# FLORIDA RETIREMENT SYSTEM

## REVISED AND FINAL GASB 67 DISCLOSURE
## Fiscal Year: July 1, 2013 to June 30, 2014

**Prepared by**

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**February 24, 2015**

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# Certification

Actuarial computations presented in this report under Statement No. 67 of the Governmental Accounting Standards Board are for purposes of assisting the FRS in fulfilling its financial accounting requirements. No attempt is being made to offer any accounting opinion or advice. This report is for fiscal year July 1, 2013 to June 30, 2014. The reporting date for determining plan assets and obligations is June 30, 2014. The calculations enclosed in this report have been made on a basis consistent with our understanding of the plan provisions. Determinations for purposes other than meeting financial reporting requirements may be significantly different than the results contained in this report. Accordingly, additional determinations may be needed for other purposes, such as judging benefit security or meeting employer funding requirements.

In preparing this report, we relied, without audit, on information as of June 30, 2013 and June 30, 2014 furnished by the FRS. This information includes, but is not limited to, statutory provisions, member census data, and financial information. Please note that this report is based on the June 30, 2014 assets for the program as reported to us by the Division of Retirement. Please see Milliman's funding valuation report dated November 26, 2014 for more information on the plan's participant group as of July 1, 2014 as well as a summary of the plan provisions and a summary of the actuarial methods and assumptions used for funding purposes.

We performed a limited review of the census and financial information used directly in our analysis and have found them to be reasonably consistent and comparable with information used for other purposes. The valuation results depend on the integrity of this information. If any of this information is inaccurate or incomplete our results may be different and our calculations may need to be revised.

We hereby certify that, to the best of our knowledge, this report, including all costs and liabilities based on actuarial assumptions and methods, is complete and accurate and determined in conformance with generally recognized and accepted actuarial principles and practices, which are consistent with the Actuarial Standards of Practice promulgated by the Actuarial Standards Board and the applicable Code of Professional Conduct and supporting Recommendations of the American Academy of Actuaries.

This valuation report is only an estimate of the Plan's financial condition as of a single date. It can neither predict the Plan's future condition nor guarantee future financial soundness. Actuarial valuations do not affect the ultimate cost of Plan benefits, only the timing of Plan contributions. While the valuation is based on an array of individually reasonable assumptions, other assumption sets may also be reasonable and valuation results based on those assumptions would be different. No one set of assumptions is uniquely correct. Determining results using alternative assumptions is outside the scope of our engagement.

Future actuarial measurements may differ significantly from the current measurements presented in this report due to factors such as, but not limited to, the following: plan experience differing from that anticipated by the economic or demographic assumptions; changes in economic or demographic assumptions; increases or decreases expected as part of the natural operation of the methodology used for these measurements (such as the end of an amortization period or additional cost or contribution requirements based on the plan’s funded status); and changes in plan provisions or applicable law. Due to the limited scope of the actuarial assignment, we did not perform an analysis of the potential range of such future measurements.

# Certification

Milliman's work is prepared solely for the internal use and benefit of the Florida Retirement System. To the extent that Milliman's work is not subject to disclosure under applicable public records laws, Milliman's work may not be provided to third parties without Milliman's prior written consent. Milliman does not intend to benefit or create a legal duty to any third party recipient of its work product. Milliman's consent to release its work product to any third party may be conditioned on the third party signing a Release, subject to the following exceptions: (a) the Plan Sponsor may provide a copy of Milliman's work, in its entirety, to the Plan Sponsor's professional service advisors who are subject to a duty of confidentiality and who agree to not use Milliman's work for any purpose other than to benefit the Fund; and (b) the Plan Sponsor may provide a copy of Milliman's work, in its entirety, to other governmental entities, as required by law.

No third party recipient of Milliman's work product should rely upon Milliman's work product. Such recipients should engage qualified professionals for advice appropriate to their specific needs.

The consultants who worked on this assignment are pension actuaries. Milliman's advice is not intended to be a substitute for qualified legal or accounting counsel.

The signing actuaries are independent of the plan sponsor. We are not aware of any relationship that would impair the objectivity of our work.

