

# Comprehensive Annual Financial Report

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TEACHER RETIREMENT SYSTEM OF TEXAS

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FIDUCIARY FUNDS OF THE STATE OF TEXAS

Fiscal Year Ended August 31, 2002





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## **TRS Mission Statement**

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**The mission of the  
Teacher Retirement System of Texas is:**

**1.**

**to deliver retirement and related benefits  
authorized by law for members and  
their beneficiaries; and**

**2.**

**to prudently invest and manage the  
assets held in trust for members  
and beneficiaries in an actuarially sound  
system administered in accordance  
with applicable fiduciary  
principles.**

# Comprehensive Annual Financial Report

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TEACHER RETIREMENT SYSTEM OF TEXAS

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FIDUCIARY FUNDS OF THE STATE OF TEXAS

Fiscal Year Ended August 31, 2002



Charles L. Dunlap, *Executive Director*

Prepared by  
Teacher Retirement System of Texas  
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# Introductory Section

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TEACHER RETIREMENT SYSTEM OF TEXAS

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## BOARD OF TRUSTEES



Front row from left: Charles L. Dunlap (*Executive Director*), Brenda L. Jackson, Cecilia Moreno, James H. (Jim) Simms (*Chairman*).  
 Back row from left: Mary Alice Baker, Linus D. Wright, H. Barham Fulmer, Wendell Whittenburg, Terence (Terry) Ellis, James P. Cummings, Sr. (*Vice Chair*).

**James H. (Jim) Simms, 2001**  
*Chairman*  
 Vice President, Amarillo National  
 Bank, Amarillo

**James P. Cummings, Sr., 2001**  
*Vice Chairman*  
 President, Wells Fargo Bank Texas,  
 N.A., San Angelo

**Mary Alice Baker, Ph.D., 2005**  
 Professor of Communication, Lamar  
 University, Beaumont

**Terence (Terry) Ellis, 2005**  
 Private Investor and Rancher,  
 New Ulm

**H. Barham Fulmer, II, 2003**  
 Senior Vice President, Southside  
 Bank, Lindale

**Brenda L. Jackson, 2003**  
 Executive Vice President of Business  
 Services, TXU Electric and Gas, Dallas

**Cecilia Moreno, Ed.D., 2003**  
 Administrative Assistant for  
 Academics-Wellness, Laredo ISD,  
 Laredo

**Wendell Whittenburg, 2001**  
 Teacher, Sweetwater

**Linus D. Wright, 2005**  
 Vice President, Paul Ray Berndtson,  
 Inc., Dallas

The Board of Trustees is responsible for the administration of the system under provisions of the state constitution and laws. The board is composed of nine trustees who are appointed to staggered terms of six years. Three trustees (Ellis, Jackson, and Cummings) are direct appointments of the governor. Two trustees (Fulmer and Simms) are appointed by the governor from a list prepared by the State Board of Education. Two trustees (Moreno and Whittenburg) are appointed by the governor from the three public school district active member candidates who have been nominated for each position by employees of public school districts. One trustee (Baker) is appointed by the governor from the three higher education active member candidates nominated by employees of institutions of higher education. One trustee (Wright) is appointed by the governor from the three retired member candidates who are nominated by retired TRS members. Appointments are subject to confirmation by the Senate. Board member terms expire August 31 of odd numbered years. In late 2002, Governor Perry appointed three new trustees to the TRS Board -- Jim Fonteno, Jr., of Houston (replacing James H. "Jim" Simms), Jarvis V. Hollingsworth of Missouri City (replacing James P. Cummings, Sr.), and Greg Poole of Conroe (replacing Wendell Whittenburg). Each trustee was appointed to a term ending August 31, 2007. The appointments are subject to Senate confirmation.

CERTIFICATE OF ACHIEVEMENT



# Certificate of Achievement for Excellence in Financial Reporting

Presented to

## Teacher Retirement System of Texas

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
August 31, 2001

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



*Imelda Aruete*  
President

*Jeffrey L. Esser*  
Executive Director



## LETTER OF TRANSMITTAL

### Teacher Retirement System of Texas



1000 Red River Street  
Austin, Texas 78701-2698  
(512) 397-6400 1-800-223-8778

November 8, 2002

The Honorable Rick Perry  
The Honorable Bill Ratliff  
The Honorable James E. "Pete" Laney  
The Board of Trustees and Members  
of the Teacher Retirement System

Dear Governor Perry, Lieutenant Governor Ratliff,  
Speaker Laney, TRS Board of Trustees and Members of  
the Teacher Retirement System:

On behalf of the board of trustees, I am pleased to present this *Comprehensive Annual Financial Report* (CAFR) of the Teacher Retirement System of Texas (TRS) for the fiscal year ended August 31, 2002, the system's 65<sup>th</sup> year of operation. During the past year the system continued to experience growth in membership reflecting the need for public school employees generated by Texas' expanding population. At year-end, system participation included 1,345 reporting employers and 1,048,086 members and retirees.

Benefit payments continued to grow as a function of member growth and significant program enhancements enacted by the legislature in recent years. For the year \$4.6 billion in benefit payments and member refunds were distributed. These dynamics coupled with a continuation of adverse investment market conditions resulted in the actuarial value of member benefits exceeding the actuarial value of assets for the first time in several years. Net plan assets were \$71.7 billion as compared to \$79.4 billion at the close of fiscal year 2001.

#### Structure of the Report

The *Comprehensive Annual Financial Report* for fiscal year 2002 is designed to provide TRS stakeholders with a thorough review of the system's operations for the past year. Responsibility for the accuracy of the data, and the completeness and fairness of the presentation, rests with management of the system. This report includes the following sections:

- The **Introductory Section** describes the system's management and highlights the year's activities, membership data and communications information.

- The **Financial Section** contains the report of the Texas State Auditor, financial statements of the system, and required supplemental information, including management's discussion and analysis.
- The **Investment Section** includes a summary of investments and performance information.
- The **Actuarial Section** contains the independent actuary's certification and selected information from the annual actuarial valuation for the fiscal year ended August 31, 2002.
- The **Benefits Section** includes a summary of retirement and death benefits available to retirees and beneficiaries, and health care benefits available to members and their families.
- The **Statistical Section** presents six-year financial and nonfinancial trend information about the pension trust fund and the health insurance trust funds.

#### Certificate of Achievement for Excellence in Financial Reporting

The Government Finance Officers Association of the United States and Canada (GFOA) awarded TRS the Certificate of Achievement for Excellence in Financial Reporting for its *Comprehensive Annual Financial Report* for the fiscal year ended August 31, 2001. To be awarded the certificate, a report must meet or exceed program standards and must satisfy both generally accepted accounting principles and applicable legal requirements. TRS has received a Certificate of Achievement for the last 12 years. We believe that the current report continues to meet program requirements, and it is being submitted to the GFOA for consideration again this year.

#### TRS – The Reporting Entity

The Teacher Retirement System of Texas was established by amendment to the Texas Constitution in 1936 and enactment of statutes in 1937 to provide a retirement program for public education employees in professional and business administration, supervision, and instruction. Benefits were later expanded to include

## LETTER OF TRANSMITTAL

disability, death and survivor benefits. In 1949, membership was expanded to include other employees of public education.

The *Texas Public School Retired Employees Group Insurance Program* was enacted in 1985 to provide health care benefits for retirees. At year-end, over 150,000 retirees and dependents participated in the program.

The 77<sup>th</sup> Texas Legislature enacted the *Texas School Employees Uniform Group Health Coverage Act*, establishing a statewide health coverage program for public school employees. Coverage began in September 2002 with an enrollment of over 170,000 employees and dependents of small to mid-sized districts, education service centers, and certain charter schools and other educational districts. Over time, availability of coverage will be expanded to include all public school districts and their employees.

### Investment Performance

For the second consecutive year equity markets declined in value and this was reflected in the pension trust fund's performance of -7.8 percent for the year. Long-term performance continues to be above inflation and the board of trustees' investment return expectation. For the past 10 years, the time-weighted compound annual return has been 8.82 percent.

Investment risks are diversified over a very broad range of market sectors and securities. This strategy reduces portfolio risk to adverse developments in sectors and issuers experiencing unusual difficulties and offers opportunity to benefit from improving performance of future market leaders. Though short-term price volatility is unpredictable and can be high, we believe that over time earnings of leading companies will be higher, offering reasonable prospects for long-term investment value growth.

### Benefits

TRS members and retirees are now realizing significant benefit enhancements provided for in bills passed by the 77<sup>th</sup> Legislature. These include *ad hoc* annuity increases for retirees and an increase in the retirement benefit formula multiplier. Such improvements follow a history of favorable legislative actions. For fiscal year 2002, benefit payments and refunds to withdrawing members totaled \$4.6 billion.

Future retirees will benefit from the increase in the retirement formula multiplier to 2.3 percent per year of creditable service. This means that members retiring with 30 years of service credit will see their retirement annuities replace 74 percent of their highest three-year average pre-retirement income net of monthly contribu-

tions to the pension trust fund.

### Actuarial Soundness

Continued adverse market performance coupled with increased benefit liabilities resulted in the actuarial value of member benefit liabilities exceeding the value of actuarial assets for the first time in several years. At year-end, the ratio of actuarial assets to actuarial liabilities was 96.3 percent. The funding ratio remains very high, particularly in view of the prolonged period of negative market returns.

The system uses a five-year smoothing process to translate annual market returns into actuarial returns that are used to develop actuarial valuations. For the current year this results in inclusion of portions of annual returns from 1998 forward, thus including some years of more favorable returns along with portions of the negative returns for 2001 and 2002. In like manner, carry-forward portions of the adverse performance for 2001 and 2002 will be included in the development of actuarial returns through fiscal year 2005. It is important to note that this will add to the challenge of achieving actuarial returns sufficient to reduce the gap between the value of actuarial liabilities and actuarial assets.

The challenge is made all the greater because the *normal cost* of adding new members (expressed as a percentage of payroll) is now greater than the combined state and member contribution rates. Taken together with the carry-forward of 2001 and 2002 negative returns, the pension trust fund would have to achieve investment returns far greater than the board's long-term expected return to restore equal balance to the value of actuarial liabilities and assets at current contribution rates.

