an open period is 31.3 years as of July 1, 2008.

REQUIRED SUPPLEMENTARY INFORMATION
OTHER POSTEMPLOYMENT BENEFITS PLAN INFORMATION

Other Postemployment Benefits Plan Information (1)
Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability(AAL) Entry Age (b)	Unfunded (UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL as Percentage of Covered Payroll ((b-a)/c)
1/1/2007	-	$548,418	$548,418	0.00%	$634,670	86.41%

(1) TRS and the State of Montana implemented GASB Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions, for the fiscal year ended June 30, 2008. Information for prior years is not available.

TEACHERS' RETIREMENT SYSTEM
A COMPONENT UNIT OF THE STATE OF MONTANA
SUPPORTING SCHEDULES
FISCAL YEARS ENDED JUNE 30, 2008 AND 2007

SCHEDULE OF ADMINISTRATIVE EXPENSES

Expenses for the administration of the plan, excluding compensated absences, depreciation and amortization, are budgeted and approved by the TRS Board. The administrative costs of the TRS are financed through realized investment income. The expenses, less amortization of intangible assets, may not exceed 1.5% of retirement benefits paid. Administrative expenses for the fiscal years ended June 30, 2008 and 2007 are outlined below:

	2008	2007
Budgeted Expenses:		
Personnel Services:		
Salaries	$ 720,003	$ 675,800
Other Compensation	2,750	2,750
Employee Benefits	223,647	205,418
Total Budgeted Personal Srvs	$ 946,400	$ 883,968
Operating Expenses:		
Contracted Services	$ 426,746	$ 231,943
Supplies & Material	22,909	25,350
Communications	37,285	33,289
Travel	21,642	21,817
Rent	58,433	48,046
Repair & Maintenance	49,892	42,235
Other Expenses	72,106	48,926
Total Budgeted Operating Exp	$ 689,013	$ 451,876
Non-Budgeted Expenses:		
Compensated Absences	$ 18,787	$ 14,008
Depreciation	20,273	5,403
Amortization of Intangible Assets	76,292	78,848
Total Non-Budgeted Expenses	$ 115,352	$ 98,259
Total Administrative Expenses	**$ 1,750,765**	**$ 1,434,103**

SCHEDULE OF PAYMENTS TO CONSULTANTS

	2008	2007
Actuarial Services	$ 141,616	$ 55,685
Personnel Services	1,095	1,045
Legal Services	24,161	4,556
Medical Evaluations	815	390
Information Technology Services	51,360	13,520
Total Consultant Payments	**$ 219,047**	**$ 75,196**

Teachers' Retirement System

System's Response

TEACHERS' RETIREMENT SYSTEM

B-3

1500 E. SIXTH AVENUE
PO BOX 200139
HELENA, MONTANA 59620-0139 (406) 444-3134 BRIAN SCHWEITZER, GOVERNOR

STATE OF MONTANA

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NOV 26 2008
LEGISLATIVE AUDIT DIV.

November 26, 2008

Tori Hunthausen
Legislative Auditor
Room 160 State Capitol
PO Box 201705
Helena MT 59620-1705

Dear Ms. Hunthausen:

The Teachers' Retirement Board appreciates the services provided by your staff in reviewing the financial statements of the Teachers' Retirement System (TRS).

This past year the funded ratio of the System increased from 79.6% at July 1, 2007, to 79.9% at July 1, 2008. However, the amortization period also increased from 28.6 years to 31.3 years. A contribution rate increase of 0.17% of pay effective July 1, 2009, or a combination of liability reductions, supplemental cash contributions, or contribution rate increases will be necessary to bring the amortization period below 30 years as required by governmental accounting standards.

The report includes two recommendations: That the System take necessary measures to ensure the System is funded on an actuarially sound basis, and that the System document procedures to monitor and test internal controls. We concur with both recommendations. The Board has identified "measures" to reduce liabilities and increases contributions, currently drafted as LC 263, and looks forward to working with the Audit Committee to identify other "measures" that may be necessary to reduce the unfunded actuarially accrued liabilities. The challenge for us all will be to identify what measures will be most successful in the current uncertain and volatile economic climate.

Legislative Audit Committee
November 26, 2008
Page 2

In addition, we will document the procedures currently used to monitor and test internal controls. This documentation will be presented to the TRS Board for approval at their February 2009 board meeting.

Thank you for the opportunity to reply to the audit report for the Teachers' Retirement System.

Sincerely,

David L. Senn
Executive Director