On the basis of the foregoing, we hereby certify that, to the best of our knowledge and belief, this report is complete and has been prepared in accordance with generally recognized accepted actuarial principles and practices. We are members of the American Academy of Actuaries and meet the Qualification Standards to render the actuarial opinion contained herein.

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# Overview of GASB 67 and GASB 68

The Governmental Accounting Standards Board (GASB) released new accounting standards for public pension plans and participating employers in 2012. These standards, GASB Statements No. 67 and 68, have substantially revised the accounting requirements previously mandated under GASB Statements No. 25 and 27. The most notable change is the distinct separation of funding from financial reporting. The Annual Required Contribution (ARC) has been eliminated under GASB 67 and 68 and is no longer relevant for financial reporting purposes. As a result, plan sponsors have been encouraged to establish a formal funding policy that is separate from financial reporting calculations.

GASB 67 applies to financial reporting for public pension plans and is required to be implemented for plan fiscal years beginning after June 15, 2013. Note that a plan's fiscal year might not be the same as each participating employer's fiscal year. Under GASB 67, enhancements to the financial statement disclosures are required, along with certain required supplementary information.

GASB 68 governs the specifics of accounting for public pension plan obligations for participating employers and is required to be implemented for employer fiscal years beginning after June 15, 2014. GASB 68 requires a liability for pension obligations, known as the Net Pension Liability, to be recognized on the balance sheets of participating employers. Changes in the Net Pension Liability will be immediately recognized as Pension Expense on the income statement or reported as deferred inflows/outflows of resources depending on the nature of the change.

# Relationship Between Valuation Date and Measurement Date

### Relationship Between Valuation Date and Measurement Date

The Valuation Date is July 1, 2014. This is the date as of which the actuarial valuation is performed. The Measurement Date is June 30, 2014

# Schedule of Employer Contributions

| Fiscal Year Ending June 30 | Actuarially Determined Contribution[1] | Actual Employer Contribution | Contribution Deficiency (Excess) | Covered Payroll[2] | Contribution as a % of Covered Payroll |
|---|---|---|---|---|---|
| 2005 | $2,141,862,000 | $2,177,492,000 | ($35,630,000) | $24,172,193,000 | 9.01% |
| 2006 | 2,193,928,000 | 2,096,884,000 | 97,044,000 | 25,314,566,000 | 8.28% |
| 2007 | 2,455,255,000 | 2,736,861,000 | (281,606,000) | 26,366,086,000 | 10.38% |
| 2008 | 2,612,672,000 | 2,796,651,000 | (183,979,000) | 26,872,418,000 | 10.41% |
| 2009 | 2,535,854,000 | 2,808,418,000 | (272,564,000) | 26,554,114,000 | 10.58% |
| 2010 | 2,447,374,000 | 2,721,618,000 | (274,244,000) | 25,747,369,000 | 10.57% |
| 2011 | 3,680,042,000 | 3,050,684,000 | 629,358,000 | 25,668,958,000 | 11.88% |
| 2012 | 1,962,816,000 | 1,185,310,000 | 777,506,000 | 24,476,272,000 | 4.84% |
| 2013 | 2,091,343,000 | 1,388,656,000 | 702,687,000 | 24,553,693,402 | 5.66% |
| 2014 | 2,190,424,344 | 2,190,424,344 | 0 | 24,723,564,758 | 8.86% |

[1] For fiscal years prior to 2013-14 the Annual Required Contribution under GASB Statement No. 27 is shown.

[2] Covered Payroll includes defined benefit plan actives and members in DROP. It excludes the payroll for Investment Plan members, and payroll on which only UAL rates are charged.

# Actuarial Methods and Assumptions Used for Funding Policy

The following actuarial methods and assumptions were used in the July 1, 2014 funding valuation. Please see the valuation report dated November 26, 2014 for further details.