### Major Initiatives

Implementation responsibilities for SB 273 and HB 3343 from the 77<sup>th</sup> Legislature were very substantial, challenging all aspects of TRS operations. TRS has focused on maintaining a high level of member service while making retirement benefit and annuity adjustments and introducing new programs included in the bills.

SB 273 included an increase in the retirement benefit formula multiplier to 2.3 percent, granted *ad hoc* increases for existing annuitants, and established a new option for certain members to purchase additional service credit. The bill also introduced a new responsibility for TRS to establish a process for certification to TRS by companies who may offer voluntary investment options that qualify under section 403(b) of the Internal Revenue Code to public school employees through payroll reduction.

HB 3343 established for the first time a state-appropri-

## LETTER OF TRANSMITTAL

ated funding structure to assist public school employers and employees with the financial cost of health care and also established a statewide health coverage program through TRS. TRS-ActiveCare was developed as a self-insured plan during the year with Blue Cross and Blue Shield of Texas as the program administrator and Medco Health Solutions as the pharmacy plan manager. First coverage commenced September 1, 2002, with over 170,000 participating employees and dependents.

Smaller districts and certain other employers were required to participate, with other employers assured of an option to consider participation not later than September 2005. Virtually all public school employers and employees, however, receive the state's financial assistance whether or not they participate in TRS-ActiveCare. The state's support is distributed through both TRS and the Texas Education Agency.

### Retiree Health Care Program

In addition to responsibilities associated with the new TRS-ActiveCare program, TRS manages TRS-Care, a health care program for retirees that was established in 1985. Funding is provided by premium payments from retiree participants and contributions by the state and active employees. Historically, the program has also generated supplemental investment income from a separate health care trust. During the past few years, however, the trust was depleted as its funds were used to help pay program claims and administrative expenses.

TRS-Care is the source of retirement health coverage upon which almost all public school retirees rely. Double-digit program cost increases driven by membership growth, utilization and medical trends have resulted in TRS requesting legislative consideration of substantial additional appropriations to maintain solvency through the coming biennium.

TRS trustees remain focused on the need to balance revenues and expenses in a fiscally responsible manner, and to offer a program that best suits all participants' needs given available resources. This challenge has been particularly difficult for all those who have an interest in retiree health care given the high compound growth rate of medical program costs. Unfortunately, we continue to expect high growth in costs which will be evidenced in funding needs for the next legislature's consideration. TRS will continue to assist with legislative evaluation of the program and options to provide the most reasonable slate of benefits within funding constraints.

### Acknowledgments

In late 2002, the governor appointed three new trustees to the board. Jarvis Hollingsworth succeeds Jim Cummings, Jim Fonteno succeeds Jim Simms, and Greg Poole succeeds Wendell Whittenburg. Trustee willingness to accept the substantial responsibilities of directing system administration is a great service to the state and to the members served by TRS. We are grateful for the dedicated service and leadership provided by Jim Simms, Jim Cummings and Wendell Whittenburg and look forward to the future contributions of new trustees.

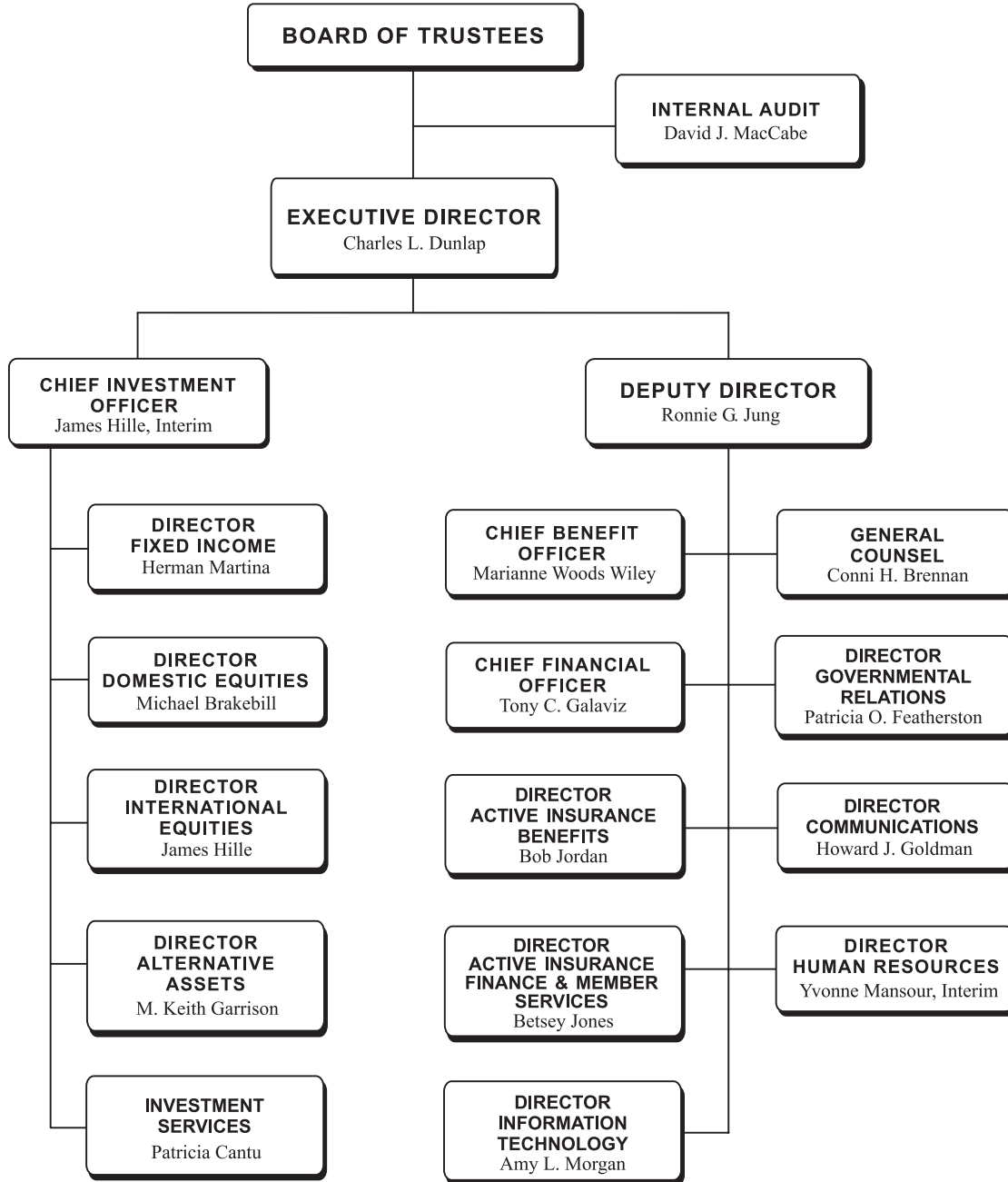
TRS trustees and staff are keenly focused on prudent pension trust fund portfolio management and efficient, service-oriented delivery of valuable retirement and related benefits for public education employees and retirees. We are pleased to report on operational results for the year and to acknowledge the substantial support of state leadership, trustees, members, interested associations, and TRS staff.

Respectfully submitted,



Charles L. Dunlap  
Executive Director

# ORGANIZATION CHART



## STAFF & ADVISORS

### ADMINISTRATIVE STAFF

Charles L. Dunlap, *Executive Director*  
Ronnie G. Jung, *Deputy Director*  
James Hille, *Interim Chief Investment Officer*  
Marianne Woods Wiley, *Chief Benefit Officer*  
Tony C. Galaviz, *Chief Financial Officer*  
Conni H. Brennan, *General Counsel*  
David J. MacCabe, *Director, Internal Audit*  
Amy L. Morgan, *Director, Information Technology*  
Frank J. DiLorenzo, *Director, Retiree Insurance*  
Bob Jordan, *Director of Benefits, Active Insurance*  
Betsey Jones, *Director of Finance and Member Services, Active Insurance*  
Howard J. Goldman, *Director, Communications*  
Patricia O. Featherston, *Director, Governmental Relations*  
Yvonne Mansour, *Interim Director, Human Resources*

### GENERAL INVESTMENT CONSULTANT

Ennis, Knupp & Associates, Inc., Chicago

### CONSULTING ACTUARY

Gabriel, Roeder, Smith & Company, Dallas

### INVESTMENT CONSULTANTS

Pathway Capital Management L.L.C., Irvine, CA  
Tremont Partners, Inc., Rye, NY

### INVESTMENT ADVISORS

I. Craig Hester, Austin  
Keith C. Brown, Austin

### AUDIT SERVICES

Texas State Auditor's Office, Austin  
Maxwell Locke & Ritter, Austin

### FIDUCIARY COUNSEL

Groom Law Group, Chartered, Washington

### MEDICAL BOARD

Dr. Alice Cox, Fredericksburg  
Dr. Homer R. Goehrs, Austin  
Dr. Larry D. Wilson, Austin

### TEXAS PUBLIC SCHOOL EMPLOYEES GROUP INSURANCE PROGRAM ADVISORY COMMITTEE

Catherine M. Hord, *Chairman*, Georgetown  
Russell E. Sayers, *Vice Chairman*, Austin  
Elizabeth Bulos, El Paso  
Shirley M. Howard, Midland  
John Osteen, McAllen  
B. Sue Passmore, Dallas  
Nelda J. Van Dyke, Brenham  
E. Lamont Veatch, Lubbock  
William T. Woody, Lorena

### HEALTH CARE CONSULTANT

Watson Wyatt Worldwide, Dallas

### MASTER CUSTODIAN AND SECURITIES LENDING AGENT

State Street Bank and Trust Company,  
Boston

### PERFORMANCE MEASUREMENT

State Street Bank and Trust Company,  
Boston

# MEMBERSHIP

## Pension Trust Fund

Membership includes employees of state-supported educational institutions in Texas. At August 31, 2002, participating employing districts included the following:

|  |                     |
|--|---------------------|
| Public Schools, Service Centers<br>and Charter Schools | 1,241               |
| Community and Junior Colleges                          | 51                  |
| Universities   | 43                  |
| Medical Schools  | 8                   |
| Other Entities   | 2                   |
| <b>Totals</b>  | <u><u>1,345</u></u> |

