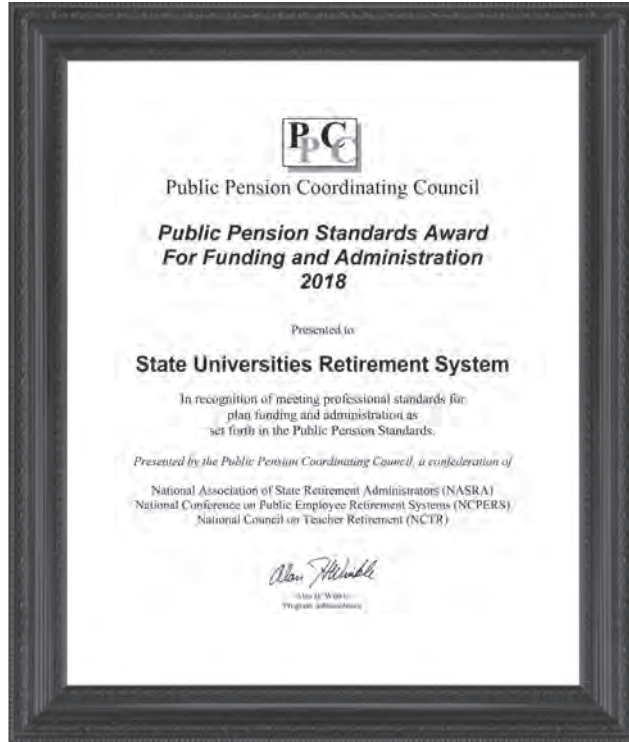


# INTRODUCTORY

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## SERVING MEMBERS FIRST

*Offering the best education, assistance and counseling for members, retirees and beneficiaries*



## LETTER OF TRANSMITTAL



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 800-275-7877 • 217-378-8800 • (Fax) 217-378-9800  
[www.surs.org](http://www.surs.org)

December 14, 2018

Board of Trustees and Executive Director  
 State Universities Retirement System  
 1901 Fox Drive  
 Champaign, IL 61820

I am pleased to present the 77th Comprehensive Annual Financial Report for the State Universities Retirement System of Illinois (SURS or the System, a component unit of the State of Illinois) for the fiscal year ended June 30, 2018.

The System was established in 1941 for the benefit of the employees of the state universities, community colleges, and certain other state educational and scientific agencies, and the survivors, dependents, and other beneficiaries of those employees. Our vision is to continue to be a respected leader among public pension funds. The SURS staff works hard to perform at the highest customer service level for our members who dedicate their careers to education.

The management of SURS is responsible for the compilation and accuracy of the financial, investment, actuarial, and statistical information contained in this report. To the best of our knowledge and belief, the enclosed information is accurate in all material respects and is reported in a manner designed to present fairly the financial position and results of operations of SURS.

Management is responsible for establishing and maintaining adequate internal controls over financial reporting. SURS' internal controls over financial reporting are designed to provide reasonable assurance regarding safekeeping of assets and reliability of financial records in accordance with generally accepted accounting principles. These controls include appropriate segregation of duties and responsibilities, and sound practices in the performance of those duties. The cost of a control should not exceed the benefits likely to be derived. The valuation of costs and benefits requires estimates and judgments by management. The objective of internal controls is to provide reasonable, rather than absolute, assurance that the financial statements are free of any material misstatements.

SURS maintains an internal audit program that employs the services of three internal auditors to determine that all controls implemented are as designed. The internal audit personnel use a detailed internal audit program to provide a continuing review of the SURS internal controls and to report audit findings and recommendations for improvements to the SURS Board of Trustees. There are inherent limitations in the effectiveness of any system of internal controls, including the possibility of human error and the circumvention or overriding of controls.

The Illinois Pension Code requires an annual audit of the financial statements of the System by independent accountants selected by the State Auditor General. This requirement has been complied with, and the independent auditor's unmodified report on the System's 2018 financial statements has been included in this report.

Accounting principles generally accepted in the United States of America 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 the MD&A and should be read in conjunction with it. The System's MD&A can be found starting on page 16 of the report.

### Profile

SURS is the administrator of a cost-sharing, multiple-employer public employee retirement system established July 21, 1941, to provide retirement annuities and other benefits for employees, survivors and other beneficiaries of those employees of the state universities, community colleges, and certain other state educational and scientific agencies. SURS services 61 employers and approximately 233,000 members and annuitants. The plans administered by SURS include a defined benefit plan established in 1941 and a defined contribution plan established in 1998. SURS is governed by an 11-member board of trustees that includes four members elected, two annuitants elected, and five members appointed by the Governor, of which the chairperson is the appointed chair of the Illinois Board of Higher Education.