| | |
|---|---|
| **Valuation Timing** | Actuarially determined contribution rates for a given plan year are calculated in the valuation conducted as of the beginning of the preceding plan year (e.g., rates for the 2015-2016 plan year are calculated in the 7/1/2014 actuarial valuation). |
| **Actuarial Cost Method** | Ultimate Entry Age Normal |
| **Amortization Method** | |
| Level percent or level dollar | Level percent |
| Closed, open, or layered periods | Closed, layered |
| Amortization period at 07/01/2014 | 30 years |
| Payroll growth rate | 3.25% |
| **Asset Valuation Method** | |
| Smoothing period | 5 years |
| Recognition method | Asymptotic |
| Corridor | 80% - 120% of fair market value |
| **Inflation** | 2.60% |
| **Salary Increases** | Varies by tier, membership class; details in valuation report |
| **Investment Rate of Return** | 7.65% |
| **Cost of Living Adjustments** | 3% for pre-July benefit 2011 service; 0% thereafter |
| **Retirement Age** | Varies by tier, membership class; details in valuation report |
| **Turnover** | Varies by tier, membership class; details in valuation report |
| **Mortality** | Generational RP-2000 with Projection Scale BB |

# Statement of Fiduciary Net Position

| | June 30, 2013 | June 30, 2014 |
|---|---|---|
| **Assets** | | |
| Cash and cash equivalents | $2,299,576,472 | $1,728,655,412 |
| Receivables and prepaid expenses: | | |
| Receivable contributions | 217,404,854 | 201,012,138 |
| Receivable investment income | 370,785,152 | 342,952,760 |
| Receivables from brokers for unsettled trades | 2,939,989,449 | 4,880,830,398 |
| Prepaid expenses | 22,221,061 | 105,587,293 |
| Total receivables | 3,550,400,516 | 5,530,382,589 |
| Investments: | | |
| Fixed income | 32,629,902,148 | 34,021,409,366 |
| Stocks | 78,667,012,553 | 89,902,475,739 |
| Short-term investments | 302,989,494 | 9,733,821 |
| Real estate | 9,041,199,549 | 9,910,892,909 |
| Alternative investments | 13,556,790,576 | 16,503,776,121 |
| Repurchase agreements | 750,000,000 | 1,150,000,000 |
| Total investments | 134,947,894,322 | 151,498,287,955 |
| Invested securities lending cash collateral | 3,245,416,854 | 4,618,259,793 |
| Capital assets net of accumulated depreciation | 0 | 0 |
| Post-audit adjustment to June 30, 2013 financials | 32,282,537 | N/A |
| Total assets | 144,075,570,701 | 163,375,585,749 |
| **Liabilities** | | |
| Other accrued expenses and benefits payable | 122,582,947 | 93,720,644 |
| Obligations under Securities Lending | 3,317,786,852 | 4,674,292,312 |
| Payable to brokers for unsettled trades | 7,573,523,999 | 8,593,280,421 |
| Total liabilities | 11,013,893,798 | 13,361,293,377 |
| **Net position restricted for pensions** | $133,061,676,904 | $150,014,292,372 |

# Statement of Changes in Fiduciary Net Position

| | June 30, 2014 |
|---|---|
| **Additions** | |
| Member contributions | $682,507,323 |
| Employer contributions | 2,190,424,344 |
| Total contributions | 2,872,931,667 |
| Transfers from other funds | 131,260,646 |
| Investment income (loss): | |
| Interest | 985,691,174 |
| Dividends | 2,201,178,475 |
| Net increase in fair value of investments | 19,454,778,191 |
| Securities lending income | 50,690,359 |
| Less investment expenses: | |
| Direct investment expense | 511,032,856 |
| Securities lending expense | 5,631,561 |
| Net investment income | 22,175,673,782 |
| Other income | 636,612,711 |
| Total additions | 25,816,478,806 |
| **Deductions** | |
| Benefit Payments[1] | 8,030,797,920 |
| Transfers to the Investment Plan | 807,719,753 |
| Refunds of member contributions | 6,993,783 |
| Administrative expenses | 18,351,882 |
| Total deductions | 8,863,863,338 |
| Net increase (decrease) | 16,952,615,468 |
| **Net position restricted for pensions** | |
| Beginning of year (June 30, 2013) | 133,061,676,904 |
| End of year (June 30, 2014) | $150,014,292,372 |

[1] Includes transfers to other funds and General Revenue funded benefit payments

# Money-Weighted Rate of Return

| Fiscal Year Ending June 30 | Net Money-Weighted Rate of Return |
|---|---|
| 2014 | 17.57% |