Employees and retirees from these entities comprise the membership of the Teacher Retirement System of Texas. At August 31, 2002, and August 31, 2001, membership consisted of the following:

|                                    | <u>Year Ended August 31,</u> |                         |
|------------------------------------|------------------------------|-------------------------|
|                                    | <u>2002</u>                  | <u>2001</u>             |
| <b>Current Members:</b>            |                              |                         |
| Active Contributing                | 733,967                      | 721,379                 |
| Active Noncontributing             | 86,656                       | 71,080                  |
| Deferred Retirement Option         | 3,290                        | 4,880                   |
| Inactive Nonvested                 | 9,419                        | 7,983                   |
| Inactive Vested                    | 13,313                       | 11,971                  |
| <b>Total Current Members</b>       | <u><u>846,645</u></u>        | <u><u>817,293</u></u>   |
| <b>Retirement Recipients:</b>      |                              |                         |
| Service                            | 184,807                      | 172,420                 |
| Disability                         | 7,858                        | 7,806                   |
| Survivor                           | 8,776                        | 8,656                   |
| <b>Total Retirement Recipients</b> | <u><u>201,441</u></u>        | <u><u>188,882</u></u>   |
| <b>TOTAL MEMBERSHIP</b>            | <u><u>1,048,086</u></u>      | <u><u>1,006,175</u></u> |

Membership changes are summarized below:

|                            | <u>2002</u>          | <u>2001</u>          |
|----------------------------|----------------------|----------------------|
| <b>Active Membership:</b>  |                      |                      |
| New Members                | 84,428               | 91,501               |
| Members Withdrawing        | (40,706)             | (44,268)             |
| Service Retirements        | (15,950)             | (13,601)             |
| Disability Retirements     | (665)                | (703)                |
| In-Service Deaths          | (1,149)              | (1,049)              |
| Other Changes              | 3,394                | (3,443)              |
| <b>Net Increase</b>        | <u><u>29,352</u></u> | <u><u>28,437</u></u> |
| <b>Retired Membership:</b> |                      |                      |
| Retirements                | 16,615               | 14,304               |
| Deaths After Retirement    | (5,581)              | (5,218)              |
| Option Continuations       | 1,340                | 1,358                |
| Other Changes              | 185                  | (955)                |
| <b>Net Increase</b>        | <u><u>12,559</u></u> | <u><u>9,489</u></u>  |

| <u>Active Member Profile</u> | <u>2002*</u> | <u>2001</u> |
|------------------------------|--------------|-------------|
| Average Annual Salary        | \$ 33,272    | \$ 29,303   |
| Average Age                  | 42.6         | 43.4        |
| Average Years of Service     | 8.8          | 9.4         |

\* Excludes noncontributing active members.

| <u>Annuitant and Beneficiary Profile</u> | <u>2002</u> | <u>2001</u> |
|--|-------------|-------------|
| Average Monthly Annuities                |             |             |
| Life Annuities                           | \$ 1,762    | \$ 1,733    |
| Disability Annuities                     | \$ 1,200    | \$ 1,176    |
| Annuities Certain                        | \$ 900      | \$ 871      |
| Average Age of Current Retirees          | 70.1        | 70.6        |
| Average Age at Retirement                |             |             |
| All Retirees                             | 60.1        | 60.6        |
| Current Year Retirees                    | 59.6        | 59.8        |
| Average Years of Service                 |             |             |
| All Retirees                             | 24.8        | 24.8        |
| Current Year Retirees                    | 25.6        | 24.9        |
| Average Salary at Retirement             |             |             |
| All Retirees                             | \$ 29,481   | \$ 27,930   |
| Current Year Retirees                    | \$ 41,918   | \$ 39,120   |

|                                      |       |       |
|--------------------------------------|-------|-------|
| Ratio of Current Members to Retirees | 4.2:1 | 4.3:1 |
|--------------------------------------|-------|-------|

## Texas Public School Retired Employees Group Insurance Program

Group insurance participation for the Retired Plan is summarized below:

|                             | <u>2002</u>           | <u>2001</u>           |
|-----------------------------|-----------------------|-----------------------|
| <b>Retired Plan:</b>        |                       |                       |
| Retirees                    | 125,245               | 117,894               |
| Surviving Spouses           | 2,912                 | 2,719                 |
| Surviving Children          | 36                    | 33                    |
| Dependent Spouses           | 19,780                | 17,394                |
| <b>TOTAL RETIRED PLAN *</b> | <u><u>147,973</u></u> | <u><u>138,040</u></u> |

\* Excludes 2,774 and 2,142 dependent children for 2002 and 2001, respectively.

## Texas School Employees Uniform Group Insurance Program

Effective September 1, 2002, TRS-ActiveCare was established to provide statewide health care benefits for active public school employees and their eligible dependents. Approximately 104,000 employees and 72,000 dependents had enrolled in this new program as of September 1, 2002.

## COMMUNICATIONS

During FY 2002, TRS undertook a number of initiatives to improve communications with its members, retirees, and the general public. Agency communications focused on print publications, the Internet, group presentations, coordination with employers, telecommunications, and market research.

### Print Publications

During the year, the agency published the *TRS News* and *Update* newsletters to inform members and district administrators of important developments relating to the agency. Working with Blue Cross and Blue Shield of Texas and with Medco Health, TRS also published a series of print materials to introduce TRS-ActiveCare, the new statewide health insurance program for public school employees, and to assist members with enrollment.

### The Internet

In FY 2002, TRS introduced a new "Online Personal Access" section of the agency's Web site, enabling active members to obtain account information online and retirees to access 1099 data. An online retirement estimate calculator now allows members to estimate their retirement annuities using data imported from TRS computer records.

The TRS Web site also saw significant expansion with new sections dedicated to TRS-ActiveCare, 403(b) certification, and agency procurement opportunities. New frequently asked questions were also added to the site to better assist active members and retirees with a variety of subjects. As a result, 789,148 Web site visits were recorded—a nearly 32 percent increase from FY 2001.

### Group Presentations

TRS made a number of group presentations to professional associations, employee and retiree groups, and at regional educational service centers. Several presentations focused on long-term care insurance and the new TRS-ActiveCare plan. Other TRS presentations covered the full range of TRS benefits. More than 19,373 people attended 219 group presentations, and 36,850 people attended TRS presentations at 11 conventions. In addition, 10,732 people visited with a TRS counselor in Austin.

During the past fiscal year, TRS expanded its use of the Texas Education Agency's T-STAR and TETN network with 13 broadcasts to public education employers and employees. T-STAR broadcasts focused on TRS-ActiveCare, long-term care coverage, how to apply for retirement benefits, TRS's *Certification Report and Comparability Study on Public School Employees' Health Coverage*, the TRS Web site, and the full range of TRS benefits. TETN

broadcasts provided information about the funding provisions of House Bill 3343.

### Coordination with Employers

The new TRS Reporting and Query System (TRAQS) was expanded in the past year. More than 394 TRS reporting entities submitted monthly reports through TRAQS by year end. The Benefit Accounting staff conducted 29 training workshops for 750 people from these reporting entities.

TRS-ActiveCare training seminars were conducted in 20 locations around the state for approximately 2,000 administrators of entities participating in the program. These seminars provided information for enrollment in TRS-ActiveCare and ongoing administrative issues.

### Telecommunications

In FY 2002, a total of 459,285 calls were handled by the agency's Telephone Counseling Center. In addition, TRS-ActiveCare staff and contractors handled over 40,000 calls. TRS initiated a study in the summer of 2002 to assess how to best serve members using new technology. The study will be completed in early 2003.

InfoLine is TRS's automated telephone information system. During FY 2002, 99,599 calls were completed within the system. InfoLine provides callers with immediate access to general TRS benefit information, day or night. Account information is also available with a personal identification number.

### Market Research

TRS conducted a member satisfaction survey in 2002. Through this project, the University of North Texas Survey Research Center interviewed 1,100 TRS active members and retirees by telephone to assess customer satisfaction with TRS services. Ninety-six percent of active members and 98.3 percent of retirees were satisfied or very satisfied with overall TRS services. Generally, respondents reported satisfaction ratings of 90 percent or higher when asked to rate specific TRS services.

TRS also undertook a customer service evaluation project using independent evaluators supplied by a private sector research firm. The Telephone Counseling Center, TRS facilities, the receptionist area, member service representatives, and benefit presentations were evaluated. TRS telephone operations produced an overall score of 92.4%—six points higher than any state office surveyed to date by the firm conducting the project. TRS receptionists and member service representatives received an overall score of 93.9%—four points higher than any other state office surveyed by the company.





# Financial Section

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TEACHER RETIREMENT SYSTEM OF TEXAS

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## INDEPENDENT AUDITOR'S REPORT

November 8, 2002

Members of the Board of Trustees  
of the Teacher Retirement System  
The Honorable Rick Perry, Governor of Texas  
and  
Members of the Texas Legislature

Ladies and Gentlemen:

We have audited the accompanying basic financial statements, listed as Exhibits I and II in the Table of Contents, of the Teacher Retirement System of Texas (System) as of and for the year ended August 31, 2002. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audit. We previously audited and reported on the basic financial statements of the System as of and for the year ended August 31, 2001; the comparative totals from these statements are included for additional analysis only.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic 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 basic financial statements referred to above present fairly, in all material respects, the combined plan net assets of the fiduciary funds of the System as of August 31, 2002, and the changes in the combined plan net assets of the fiduciary funds for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The information included in Management's Discussion and Analysis; Required Supplementary Information; Exhibits A, B, and C; and Schedules 1 through 5 is presented for purposes of additional analysis and is not a required part of the basic financial statements. This supplemental information is the responsibility of the management of the System. 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.

We did not audit the Introductory, Investment, Actuarial, Benefits, and Statistical sections and, accordingly, we do not express an opinion on them.

As discussed in Note I.C to the basic financial statements, the System has adopted Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended, for the year ended August 31, 2002.