# LETTER OF TRANSMITTAL

## Funding

SURS is funded through contributions from non-employer, employer and employee contributions as well as investment earnings. The State of Illinois, a non-employer contributing entity, provides funding from two sources: the general Revenue Fund and the State Pensions Fund, which is funded with proceeds from unclaimed property. Annually, the SURS actuary determines the annual "statutory contribution" needed to meet current and future benefit obligations in accordance with the Illinois Pension Code, which sets forth the manner of calculating the statutory contribution under the Statutory Funding Plan. The Statutory Funding Plan requires the state to contribute annually an amount equal to a constant percent of pensionable (capped) payroll necessary to allow the System to achieve a 90% funded ratio by fiscal year 2045, subject to any revisions necessitated by actuarial gains or losses, or actuarial assumptions. The majority of the \$1.6 billion statutory contribution for fiscal year 2018 was received through continuing appropriation based on 40 ILCS 15/11(b). As of June 30, 2018, the plan net position as a percentage of the total pension liability was 41.27%. The funding issue confronting SURS continues to represent a challenge to the System. Although the statutory contribution requirement was met in fiscal year 2018, the Statutory Funding Policy creates a perpetual contribution variance of underfunding the System in earlier years. In later years, the statutory contribution would exceed a contribution equal to normal cost plus a 30-year closed period level percent of pay amortization of the unfunded liability. Further information is presented in the Required Supplementary Information related to employer contributions and the funding of the plan.

## Investments

Investments are made under the authority of the prudent expert rule, which states that fiduciaries must discharge their duties with the care, skill, prudence, and diligence that a prudent person acting in a like capacity and familiar with such matters would use under conditions prevailing at the time. This standard has enabled the System to invest in different types of asset classes seeking to increase return while lowering risk through diversification.

The System retains professional investment firms who serve as fiduciaries and are afforded full discretion to manage the assets entrusted to them in accordance with written policies and guidelines established by the board of trustees. Our goal is to optimize the long-term return of the System's investments.

The SURS defined benefit plan net position increased to \$19.3 billion. The Investment section of this report contains yield information, a summary of SURS' investment portfolio, and a summary of the investment objectives and policies. Taken as a whole, the SURS portfolio of investments produced a return of 8.2%, net of fees, for the year ended June 30, 2018. The SURS investment program has a long-term horizon. The returns, net of fees, are 6.8% over the last three years and 6.7% over the last 10 years. The SURS defined contribution (Self-Managed Plan) assets increased from \$2.2 billion to \$2.5 billion.

The SURS defined benefit plan assets show a negative return of 2.06% through October 31, 2018, bringing the total defined benefit plan investments to approximately \$18.6 billion.

## Legislation

*Public Act 100-0554* was signed into law on November 16, 2017, and requires that each officer, member, employee, and each natural person required to register as a lobbyist to complete, at least annually, a sexual harassment training program.

*Public Act 100-0040* was signed into law on August 8, 2017, to amend the Data Security on State Computers Act. It requires every employee to annually undergo training by the Department of Innovation and Technology concerning cybersecurity.

*Public Act 100-0023* was signed into law on July 6, 2017 and included a provision for creating an optional hybrid pension plan that would be available to current Tier II members and future new hires. The law also requires that:

- Beginning in fiscal year 2018, the employer will be responsible for: (1) the employer normal cost of the defined benefits of optional hybrid plan participants and the employer normal cost of the defined benefits of participants who would have been in the optional hybrid plan but elected to participate in the Tier II plan; and (2) the unfunded liability of the defined benefits of optional hybrid plan participants, participants who would have been in the optional hybrid plan but elected to participate in the Tier II plan, and participants who currently participate in the Tier II plan but elect to participate in the optional hybrid plan.
- Beginning in FY 2021, the employer will pay a 2% surcharge for optional hybrid plan participants and participants who would have been in the optional hybrid plan but elected to participate in the Tier II plan.

## LETTER OF TRANSMITTAL

- The employer pays the employer normal cost of the portion of an employee's earnings that exceed the amount of salary set for the Governor, for the academic year beginning on or after July 1, 2017.

Implementation of the optional hybrid plan created by PA 100-0023 is pending. SURS is awaiting further legislation to clarify language regarding the creation of the defined contribution program and to resolve conflicts between the law and the Internal Revenue Code.