## Calculation of Money-Weighted Rate of Return

The money-weighted rate of return considers the changing amounts actually invested during a period and weights the amount of pension plan investments by the proportion of time they are available to earn a return during that period. External cash flows are determined on a monthly basis and are assumed to occur at the beginning of each month. External cash inflows are netted with external cash outflows, resulting in a net external cash flow in each month. The money-weighted rate of return is calculated net of investment expenses.

| | Net External Cash Flows | Periods Invested | Period Weight | Net External Cash Flows With Interest |
|---|---|---|---|---|
| Beginning Value - July 1, 2013 | $133,061,676,904 | 12 | 1.00 | $156,443,484,233 |
| Monthly net external cash flows: | | | | |
| July | (686,814,762) | 12 | 1.00 | (807,502,933) |
| August | (573,350,820) | 11 | 0.92 | (665,427,227) |
| September | (524,543,869) | 10 | 0.83 | (599,976,914) |
| October | (470,668,981) | 9 | 0.75 | (531,427,401) |
| November | (425,996,569) | 8 | 0.67 | (474,799,341) |
| December | (437,234,699) | 7 | 0.58 | (480,276,374) |
| January | (484,929,252) | 6 | 0.50 | (525,812,161) |
| February | (498,135,336) | 5 | 0.42 | (533,181,700) |
| March | (461,767,896) | 4 | 0.33 | (487,106,827) |
| April | (454,900,222) | 3 | 0.25 | (473,687,878) |
| May | (474,692,319) | 2 | 0.17 | (487,937,242) |
| June | (357,397,267) | 1 | 0.08 | (362,055,864) |
| Ending Value - June 30, 2014 | 150,014,292,372 | | | 150,014,292,371 |
| Money-Weighted Rate of Return | 17.57% | | | |

# Long-Term Expected Rate of Return

To develop an analytical basis for the selection of the long-term expected rate of return assumption, in September 2014 the FRS Actuarial Assumptions conference reviewed long-term assumptions developed by both Milliman's capital market assumptions team and by a capital market assumptions team from Hewitt EnnisKnupp, which consults to the Florida State Board of Administration. The table below shows Milliman's assumptions for each of the asset classes in which the plan was invested at that time based on the long-term target asset allocation. The allocation policy's description of each asset class was used to map the target allocation to the asset classes shown below. Each asset class assumption is based on a consistent set of underlying assumptions, and includes an adjustment for the inflation assumption. These assumptions are not based on historical returns, but instead are based on a forward-looking capital market economic model.

| Asset Class | Target Allocation* | Annual Arithmetic Return | Compound Annual (Geometric) Return | Standard Deviation |
|---|---|---|---|---|
| Cash | 1.00% | 3.11% | 3.10% | 1.65% |
| Intermediate-Term Bonds | 18.00% | 4.18% | 4.05% | 5.15% |
| High Yield Bonds | 3.00% | 6.79% | 6.25% | 10.95% |
| Broad US Equities | 26.50% | 8.51% | 6.95% | 18.90% |
| Developed Foreign Equities | 21.20% | 8.66% | 6.85% | 20.40% |
| Emerging Market Equities | 5.30% | 11.58% | 7.60% | 31.15% |
| Private Equity | 6.00% | 11.80% | 8.11% | 30.00% |
| Hedge Funds / Absolute Return | 7.00% | 5.81% | 5.35% | 10.00% |
| Real Estate (Property) | 12.00% | 7.11% | 6.35% | 13.00% |
| | | | | |
| Assumed Inflation - Mean | | 2.60% | | 2.00% |

* As outlined in the Plan's investment policy

# Depletion Date Projection

GASB 67 generally requires that a blended discount rate be used to measure the Total Pension Liability (the Actuarial Accrued Liability calculated using the Individual Entry Age Normal Cost Method). The long-term expected return on plan investments may be used to discount liabilities to the extent that the plan's Fiduciary Net Position (fair market value of assets) is projected to cover benefit payments and administrative expenses. A 20-year high quality (AA/Aa or higher) municipal bond rate must be used for periods where the Fiduciary Net Position is not projected to cover benefit payments and administrative expenses. Determining the discount rate under GASB 67 will often require that the actuary perform projections of future benefit payments and asset values. GASB 67 (paragraph 43) does allow for alternative evaluations of projected solvency, if such evaluation can reliably be made. GASB does not contemplate a specific method for making an alternative evaluation of sufficiency; it is left to professional judgment.