In accordance with *Government Auditing Standards*, we will also report on our consideration of the System's internal controls and its compliance with certain provisions of laws and regulations material to the basic financial statements in a separate report. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Lawrence F. Alwin, CPA  
State Auditor

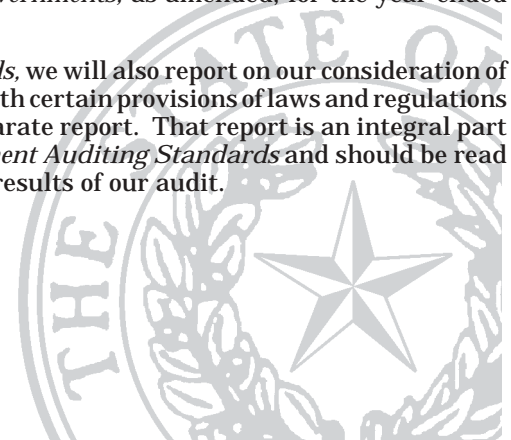
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## MANAGEMENT'S DISCUSSION AND ANALYSIS

The following is Management's Discussion and Analysis (MD&A) of the Teacher Retirement System's (TRS) financial performance for the fiscal year ended August 31, 2002. The MD&A is presented as a narrative overview and analysis in conjunction with the Executive Director's Letter of Transmittal included in the Introductory Section of the TRS Comprehensive Annual Financial Report.

TRS is responsible for administering retirement and related benefits to employees and beneficiaries of employees of Texas public state supported educational institutions. TRS also administers the Texas Public School Employees Group Insurance Program (Retired Plan and Active Plan), and the 403(b) Certification Program.

### Financial Highlights

- The net assets of the TRS pension trust fund decreased by (\$7.7) billion, or (9.7%). The decrease was due primarily to negative investment returns and benefit payments exceeding employee and state contributions.
- As of August 31, 2002, the date of the most recent actuarial valuation, the TRS pension trust funding ratio of actuarial assets as a percentage of actuarial liabilities is 96.3%, which is lower than the 102.5% level at August 31, 2001.
- The TRS rate of return on investments for the year ended August 31, 2002 of (7.81%) on a market value basis and was due primarily to a downturn in equity markets. The rate of return for fiscal year 2001 was (10.61%).
- Net assets of the TRS Retired Group Insurance Program increased \$107.9 million in fiscal year 2002. The net increase is a result of \$285.5 million in additional state appropriations, offset by a depletion of resources due to increased membership and higher medical and drug costs.
- The current TRS Active Group Insurance Program health care component was in the final stages of operation during fiscal year 2002 with a net asset increase of \$682,000 due primarily to investment earnings. Optional types of insurance will still be offered, and a new group health insurance plan for active members will begin operations September 1, 2002.

### Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the TRS basic financial statements, which comprise the following components:

- Fund financial statements
- Notes to the financial statements
- Required supplementary information
- Other supplemental schedules

Collectively, this information presents the combined net assets held in trust for pension benefits and other purposes as of August 31, 2002, and summarizes the combined changes in net assets held in trust for pension benefits and other purposes. The information available in each of these sections is briefly summarized below.

• **Fund Financial Statements.** Financial statements are presented for all fiduciary funds as of August 31, 2002. Fiduciary fund types presented include the pension trust fund, two health insurance trust funds (group insurance programs), an administrative trust fund (403(b) certification program), and agency funds. Fiduciary funds are used to account for resources held for the benefit of parties outside TRS. A combined statement of fiduciary net assets and a combined statement of changes in fiduciary net assets are presented for the fiduciary funds as of August 31, 2002, and for the year then ended. Comparative information as of August 31, 2001, and for the year then ended also has been presented. These financial statements reflect the resources available to pay benefits to retirees and other beneficiaries and to pay health care claims for covered participants.

• **Notes to the Financial Statements.** The financial statement notes provide additional information that is essential to a full understanding of the data provided in the fund financial statements. Information available in the notes to the financial statements is described below:

– Note I provides a summary of significant accounting policies, including the basis of accounting, budgets and appropriations, explanations of major asset and liability classes, and legal reserve

## MANAGEMENT'S DISCUSSION AND ANALYSIS

information. Also included is a general description of TRS as well as a description of each of the funds administered by TRS.

- Note II describes deposits and investments, including investing authority, investment risk categorizations, and additional information about cash, securities lending, derivatives, covered call options, international currency contracts, alternative investments, and contingent commitments.

- Note III provides information on fringe benefits paid by the state for employees of the group insurance programs.

- Note IV describes deferred compensation plans available to TRS employees.

- Note V provides information on contingent liabilities such as TRS employees' accumulated sick leave and lump sum death benefits.

- Note VI addresses TRS' continuance subject to review under the Texas Sunset Act.

- Note VII describes post-employment health care benefits provided to TRS employees and retired public school employees.

- Note VIII addresses risk management issues related to the group insurance program for active school district employees.

- Note IX provides information on TRS real estate corporations and summarizes the financial activity from their operations.

- Note X provides pension disclosure information, including detailed data on the plan description as well as contributions required and made.

- **Required Supplementary Information.** Required supplementary information consists of schedules and related notes concerning the funding status of the pension plan administered by TRS. Also included in this component is Management's Discussion and Analysis.

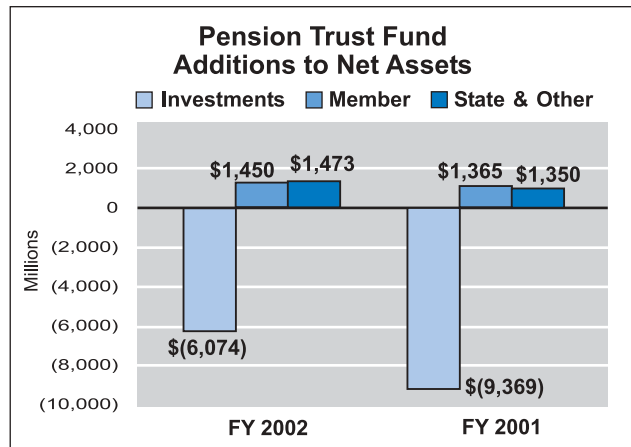
- **Other Supplementary Schedules.** Other schedules include information on fiduciary fund types other than the pension trust fund, changes in reserve account balances, budgets for administrative expenses, activity in investment portfolios, investing activity expenses, and payments to consultants.

### Financial Analysis of TRS Funds

#### Pension Trust Fund

Net assets held in trust for benefits at August 31, 2002 were \$71.7 billion, a decrease of (\$7.7) billion, from \$79.4 billion at August 31, 2001.

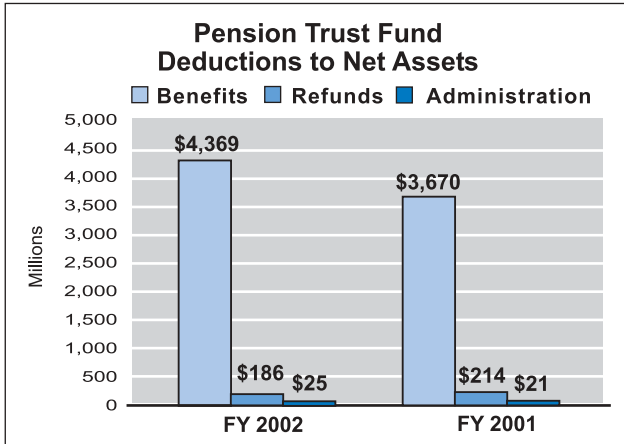
Additions to TRS net assets held in trust for benefits include member, state and reporting employer contributions as well as investment income. Member, state and employer contributions grew \$166 million, or 6.3%, during fiscal year 2002 due to increases in active membership as well as growth in annual payroll. Investment losses during fiscal year 2002 were (\$6.1) billion compared to fiscal year 2001 investment losses of (\$9.4) billion. Investment losses were due to the downturn in equity markets and the slowdown in the U.S. economy. The terrorist attacks of September 11, 2001, as well as weakened confidence in corporate America, further exacerbated the decline.



Deductions from TRS net assets held in trust for benefits are mainly retirement, death, and survivor benefits. Other deductions include refunds of member contributions and administrative expenses. During fiscal year 2002, benefit payments, including transfers to the Employees Retirement System of Texas, totaled \$4.37 billion, an increase of \$699 million, or 19.1%, over fiscal year 2001 benefit payments of \$3.67 billion. This increase is due to growth in retiree membership and recent benefit enhancements. All other deductions for fiscal year 2002 totaled \$211 million, a decrease of (\$24.2) million, or (10.3%), from

## MANAGEMENT'S DISCUSSION AND ANALYSIS

\$235.2 million in fiscal year 2002. Administrative expenses for fiscal year 2002 on a cost per member basis were \$35.80 as compared to \$32.45 for fiscal year 2001.



### Health Insurance Trust Fund Retired Plan

During fiscal year 2002 net assets of the Retired Group Insurance Program increased by \$107.9 million, from a (\$36.0) million deficit to \$71.9 million.

Additions to net assets include retiree premiums, state and active member contributions, supplemental state appropriations, and investment earnings. Retiree premiums for fiscal year 2002 increased \$12.6 million, or 9.6%, over fiscal year 2001 due to growth in the number of plan participants. State and active member contributions increased in fiscal year 2002 by \$7.0 million, or 5.1%, due to payroll growth. Supplemental state appropriations for fiscal year 2002 were \$285.5 million as compared to \$76.3 million in fiscal year 2001. The supplemental funds were needed to maintain solvency of the retired group insurance program through August 31, 2002. Investment earnings for fiscal year 2002 increased \$1.3 million from fiscal year 2001 due to increased holdings of short-term investments during fiscal year 2002.

Deductions from net assets include claims payments, claims processing costs and administrative expenses. Claims payments during fiscal year 2002 totaled \$451.7 million and increased \$61.2 million, or 15.7%, over claims payments of \$390.5 million in fiscal year 2001. Claims payments increased due to growth in the number of plan participants and the rising costs of health care and pharmacy benefits. Claims processing costs increased \$.8 million, or 5.1%, also

due to increased claims volume. Administrative expenses for fiscal year 2002 remained stable at \$2.2 million, decreasing (2.6%) from fiscal year 2001.

### Health Insurance Trust Fund Active Plan

During fiscal year 2002 net assets of the Active Group Insurance Program increased by \$.7 million.

Additions to net assets include administrative fees, investment income, and state appropriations. Administrative fees for fiscal year 2002 increased by \$38,000 over fiscal year 2001 due to a fee rate increase effective in January 2002. Investment earnings of \$.6 million in fiscal year 2002 reflected a decrease of (\$.8) million from fiscal year 2001 due to lower interest rates.