### Major Initiatives

In fiscal year 2018, SURS staff worked to implement legislative changes, advance investment policy, strengthen the System's security, create new educational tools, and complete a board election.

- Technology is always at the forefront of efficiency and security, and over the years SURS has consistently improved our systems and updated our equipment. This past year our IT team:
  - Deployed a cloud-based VOIP solution to enhance the service rendered to our members.
  - Migrated to a cloud-hosted Disaster Recovery solution; thereby reducing our recovery time from business days to business hours.
  - Began a migration to a cloud-hosted email and collaboration suite that will allow for optimized workforce interactions.
  - Added a chief technology officer (CTO) to oversee future updates. The CTO will manage application development and research, as well as facility operations.
- SURS united its member services and outreach teams under one director for better, more cohesive customer service. Education efforts focused on providing useful, electronic information to help members in all stages of their careers prepare for retirement, including webinars, online information, and email communication.
- In February 2018, the SURS Board of Trustees approved hiring PCA as its general investment consultant for a five-year term.
- In March 2018, the board hired Cammack Retirement Group as the System's defined contribution consultant.
- In April 2018, the Self-Managed Plan began working with a dedicated defined contribution (DC) consultant to improve member education and fund choices.
- SURS held a board election April 2 – May 1, 2018. Steven Rock and Collin Van Meter were elected on May 2 to serve on the SURS Board of Trustees by the System's active members. John Engstrom was elected to serve as an annuitant trustee. All are serving six-year terms which began July 15, 2018. Voting was handled exclusively by Election-America, an impartial election service company.

### Awards and Recognition

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to SURS for its component unit financial report for the fiscal year ended June 30, 2017. This is the thirty-fourth consecutive year the System has earned this award.

To be awarded the Certificate of Achievement, a governmental unit must publish an easily readable and efficiently organized comprehensive annual financial report whose contents conform to program standards. The 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.

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

The Public Pension Coordinating Council (PPCC), a coalition of three national associations that represents more than 500 of the largest pension plans in the U.S., awarded SURS the *Public Pension Standards Award for Funding and Administration*. Public Pension Standards are a benchmark to measure public defined benefit plans in the areas of retirement system management, administration, and funding.

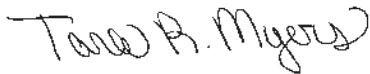
## LETTER OF TRANSMITTAL

### **Acknowledgements**

This report was prepared through the combined effort of the SURS staff under the leadership of the Board of Trustees. It is intended to provide reliable information to its users for making decisions and for determining responsible stewardship for the assets contributed by the members and the State of Illinois.

The report is made available to the Governor, the State Auditor General, the members of the General Assembly, participating employers, and to other interested persons by request. We thank all those whose impact in Illinois' universities and colleges guide the future. We hope they will find this report informative. A copy of this report and our Annual Report Summary will be available on our website, [www.surs.org](http://www.surs.org).