The following circumstances justify an alternative evaluation of sufficiency for the Florida Retirement System:

- The Florida Retirement System has a formal written policy to calculate an Actuarially Determined Contribution (ADC), which is articulated in the actuarial valuation report.

- The ADC is based on a closed, layered amortization period, which means that payment of the full ADC each year will bring the plan to a 100% funded position by the end of the amortization period if future experience follows assumption.

- GASB 67 specifies that the projections regarding future solvency assume that plan assets earn the assumed rate of return and there are no future changes in the plan provisions or actuarial methods and assumptions, which means that the projections would not reflect any adverse future experience which might impact the plan's funded position

Based on these circumstances, it is our professional opinion that the detailed depletion date projections outlined in GASB 67 would clearly indicate that the Fiduciary Net Position is always projected to be sufficient to cover benefit payments and administrative expenses. As such, the detailed projections were not developed.

# Net Pension Liability

| Net Pension Liability | June 30, 2013 | June 30, 2014 |
|---|---|---|
| Total pension liability | $150,276,127,590 | $156,115,762,947 |
| Fiduciary net position | 133,061,676,904 | 150,014,292,372 |
| Net pension liability | 17,214,450,686 | 6,101,470,575 |
| Fiduciary net position as a % of total pension liability | 88.54% | 96.09% |
| Covered payroll | 24,568,641,999 | 24,723,564,758 |
| Net pension liability as a % of covered payroll | 70.07% | 24.68% |

The total pension liability was determined by an actuarial valuation as of the valuation date, calculated based on the discount rate and actuarial assumptions below. The total pension liability is calculated using the Individual Entry Age Normal cost allocation method, which differs from the Ultimate Entry Age Normal cost allocation method used in the funding valuation for the System. Additionally, the net pension liability above has been adjusted upward to reflect any balance in the Contribution Clearing Trust Fund as of the measurement date.

## Discount Rate

| | | |
|---|---|---|
| Discount rate | 7.75% | 7.65% |
| Long-term expected rate of return, net of investment expense | 7.75% | 7.65% |
| Municipal bond rate | N/A | N/A |

The plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the discount rate for calculating the total pension liability is equal to the long-term expected rate of return.

## Other Key Actuarial Assumptions

The actuarial assumptions that determined the total pension liability as of June 30, 2014 were based on the results of an actuarial experience study for the period July 1, 2008 - June 30, 2013.

| | | |
|---|---|---|
| Valuation date | July 1, 2013 | July 1, 2014 |
| Measurement date | June 30, 2013 | June 30, 2014 |
| Inflation | 3.00% | 2.60% |
| Salary increases including inflation | 4.00%* | 3.25%** |
| Mortality | Generational RP-2000 with Projection Scale AA* | Generational RP-2000 with Projection Scale BB** |
| Actuarial cost method | Entry Age Normal | Entry Age Normal |

* See July 1, 2013 Actuarial Valuation Report for details

** See July 1, 2014 Actuarial Valuation Report for details

# Changes in Net Pension Liability

| Changes in Net Pension Liability | Total Pension Liability (a) | Increase (Decrease) Plan Fiduciary Net Position (b) | Net Pension Liability (a) - (b) |
|---|---|---|---|
| Balances as of June 30, 2013 | $150,276,127,590 | $133,061,676,904 | $17,214,450,686 |
| Changes for the year: | | | |
| Service cost | 2,256,738,453 | | 2,256,738,453 |
| Interest on total pension liability | 11,489,920,524 | | 11,489,920,524 |
| Effect of plan changes | 0 | | 0 |
| Effect of economic/demographic gains or losses | (448,818,280) | | (448,818,280) |
| Effect of assumptions changes or inputs | 1,256,045,470 | | 1,256,045,470 |
| Benefit payments[1] | (8,714,250,810) | (8,714,250,810) | 0 |
| Employer contributions | | 2,190,424,344 | (2,190,424,344) |
| Member contributions | | 682,507,323 | (682,507,323) |
| Net investment income | | 22,812,286,493 | (22,812,286,493) |
| Administrative expenses | | (18,351,882) | 18,351,882 |
| Balances as of June 30, 2014 | 156,115,762,947 | 150,014,292,372 | 6,101,470,575 |

[1] Benefit payments shown above include transfers to the Investment Plan and returns of contributions, net of $131,260,646 in transfers from other funds.