Deductions from net assets include an adjustment for prior year claims payments and administrative expenses. Administrative expenses of \$2.7 million for fiscal year 2002 increased \$2.3 million over fiscal year 2001. This increase was due to the implementation costs for the new TRS- ActiveCare plan (created by H.B. 3343, 77<sup>th</sup> Legislature) that will begin operations September 1, 2002. These implementation costs were fully funded by supplemental state appropriations and had no impact on the net assets of the fund.

### 403(b) Administrative Trust Fund

The 403(b) Certification Program (created by S.B. 273, 77<sup>th</sup> Legislature), which began operations in fiscal year 2002, ended the year with \$206,000 in net assets. The fund's additions include \$325,000 in certification fees and approximately \$1,200 in interest income. The only deduction from the fund was administrative expenses of approximately \$124,000.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Net Assets – Pension Trust Fund (Dollars in Thousands)

|                               | Fiscal Year<br>2002  | Fiscal Year<br>2001  | Dollar<br>Change       | Percentage<br>Change |
|-------------------------------|----------------------|----------------------|------------------------|----------------------|
| <b>Assets</b>                 |                      |                      |                        |                      |
| Cash and Receivables          | \$ 1,383,182         | \$ 1,504,002         | \$ (120,820)           | -8.0%                |
| Investments                   | 70,841,182           | 78,731,131           | (7,889,949)            | -10.0%               |
| Securities Lending Collateral | 63,407               | 10,261,028           | (10,197,621)           | -99.4%               |
| Capital Assets and Other      | 32,847               | 35,784               | (2,937)                | -8.2%                |
| <b>TOTAL ASSETS</b>           | <b>\$ 72,320,618</b> | <b>\$ 90,531,945</b> | <b>\$ (18,211,327)</b> | <b>-20.1%</b>        |
| <b>Liabilities</b>            |                      |                      |                        |                      |
| Benefits Payable              | \$ 409,871           | \$ 324,713           | \$ 85,158              | 26.2%                |
| Investment Purchases Payable  | 117,527              | 490,031              | (372,504)              | -76.0%               |
| Accounts Payable and Other    | 34,011               | 28,358               | 5,653                  | 19.9%                |
| Securities Lending Collateral | 63,407               | 10,261,028           | (10,197,621)           | -99.4%               |
| <b>TOTAL LIABILITIES</b>      | <b>\$ 624,816</b>    | <b>\$ 11,104,130</b> | <b>\$ (10,479,314)</b> | <b>-94.4%</b>        |
| <b>Total Net Assets*</b>      | <b>\$ 71,695,802</b> | <b>\$ 79,427,815</b> | <b>\$ (7,732,013)</b>  | <b>-9.7%</b>         |

\* Dollar change includes a restatement in fiscal year 2002 beginning net assets of (\$1,051,000).

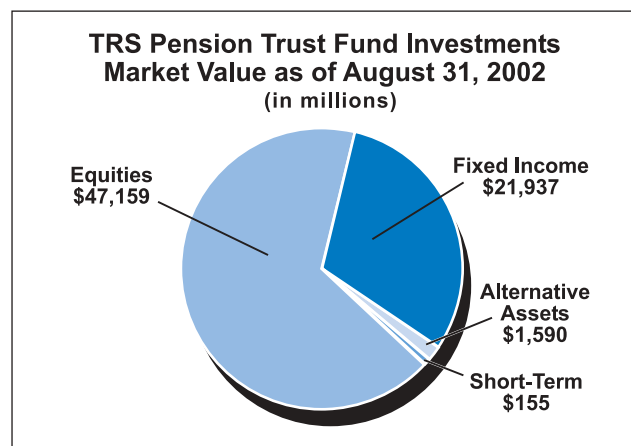
As the above table shows, pension trust fund net assets decreased by (\$7.7) billion, or (9.7%), in fiscal year 2002. This decrease reflects the negative investment returns due to the difficult financial markets. The decrease in cash and receivables is primarily due to the decrease in the receivable from brokers for unsettled trades at August 31, 2002, and a decrease in interest income due but unpaid at

August 31, 2002. The decrease in securities lending collateral is a result of the transition to a new securities lending agent at fiscal year end. The decrease in investments purchased payable is due to a decrease in unsettled trades at August 31, 2002.

The following table presents the investment allocation as of fiscal year end 2002 and 2001 as compared to the normal allocation for 2002 and 2001.

|                           | Fiscal Year<br>2002 Normal | Fiscal Year<br>2002 Actual | Fiscal Year<br>2001 Normal | Fiscal Year<br>2001 Actual |
|---------------------------|----------------------------|----------------------------|----------------------------|----------------------------|
| <b>Equities</b>           | 65.5%                      | 64.4%                      | 65.5%                      | 63.1%                      |
| <b>Fixed Income</b>       | 29.5%                      | 30.2%                      | 29.5%                      | 31.9%                      |
| <b>Alternative Assets</b> | 4.5%                       | 4.5%                       | 4.5%                       | 4.5%                       |
| <b>Short-Term</b>         | 0.5%                       | 0.9%                       | 0.5%                       | 0.5%                       |

The change from fiscal year 2001 to fiscal year 2002 in the actual weightings between fixed income and equities is primarily due to the rebalancing of the fixed income portfolio which was above target in fiscal year 2001. Rebalancing was necessary due to the deterioration in the U.S. equity markets at the end of fiscal year 2001. Proceeds from the sale of fixed income assets were allocated to equity purchases, increasing the allocation to equities. Short-term fiscal year 2002 actual weightings increased over the prior fiscal year due to increased liquidity requirements necessary to fund changes in portfolio weightings in a volatile market. These investment allocation targets are set by the TRS Board of Trustees with latitude for moderate deviations by TRS investment staff.



## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Changes in Net Assets – Pension Trust Fund (Dollars in Thousands)

|  | Fiscal Year<br>2002   | Fiscal Year<br>2001    | Dollar<br>Change    | Percentage<br>Change |
|--|-----------------------|------------------------|---------------------|----------------------|
| <b>Additions</b>                         |                       |                        |                     |                      |
| Member Contributions                     | \$ 1,450,312          | \$ 1,364,689           | \$ 85,623           | 6.3%                 |
| State and Other                          | 1,473,210             | 1,349,782              | 123,428             | 9.1%                 |
| Investment Income (Loss)                 | (6,074,335)           | (9,368,804)            | 3,294,469           | 35.2%                |
| <b>TOTAL ADDITIONS</b>                   | <b>\$ (3,150,813)</b> | <b>\$ (6,654,333)</b>  | <b>\$ 3,503,520</b> | <b>52.7%</b>         |
| <b>Deductions</b>                        |                       |                        |                     |                      |
| Retirement Benefits                      | \$ 4,369,131          | \$ 3,669,780           | \$ 699,351          | 19.1%                |
| Refunds of Contributions                 | 186,421               | 214,435                | (28,014)            | -13.1%               |
| Administrative Expenses                  | 24,597                | 20,795                 | 3,802               | 18.3%                |
| <b>TOTAL DEDUCTIONS</b>                  | <b>\$ 4,580,149</b>   | <b>\$ 3,905,010</b>    | <b>\$ 675,139</b>   | <b>17.3%</b>         |
| <b>Increase (Decrease) in Net Assets</b> | <b>\$ (7,730,962)</b> | <b>\$ (10,559,343)</b> | <b>\$ 2,828,381</b> | <b>26.8%</b>         |

**Additions.** Additions to fund benefits are accumulated through contributions and returns on invested funds. Member and state contributions for fiscal year 2002 totaled \$2.8 billion. This represents an increase of \$166 million, or approximately 6.3%, over fiscal year 2001 due to increases in membership and growth in the payroll base. The contribution rates for fiscal year 2002 remained the same as fiscal year 2001 with the members contributing 6.4% and the state contributing 6.0% of payroll.

TRS incurred overall negative returns on the market value of its investments during fiscal year 2002. Net depreciation in market value totaled (\$8.5) billion, a \$3.6 billion loss reduction as compared to the loss recorded in fiscal year 2001 of (\$12.1) billion. Interest, dividends and other investment income totaled \$2.37 billion, a decrease of (\$296) million from fiscal year 2001. Securities lending income, net of related expenses, was \$44.6 million, a decrease of (\$888,000) from fiscal year 2001. The total rate of return for the TRS investment portfolio in fiscal year 2002 was (7.81%) as compared to (10.61%) for fiscal year 2001. When comparing returns it is important to remember that as a pension fund, the TRS investment performance has a very long horizon. Some of the longer-term results for the total fund for the periods ending August 31, 2002 are:

- Three-Year (2.07%)
- Five-Year 4.20%
- Ten-Year 8.82%

**Deductions.** The expenses paid by the TRS pension fund include benefit payments, refunds of member contributions, and administrative expenses. Deductions for fiscal year 2002 totaled \$4.6 billion, an increase of \$675 million from fiscal year 2001. The increase in benefit payments to members and beneficiaries of \$699 million resulted from growth in the number of retirement recipients from 188,882 at the end of fiscal year 2001 to 201,441 at the end of fiscal year 2002, as well as increases in all average monthly annuities. Refunds of member contributions decreased (\$28) million, and administrative expenses increased \$3.8 million for fiscal year 2002 as compared to fiscal year 2001. Administrative expenses increases were due primarily to salary increases and additional employees, both authorized by the legislature for fiscal year 2002.

### Requests for Information

This financial report is designed to provide a general overview of the Teacher Retirement System finances for all those with an interest in the system's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Communications Department of the Teacher Retirement System, 1000 Red River Street, Austin, Texas 78701.