Respectfully submitted,



Tara R. Myers  
Chief Financial Officer

BOARD OF TRUSTEES



**Tom Cross**  
Chairperson  
Appointed



**John Engstrom**  
Vice Chairperson  
Elected



**Dennis Cullen**  
Appointed  
Treasurer



**Aaron Ammons**  
Elected



**Mark Cozzi**  
Appointed



**J. Fred Giertz**  
Elected



**Paul R. T. Johnson Jr.**  
Appointed



**Craig McCrohon**  
Appointed

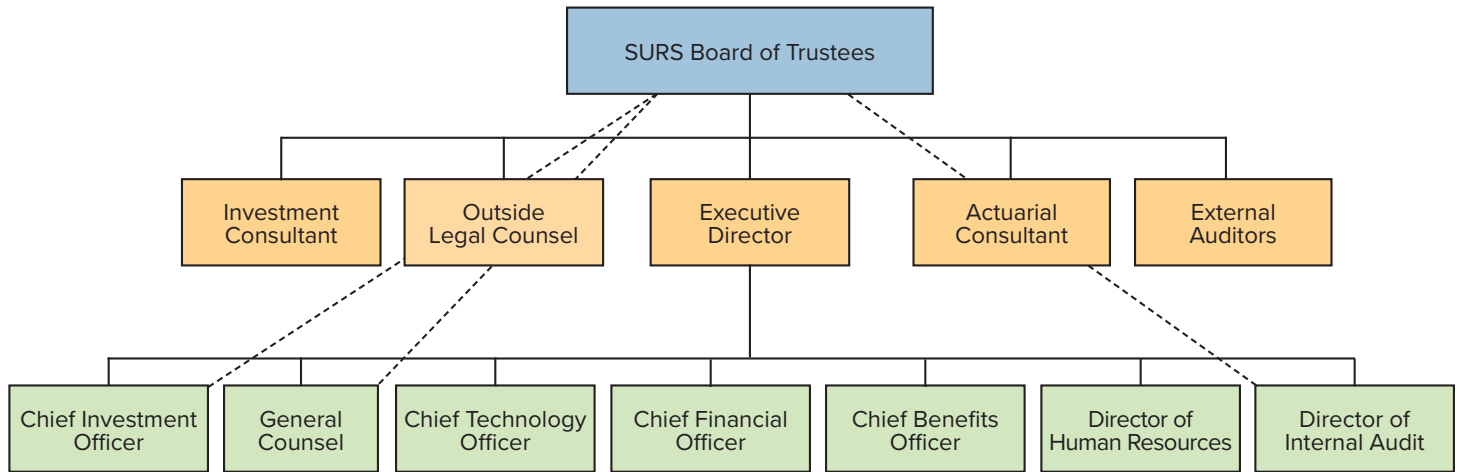


**Steven Rock**  
Elected



**Antonio Vasquez**  
Elected

## ORGANIZATIONAL CHART



## EXECUTIVE TEAM

Executive Director .....	Martin Noven
Chief Investment Officer .....	Douglas Wesley
General Counsel .....	Bianca Green
Chief Technology Officer .....	Jefferey Saiger
Chief Financial Officer .....	Tara Myers
Chief Benefits Officer .....	Suzanne Mayer
Director of Human Resources .....	Brenda Dunn
Director of Internal Audit .....	Steve Hayward



## CONSULTING AND PROFESSIONAL SERVICES

### Actuary

Gabriel, Roeder, Smith & Co.

### Auditor

BKD, LLP (Acting as Special Assistant Auditor for the Illinois Office of Auditor General)

### Legal Counsel

Burke Burns & Pinelli, Ltd.

Ice Miller LLP

Jackson Walker LLP

Mayer Brown LLP

Squire Patton Boggs

### Consultants and Other Vendors

Glass Lewis & Co. LLC

Mesirow Insurance Services

SecureWorks Inc.

Upkeep Maintenance Service

Springfield Electric

Tave Risk Management

### Master Trustee and Custodian

The Northern Trust Company

### Investment Consultants, Measurement and Counsel

NEPC, LLC

Pension Consulting Alliance

### Investment Advisors

Adams Street Partners

Alinda Capital Partners

AQR Capital Management

BlackRock Institutional Trust Company

BlueBay Asset Management

Blue Vista Capital Management

Brookfield Asset Management

CastleArk Management

Colchester Global Investors

Courtland Partners

Crow Holdings

Deutsche Bank

Dune Capital Management

Fidelity Institutional Asset Management

Franklin Templeton Real Estate Advisors

Heitman Capital Management

Invesco

J.P. Morgan Asset Management

KKR Prisma

Macquarie Capital

Mesirow Financial Investment Management

Mondrian Investment Partners

Neuberger Berman

Northern Trust Asset Management

Oaktree Capital Management

Pacific Alternative Asset Management Company

Pacific Investment Management Company

Pantheon Ventures

Parametric Clifton

Progress Investment Management Company

Prudential Fixed Income

RhumbLine Advisers

RREEF

State Street Global Advisors

T. Rowe Price

TCW

UBS Realty Investors

Wellington Management Company

### Manager Diversity Program Investment Advisors

Ativo Capital Management

Basis Management Group

Channing Capital Management

Denali Advisors

EARNEST Partners

Fairview Capital Partners

Franklin Templeton Real Estate Advisors

Garcia Hamilton & Associates

Gladius Capital Management

GlobeFlex Capital

LM Capital Group

Matarin Capital Management

Muller and Monroe Asset Management

Piedmont Investment Advisors

Pugh Capital Management

Smith Graham & Company

Strategic Global Advisors

### Progress Investment Management Company Emerging Manager Investment Advisors

Affinity Investment Advisors

ARGA Investment Management

Brown Capital Management

Denali Advisors

Garcia Hamilton & Associates

GIA Partners

Glovista Investments

Integrity Fixed Income Management

LM Capital Group

New Century Advisors

Piedmont Investment Advisors

Ramirez Asset Management

Solstein Capital

Strategic Global Advisors

### Self-Managed Plan Service Providers

Fidelity Investments

Teachers Insurance Annuity Association

Schedule of Fees and Commissions can be found in the Investment Section Supporting Schedules, pages 72-74.