## Sensitivity Analysis

The following presents the net pension liability of the FRS, calculated using the discount rate of 7.65%, as well as what the FRS's net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (6.65%) or 1 percentage point higher (8.65%) than the current rate.

| | 1% Decrease 6.65% | Current Discount Rate 7.65% | 1% Increase 8.65% |
|---|---|---|---|
| Total pension liability | $176,111,092,436 | $156,115,762,947 | $139,483,464,095 |
| Fiduciary net position | 150,014,292,372 | 150,014,292,372 | 150,014,292,372 |
| Net pension liability | 26,096,800,064 | 6,101,470,575 | (10,530,828,277) |

## Schedule of Changes in Net Pension Liability and Related Ratios[1]

| | June 30, 2014 |
|---|---|
| **Total Pension Liability** | |
| Service cost | $2,256,738 |
| Interest on total pension liability | 11,489,921 |
| Effect of plan changes | 0 |
| Effect of economic/demographic (gains) or losses | (448,818) |
| Effect of assumption changes or inputs | 1,256,045 |
| Benefit payments | (8,714,251) |
| Net change in total pension liability | 5,839,635 |
| | |
| Total pension liability, beginning | 150,276,128 |
| Total pension liability, ending (a) | 156,115,763 |
| | |
| **Fiduciary Net Position** | |
| Employer contributions | $2,190,424 |
| Member contributions | 682,507 |
| Investment income net of investment expenses | 22,812,286 |
| Benefit payments | (8,714,251) |
| Administrative expenses | (18,352) |
| Net change in plan fiduciary net position | 16,952,615 |
| | |
| Fiduciary net position, beginning | 133,061,677 |
| Fiduciary net position, ending (b) | 150,014,292 |
| | |
| Net pension liability, ending = (a) - (b) | $6,101,471 |
| | |
| Fiduciary net position as a % of total pension liability | 96.09% |
| | |
| Covered payroll | $24,723,565 |
| | |
| Net pension liability as a % of covered payroll | 24.68% |

[1] This exhibit will fill in to a ten-year schedule as results for new fiscal years are calculated.

# Glossary

**Actuarially Determined Contribution**
A target contribution to a defined benefit pension plan for the reporting period, determined based on the funding policy and most recent measurement available when the contribution for the reporting period was adopted.

**Deferred Inflows/Outflows of Resources**
Portion of changes in net pension liability that is not immediately recognized in Pension Expense. These changes include differences between expected and actual experience, changes in assumptions, and differences between expected and actual earnings on plan investments.

**Discount Rate**
Single rate of return that, when applied to all projected benefit payments, results in an actuarial present value of projected benefit payments equal to the sum of:

1) The actuarial present value of benefit payments projected to be made in future periods where the plan assets are projected to be sufficient to meet benefit payments, calculated using the Long-Term Expected Rate of Return.
2) The actuarial present value of projected benefit payments not included in (1), calculated using the Municipal Bond Rate.

**Fiduciary Net Position**
Equal to market value of assets.

**Long-Term Expected Rate of Return**
Long-term expected rate of return on pension plan investments expected to be used to finance the payment of benefits, net of investment expenses.

**Money-Weighted Rate of Return**
The internal rate of return on pension plan investments, net of investment expenses.

**Municipal Bond Rate**
Yield or index rate for 20-year, tax-exempt general obligation municipal bonds with an average rating of AA/Aa or higher.

**Net Pension Liability**
Total Pension Liability minus the Plan's Fiduciary Net Position (unfunded accrued liability).

**Projected Benefit Payments**
All benefits estimated to be payable through the pension plan to current active and inactive employees as a result of their past service and expected future service.

**Service Cost**
The portion of the actuarial present value of projected benefit payments that is attributed to a valuation year.

**Total Pension Liability**
The portion of actuarial present value of projected benefit payments that is attributable to past periods of member service using the Entry Age Normal cost method based on the requirements of GASB 67 and 68.