**Combined Statement of Fiduciary Net Assets**

AUGUST 31, 2002 (With Comparative Totals for August 31, 2001)

EXHIBIT



|   | FIDUCIARY FUND<br>TYPES  |   |
|---|--------------------------|---|
|   | Pension<br>Trust Fund    | Health Insurance<br>and Other Benefits<br>Trust Funds |
| <b>ASSETS</b>   |                          |   |
| <b>Cash:</b>  |                          |   |
| Cash in State Treasury  | \$ 811,753,540           | \$ 68,221,950   |
| Cash in Bank  | 17,390,684               |   |
| Cash on Hand  | 14,821,930               | 409   |
| <b>TOTAL CASH</b>   | <b>\$ 843,966,154</b>    | <b>\$ 68,222,359</b>                                  |
| <b>Legislative Appropriations</b>   | <b>\$</b>                | <b>\$ 483,287</b>                                     |
| <b>Receivables:</b>   |                          |   |
| Sale of Investments   | \$ 124,252,018           | \$  |
| Interest and Dividends  | 310,013,325              | 154,218   |
| Member and Retiree  | 43,755,910               | 15,255,612  |
| Due from State's General Revenue Fund   | 50,981,538               | 4,332,402   |
| Certification Fees  |                          | 10,000  |
| Reporting Employers   | 10,003,595               |   |
| Other   | 209,609                  | 1,000,000   |
| <b>TOTAL RECEIVABLES</b>  | <b>\$ 539,215,995</b>    | <b>\$ 20,752,232</b>                                  |
| <b>Investments (Note I.F.):</b>   |                          |   |
| Short-Term  | \$ 155,166,395           | \$ 95,839,435   |
| Equity Securities   | 47,158,684,804           |   |
| Fixed Income  | 21,936,912,851           |   |
| Alternative Investments   | 1,585,117,738            |   |
| Real Estate Held for Sale (Note IX.)  | 5,300,000                |   |
| <b>TOTAL INVESTMENTS</b>  | <b>\$ 70,841,181,788</b> | <b>\$ 95,839,435</b>                                  |
| Invested Securities Lending Collateral  | \$ 63,407,088            | \$ -0-  |
| <b>Other Assets:</b>  |                          |   |
| Land  | \$ 1,658,310             | \$  |
| Building, Capital Projects and Equipment, at Cost,<br>Net of Accumulated Depreciation | 31,188,802               |   |
| Deferred Assets   |                          |   |
| <b>TOTAL OTHER ASSETS</b>   | <b>\$ 32,847,112</b>     | <b>\$ -0-</b>   |
| <b>TOTAL ASSETS</b>   | <b>\$ 72,320,618,137</b> | <b>\$ 185,297,313</b>                                 |

| FIDUCIARY FUND<br>TYPES |                   | TOTALS            |  |
|-------------------------|-------------------|-------------------|--|
| Agency<br>Funds         | 2002              | 2001              |  |
| \$ 12,463               | \$ 879,987,953    | \$ 791,178,725    |  |
|                         | 17,390,684        | 13,083,124        |  |
|                         | 14,822,339        | 864,038           |  |
| \$ 12,463               | \$ 912,200,976    | \$ 805,125,887    |  |
| \$                      | \$ 483,287        | \$                |  |
| \$                      | \$ 124,252,018    | \$ 178,845,094    |  |
|                         | 310,167,543       | 390,567,606       |  |
|                         | 59,011,522        | 59,400,792        |  |
|                         | 55,313,940        | 100,461,337       |  |
|                         | 10,000            |                   |  |
| 8,358,434               | 18,362,029        | 16,726,121        |  |
|                         | 1,209,609         | 1,350,766         |  |
| \$ 8,358,434            | \$ 568,326,661    | \$ 747,351,716    |  |
| \$                      | \$ 251,005,830    | \$ 375,525,643    |  |
|                         | 47,158,684,804    | 50,166,933,864    |  |
|                         | 21,936,912,851    | 26,811,290,348    |  |
|                         | 1,585,117,738     | 1,395,972,229     |  |
|                         | 5,300,000         | 5,626,000         |  |
| \$ -0-                  | \$ 70,937,021,223 | \$ 78,755,348,084 |  |
| \$ -0-                  | \$ 63,407,088     | \$ 10,261,027,566 |  |
| \$                      | \$ 1,658,310      | \$ 1,658,310      |  |
|                         | 31,188,802        | 34,155,919        |  |
|                         |                   | 1,500             |  |
| \$ -0-                  | \$ 32,847,112     | \$ 35,815,729     |  |
| \$ 8,370,897            | \$ 72,514,286,347 | \$ 90,604,668,982 |  |

(to next page)

## Combined Statement of Fiduciary Net Assets

AUGUST 31, 2002 (With Comparative Totals for August 31, 2001)  
(concluded)

EXHIBIT



|   | FIDUCIARY FUND<br>TYPES  |   |
|---|--------------------------|---|
|   | Pension<br>Trust Fund    | Health Insurance<br>and Other Benefits<br>Trust Funds |
| <b>LIABILITIES</b>  |                          |   |
| Accounts Payable  | \$ 3,477,513             | \$ 9,565,548  |
| Benefits Payable  | 409,870,523              | 78,724,190  |
| Accounts Payable - General Revenue Fund   |                          |   |
| Funds Held for Others   |                          |   |
| Investments Purchased Payable   | 117,526,610              |   |
| Reinstatement Installment Receipts  | 28,336,570               |   |
| Compensable Absences Payable  | 2,197,472                |   |
| Securities Lending Collateral   | 63,407,088               |   |
| <b>TOTAL LIABILITIES</b>  | <b>\$ 624,815,776</b>    | <b>\$ 88,289,738</b>                                  |
| <b>NET ASSETS HELD IN TRUST<br/>FOR PENSION BENEFITS AND<br/>OTHER PURPOSES</b> | <b>\$ 71,695,802,361</b> | <b>\$ 97,007,575</b>                                  |

(A schedule of funding progress is presented on page 38.)

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

| FIDUCIARY FUND<br>TYPES |                   | TOTALS            |  |
|-------------------------|-------------------|-------------------|--|
| Agency<br>Funds         | 2002              | 2001              |  |
| \$                      | \$ 13,043,061     | \$ 13,372,364     |  |
|                         | 488,594,713       | 392,033,277       |  |
| 8,358,434               | 8,358,434         | 7,692,071         |  |
| 12,463                  | 12,463            | 7,085             |  |
|                         | 117,526,610       | 490,030,777       |  |
|                         | 28,336,570        | 22,422,527        |  |
|                         | 2,197,472         | 2,039,164         |  |
|                         | 63,407,088        | 10,261,027,566    |  |
| \$ 8,370,897            | \$ 721,476,411    | \$ 11,188,624,831 |  |
| \$ -0-                  | \$ 71,792,809,936 | \$ 79,416,044,151 |  |

## Combined Statement of Changes in Fiduciary Net Assets

YEAR ENDED AUGUST 31 (With Comparative Totals for August 31, 2001)

EXHIBIT



|   | Pension<br>Trust Fund     | Health Insurance<br>and Other Benefits |
|---|---------------------------|--|
| <b>ADDITIONS:</b>   |                           |  |
| <b>Contributions:</b>   |                           |  |
| Premiums  | \$                        | \$ 143,797,748                         |
| Member  | 1,450,311,521             | 47,378,092                             |
| State   | 1,201,257,586             | 380,271,220                            |
| Reporting Employers   | 157,781,530               |  |
| On Behalf Fringe Benefits Paid by the State (Note III.)   |                           | 63,638                                 |
| <b>TOTAL CONTRIBUTIONS</b>  | <b>\$ 2,809,350,637</b>   | <b>\$ 571,510,698</b>                  |
| <b>Investment Income:</b>   |                           |  |
| From Investing Activities:  |                           |  |
| Net Depreciation in Fair Value of Investments   | \$ (8,477,880,514)        | \$                                     |
| Interest  | 1,580,458,310             | 7,732,644                              |
| Dividends   | 790,900,360               |  |
| Net Income on Operations of Real Estate<br>Held for Sale (Note IX.)                             | 532,099                   |  |
| <b>TOTAL INVESTING ACTIVITIES INCOME (LOSS)</b>   | <b>\$ (6,105,989,745)</b> | <b>\$ 7,732,644</b>                    |
| Less Investing Activity Expenses  | (12,921,671)              |  |
| <b>NET INCOME (LOSS) FROM INVESTING ACTIVITIES</b>  | <b>\$ (6,118,911,416)</b> | <b>\$ 7,732,644</b>                    |
| From Securities Lending Activities:   |                           |  |
| Securities Lending Income   | \$ 221,743,809            | \$ 47                                  |
| Securities Lending Expenses:  |                           |  |
| Borrower Rebates  | (167,792,011)             |  |
| Management Fees   | (9,375,669)               |  |
| <b>Net Income from Securities Lending Activities</b>  | <b>\$ 44,576,129</b>      | <b>\$ 47</b>                           |
| <b>TOTAL NET INVESTMENT INCOME (LOSS)</b>   | <b>\$ (6,074,335,287)</b> | <b>\$ 7,732,691</b>                    |
| <b>Other Additions:</b>   |                           |  |
| Administrative/Certification Fees   | \$                        | \$ 433,198                             |
| Reinstatement of Withdrawals  | 64,705,929                |  |
| Reinstatement Fees  | 45,682,652                |  |
| Miscellaneous Revenues  | 491                       |  |
| Transfers from Employees Retirement System of Texas   | 3,091,464                 |  |
| Legislative Appropriations (Lapsed) for Administrative<br>Expenses                              |                           | 2,674,579                              |
| Legislative Appropriations for Excess Benefits (Note I.E.)                                      | 690,735                   |  |
| <b>TOTAL OTHER ADDITIONS</b>  | <b>\$ 114,171,271</b>     | <b>\$ 3,107,777</b>                    |
| <b>TOTAL ADDITIONS</b>  | <b>\$ (3,150,813,379)</b> | <b>\$ 582,351,166</b>                  |
| <b>DEDUCTIONS:</b>  |                           |  |
| Benefits  | \$ 4,344,255,724          | \$                                     |
| Withdrawal of Member Accounts   | 186,421,065               |  |
| Claims  |                           | 451,675,215                            |
| Claims Processing   |                           | 16,828,256                             |
| Administrative Expenses (Net of Investment Expenses<br>Above)                                   | 24,597,361                | 5,037,666                              |
| Transfers to Employees Retirement System of Texas   | 24,183,510                |  |
| Excess Benefits   | 690,735                   |  |
| <b>TOTAL DEDUCTIONS</b>   | <b>\$ 4,580,148,395</b>   | <b>\$ 473,541,137</b>                  |
| <b>Net Increase (Decrease)</b>  | <b>\$ (7,730,961,774)</b> | <b>\$ 108,810,029</b>                  |
| <b>Net Assets Held in Trust for Pension Benefits and<br/>Other Purposes - Beginning of Year</b> | <b>\$ 79,427,814,814</b>  | <b>\$ (11,770,663)</b>                 |
| <b>Restatements (Note I.F.)</b>   | <b>(1,050,679)</b>        | <b>(31,791)</b>                        |
| <b>Beginning of Year, As Restated</b>   | <b>\$ 79,426,764,135</b>  | <b>\$ (11,802,454)</b>                 |
| <b>Net Assets Held in Trust for Pension Benefits and<br/>Other Purposes - End of Year</b>       | <b>\$ 71,695,802,361</b>  | <b>\$ 97,007,575</b>                   |

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

| TOTALS                    |                            |
|---------------------------|----------------------------|
| 2002                      | 2001                       |
| \$ 143,797,748            | \$ 131,213,445             |
| 1,497,689,613             | 1,409,748,781              |
| 1,581,528,806             | 1,309,159,002              |
| 157,781,530               | 136,247,871                |
| 63,638                    | 39,062                     |
| <u>\$ 3,380,861,335</u>   | <u>\$ 2,986,408,161</u>    |
| \$ (8,477,880,514)        | \$ (12,070,475,742)        |
| 1,588,190,954             | 1,951,301,931              |
| 790,900,360               | 722,508,297                |
| 532,099                   | 1,484,864                  |
| <u>\$ (6,098,257,101)</u> | <u>\$ (9,395,180,650)</u>  |
| (12,921,671)              | (11,852,877)               |
| <u>\$ (6,111,178,772)</u> | <u>\$ (9,407,033,527)</u>  |
| \$ 221,743,856            | \$ 623,321,569             |
| (167,792,011)             | (568,343,763)              |
| (9,375,669)               | (9,510,703)                |
| <u>\$ 44,576,176</u>      | <u>\$ 45,467,103</u>       |
| <u>\$ (6,066,602,596)</u> | <u>\$ (9,361,566,424)</u>  |
| \$ 433,198                | \$ 70,340                  |
| 64,705,929                | 33,587,118                 |
| 45,682,652                | 34,761,307                 |
| 491                       | 6,733                      |
| 3,091,464                 | 2,068,339                  |
| 2,674,579                 | (38,522)                   |
| 690,735                   | 356,316                    |
| <u>\$ 117,279,048</u>     | <u>\$ 70,811,631</u>       |
| <u>\$ (2,568,462,213)</u> | <u>\$ (6,304,346,632)</u>  |
| \$ 4,344,255,724          | \$ 3,648,760,338           |
| 186,421,065               | 214,434,792                |
| 451,675,215               | 390,507,811                |
| 16,828,256                | 16,017,259                 |
| 29,635,027                | 23,490,686                 |
| 24,183,510                | 20,663,196                 |
| 690,735                   | 356,316                    |
| <u>\$ 5,053,689,532</u>   | <u>\$ 4,314,230,398</u>    |
| <u>\$ (7,622,151,745)</u> | <u>\$ (10,618,577,030)</u> |
| \$ 79,416,044,151         | \$ 90,034,621,181          |
| (1,082,470)               |                            |
| <u>\$ 79,414,961,681</u>  | <u>\$ 90,034,621,181</u>   |
| <u>\$ 71,792,809,936</u>  | <u>\$ 79,416,044,151</u>   |

## NOTES TO THE FINANCIAL STATEMENTS

### I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### A. REPORTING ENTITY

The Teacher Retirement System of Texas (TRS) is governed by a nine member board of trustees which has significant independence in the operations and management of the system. The legislature confirms trustees appointed by the governor, establishes laws with regard to structure, benefits and contributions, and authorizes pension trust fund administrative expenses. For financial reporting purposes, the state of Texas is considered the primary reporting government. TRS' financial statements are included and reported as a fiduciary fund type of the state.

This report includes all activities and organizations for which TRS exercises fiscal control and responsibility and includes all funds that comprise the system's legal entity.

TRS administers retirement and related benefits to employees and beneficiaries of employees of the public state supported educational institutions of Texas. It operates primarily under the provisions of Texas Constitution, Article XVI, Section 67 and Texas Government Code, Title 8, Subtitle C.

The system administers the Texas Public School Employees Group Insurance Program. This program provides two insurance plans, the Retired Plan and the Active Plan. The Retired Plan is considered a postemployment benefit which provides insurance coverage for certain persons (and their dependents) who retire under TRS. The Active Plan became effective September 1, 1996, and added an optional source of health insurance for school districts. The statutory authority for the insurance program is Tex. Ins. Code Ann. art.3.50-4.

Included in this report as a blended component unit are wholly owned subsidiary corporations established for the purpose of holding title to real estate acquired through foreclosure or deed in lieu of foreclosure. The system owns all the shares of the title-holding corporations and appoints all members to each board of directors. (Refer to note IX. for additional disclosure.)

#### B. MEASUREMENT FOCUS, BASIS OF ACCOUNTING, AND BASIS OF PRESENTATION

The accounts of TRS are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a complete set of self-balancing accounts that comprise its assets, liabilities, additions and deductions. The funds used to reflect the system's transactions are all fiduciary funds, including pension trust, health insurance and other benefits trusts, and agency funds. These fiduciary

funds account for assets held by TRS in a trustee capacity or as an agent on behalf of others.

The TRS Pension Trust Fund as well as the Health Insurance and Other Benefits Trust Funds (which include the Retired and Active Group Insurance Plans and the 403(b) Certification Program) are accounted for on the flow of economic resources measurement focus and the accrual basis of accounting. All economic resources, including financial and capital assets and related liabilities, both current and long-term, and the changes therein are reported in the funds' financial statements. Additions, including contributions, are recognized when earned, and deductions, including benefit payments, refunds, and claims, are recognized when the liability is incurred. Capital assets are depreciated.

Agency funds are custodial in nature and do not measure the results of operations. Assets and liabilities are recorded using the accrual basis of accounting. TRS agency funds are used to report assets collected and transferred to the state.

#### C. NEW ACCOUNTING PRONOUNCEMENT

The accompanying financial statements of TRS have been prepared to conform with Generally Accepted Accounting Principles (GAAP) as established by the Governmental Accounting Standards Board (GASB). In June 1999 the GASB issued Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments* (GASB 34). In June 2001 the GASB issued Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, which amended certain provisions of GASB 34. TRS has adopted the new pronouncement, as amended, for the year ended August 31, 2002 (with comparative totals for fiscal year 2001 restated in GASB 34 format).

The adoption of GASB 34 required TRS to make changes to the presentation of its basic financial statements, in addition to requiring the presentation of TRS Management's Discussion and Analysis (MD&A). The MD&A is considered to be required supplementary information and precedes the financial statements. Other changes include:

- The Combined Statement of Fiduciary Net Assets has been modified to include the Health Insurance and Other Benefits Trust Funds (formerly Expendable Trust Funds) in the net assets format.
- The Combined Statement of Changes in Fiduciary Net Assets has been modified to include the Health Insurance and Other Benefits Trust Funds (formerly Expendable Trust Funds), thus eliminating the Statement of Revenues and Expenditures for these funds.



**NOTES TO THE FINANCIAL STATEMENTS**

The adoption of GASB 34 did not have an impact on the net assets of the TRS Pension Trust Fund.

**D. COMPARATIVE TOTALS**

Total columns on the general purpose financial statements do not represent consolidated financial information. These totals are not necessary for a fair presentation of the financial statements but are presented to facilitate financial analysis.

**E. BUDGETS AND APPROPRIATIONS**

The system's pension trust fund receives appropriations for state contributions for retirement benefits. In fiscal years 2002 and 2001, state contributions were made to the retirement system at the rate of 6.0% of the aggregate compensation paid to retirement system members each year.

Effective September 1, 1997, legislation authorized TRS to administer a governmental excess benefit arrangement under section 415 (m) of the Internal Revenue Code of 1986 (26 U.S.C. section 415 (m)). This legislation created a separate, nonqualified, unfunded excess benefit arrangement outside the trust fund of the retirement system. Contributions to this arrangement are made from the state's general revenue appropriations. These contributions are not held in trust and may not be commingled with other funds of the retirement system. For reporting purposes only, the contributions and benefits are reflected on Exhibit II, Combined Statement of Changes in Fiduciary Net Assets.

The Pension Trust Fund administrative costs and capital outlay are controlled by an annual budget approved by the board of trustees. In fiscal year 2002, all administrative costs and capital outlay were paid from the pension trust fund.

The Health Insurance and Other Benefits Trust Funds administrative costs are controlled by means of an annual budget approved by the board of trustees. The Texas Public School Employees Group Insurance Program - Retired Plan receives appropriations from the state's General Revenue Fund equal to .50% of the salary of each public school active employee.

The Texas Public School Employees Group Insurance Program - Active Plan receives revenue from public school active employees, participating public school districts, and earnings on investment reserves. Operating expenditures for the Active Plan are to be recovered from administrative fees charged to participating public school districts.

The 403(b) Certification Program receives revenue from companies seeking to certify to TRS in order to offer to employees of educational institutions a qualified investment product under IRS Code Section 403(b) through payroll reduction.

TRS was appropriated \$3 million in fiscal year 2002 for implementation costs related to the new TRS-

ActiveCare program enacted by HB 3343, 77th Legislature.

**F. ASSETS, LIABILITIES, AND LEGAL RESERVES**

**Investments**

Investments are reported at fair value. The fair value of investments is based on published market prices and quotations at current exchange rates. For investments, mostly organized as limited partnerships and valued at \$2.439 billion dollars (3.4% of total investments) as of August 31, 2002, where no readily ascertainable market value exists (including private equity, strategically traded securities, high yield bonds, and real estate), management has determined fair values for the individual investments based on the capital account balance at the closest available reporting period, as communicated by the general partner, adjusted for subsequent contributions, distributions, management fees, and reserves. Management's estimated market values for investments without readily ascertainable market values could differ significantly if a ready market for these assets existed.

**Fixed Assets**

Fixed assets are capitalized at historical cost or, if not purchased, at fair value on date of acquisition. Depreciation has been provided over the estimated useful lives of the assets using the straight-line method. The estimated useful lives are as follows:

|   | <u>Years</u> |
|---|--------------|
| Building                                | 50           |
| Building Improvements                   | 15           |
| Furniture and Equipment - Office        | 5            |
| Capital Projects - Benefits Enhancement | 15           |

Net Assets Held in Trust for Pension Benefits and Other Purposes - Beginning of Year on Exhibits II and B has been restated for fiscal year 2002. The restatement amounts, which total \$1,082,470 reflect a change in capitalization threshold from \$1,000 to \$5,000 for TRS fixed assets.

**Liabilities**

Accounts payable represents the liability for assets or services received at fiscal year end for which payment is pending.

Benefits payable for the pension trust fund represents the liability for retirement, disability, and death benefits due at fiscal year end and payable within the next 30 days. Benefits payable for the health insurance trust funds includes an estimate for insurance claims incurred but not reported to the system at balance sheet date.

Investments purchased payable represents the

## NOTES TO THE FINANCIAL STATEMENTS

liability for securities purchased prior to fiscal year end for which cash payment will be made after fiscal year end.

Reinstatement installment receipts are payments for service purchases establishing additional creditable service. Payments are made on a monthly basis for up to five years until sufficient to cover the total cost of the service purchased. Amounts paid, less administrative expenses, are refundable on demand. Revenues will be reported at the time the payments are sufficient to cover the total cost.

Employee compensable leave balances are accounted for on a cost of service measurement focus. This means that all liabilities associated with a fund's activity are included on its statement of fiduciary net assets. Salary costs related to employees' rights to be compensated for future absences are accrued as expenses of the period in which services are rendered.

Employee compensable leave balances at August 31, 2002, and the system's monetary liability, computed by multiplying the ending balance of compensable leave times the year-end average individual employee hourly salary rate, were as follows:

*Pension Trust Fund:*

|                    | <u>Hours</u>  | <u>Dollars</u>     |
|--------------------|---------------|--------------------|
| Annual Leave       | 55,449        | \$1,728,861        |
| Compensatory Time: |               |                    |
| FLSA               | 5,664         | 137,148            |
| State              | 8,668         | 331,462            |
| Total              | <u>69,781</u> | <u>\$2,197,471</u> |

*Health Insurance and Other Benefits Trust Funds:*

|                    | <u>Hours</u> | <u>Dollars</u>   |
|--------------------|--------------|------------------|
| Annual Leave       | 2,617        | \$ 67,317        |
| Compensatory Time: |              |                  |
| FLSA               | 907          | 18,251           |
| State              | 397          | 10,742           |
| Total              | <u>3,921</u> | <u>\$ 96,310</u> |

The difference between the balance at August 31, 2001 and 2002, has been included in the funds' expenses for the year ended August 31, 2002.

**Legal Reserve Account Balances**

The pension trust fund has five legally required reserves. The balances in these reserves are sufficient to meet the statutory requirements. The Member Savings Account reserve represents the accumulation of active member deposits plus interest and has a balance at August 31, 2002, of \$16,423,728,463. The State Contribution Account consists of reserves available to fund future active member retirement, death, and survivor benefits and has a balance at August 31, 2002, of

\$16,236,923,769. The Retired Reserve Account represents reserves to pay retirement, death, and survivor benefits and post-retirement benefit increases and has a balance at August 31, 2002, of \$38,713,739,339. The Deferred Retirement Option Account consists of the accumulation of participating member deposits plus interest less benefits paid out and has a balance at August 31, 2002, of \$302,608,868. Net capital gains or losses are accumulated in the Interest Account and transferred to the State Contribution Account together with any other balance remaining in the Interest Account. The Expense Account represents reserves to pay administrative expenses of the pension trust fund that exceed the state's appropriations and that are required to perform the fiduciary duties of the board. This reserve has a balance at August 31, 2002, of \$18,801,922.

**G. INTERFUND TRANSACTIONS AND BALANCES**

Transactions between the system's funds have been classified in accordance with the following criteria which are consistent with generally accepted accounting principles.

**Quasi-external Transactions**

These transactions are reported using the appropriate classification accounts for additions or deductions as if transacted with parties external to the state, i.e., they are not presented as transfers. The interfund receivables and payables related to quasi-external transactions are classified as Accounts Receivable and Accounts Payable on the statement of fiduciary net assets.

The pension trust fund provides various services to the health insurance and other benefits trust funds and accounts for these services as quasi-external transactions.

**H. INTERAGENCY TRANSACTIONS AND BALANCES**

Interagency transactions have been classified using the above criteria for quasi-external transactions.

## II. DEPOSITS AND INVESTMENTS

**A. CASH IN STATE TREASURY**

All cash, except for the travel advance account and the securities clearing accounts as identified in note II.D., is deposited in the State Treasury. The State Treasury invests funds in time deposits, repurchase and reverse repurchase agreements, obligations of the United States, and obligations of various federal credit organizations. The State Treasury has an arrangement with financial institutions to collateralize state deposits in excess of depository insurance.

## NOTES TO THE FINANCIAL STATEMENTS

### B. CASH ON HAND

At August 31, 2002, the system had \$14,822,339 in cash on hand. Of this total, \$14,804,235 was related to checks for purchases of special service that were being held pending approval of rollover transfer forms. The remainder was deposited within the first few business days after fiscal year end.

### C. DEPOSITS IN BANK

The wholly owned subsidiary corporations (note IX.) each participate in a cash management program. Each corporation transfers excess cash balances to an open-ended mutual fund daily. Cash in Bank is held for pending investment transactions.

### D. SECURITIES CLEARING ACCOUNT

The system is authorized to contract with one or more commercial banks to serve as custodians of cash or securities, pending completion of investment settlements, and may authorize a bank acting as custodian to invest the cash in short-term securities approved by the board of trustees. The custodian accounts are maintained in the custodian's trust department or are structured to provide the maximum FDIC coverage.

### E. INVESTMENT LEGAL PROVISIONS AND OTHER CONSTRAINTS

Article XVI, Section 67 of the Constitution of the State of Texas authorizes the board of trustees to invest the funds of the system in such securities as the board may consider prudent investments. The board "shall exercise the judgment and care under the circumstances then prevailing that persons of ordinary prudence, discretion, and intelligence exercise in the management of their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable income therefrom as well as the probable safety of their capital" (the prudent person rule). In determining whether a trustee has exercised prudence with respect to an investment decision, such determination shall be made taking into consideration the investment of all the assets of the trust, or the assets of the collective investment vehicle, over which the trustee had management and control. Trustees establish specific asset allocations, benchmarks, eligible investments and quantitative criteria with the assistance of their investment counsel and investment advisors. Trustees utilize asset allocations and portfolio standards they believe are prudent and appropriate for the long-term objectives of the fund. Categories of permissible investments include equities, fixed income, real estate mortgages, cash equivalents, and alternative investments including the Texas Growth Fund.

### F. LEVEL OF RISK

Deposits and investments have been categorized to provide an indication of the level of risk at year end. The categories of risk for deposits are as follows:

1. Fully insured by federal depository insurance or collateralized with securities held by the system or its agent in the system's name. Collateral for Cash in State Treasury is held in the state's name.

2. Collateralized with securities held by the pledging financial institution's trust department or agent in the system's name.

3. Uncollateralized.

The highest balance of uncollateralized cash during the reporting period was \$63.8 million as a result of investments pending settlement. The total cash available at August 31, 2002, is as follows:

**NOTES TO THE FINANCIAL STATEMENTS**

|   | <u>Carrying<br/>Amount</u> | <u>Bank<br/>Balance</u> | <u>Category<br/>1</u> | <u>Category<br/>3</u> |
|---|----------------------------|-------------------------|-----------------------|-----------------------|
| Cash in Bank                              | \$ 17,258,010              | \$ 17,258,010           | \$                    | \$ 17,258,010         |
| Subsidiary Depository Lockbox<br>Accounts | 29,675                     | 29,675                  | 29,675                |                       |
| Subsidiary Other Operating<br>Accounts    | 82,999                     | 182,927                 | 182,927               |                       |
| Travel Advance Accounts                   | 20,000                     | 19,680                  | 19,680                |                       |
| <b>Total Cash in Bank</b>                 | <b>\$ 17,390,684</b>       | <b>\$ 17,490,292</b>    | <b>\$ 232,282</b>     | <b>\$ 17,258,010</b>  |
| Cash on Hand                              | 14,822,339                 |                         |                       |                       |
| Cash in State Treasury                    | 879,987,953                |                         |                       |                       |
| <b>Total Deposits<br/>(Exhibit I)</b>     | <b>\$ 912,200,976</b>      |                         |                       |                       |

TRS investments in securities are categorized below and on the following page to give an indication of the category risk level assumed by the system at August 31, 2002, as defined by GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements) and Reverse Repurchase Agreements*. Category 1, the lowest risk, includes investments that are insured or registered, or for which the securities are held by the system or its agent in the system's name. All investments are registered in the name of Teacher

Retirement System or in the name of the system's custodian which was established through a master trust custodial agreement. The securities are held by the custodian in the name of the system. The invested cash collateral held for securities lending is included in Category 3. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty. The fair values of investments at August 31, 2002, are as follows:

**Pension Trust Fund**

| <u>Investment Type</u>                         | <u>Category 1</u> | <u>Category 3</u> | <u>Category<br/>Rating Not<br/>Required</u> | <u>Total</u>      |
|--|-------------------|-------------------|---|-------------------|
| <b>Categorized:</b>                            |                   |                   |   |                   |
| Domestic Equities                              | \$ 37,974,077,904 | \$                | \$  | \$ 37,974,077,904 |
| International Equities                         | 9,098,557,004     |                   |   | 9,098,557,004     |
| U.S. Government Obligations                    | 5,829,589,161     |                   |   | 5,829,589,161     |
| U.S. Government Agency Obligations             | 2,527,285,651     |                   |   | 2,527,285,651     |
| Mortgage Backed Obligations                    |                   |                   |   |                   |
| U.S. Government Mortgage<br>Backed Obligations | 3,717,056,871     |                   |   | 3,717,056,871     |
| Collateralized Mortgage Obligations            | 2,552,505,766     |                   |   | 2,552,505,766     |
| Corporate Obligations                          | 4,309,307,754     |                   |   | 4,309,307,754     |
| International Government Obligations           | 693,433,208       |                   |   | 693,433,208       |
| International Obligations Other                | 1,219,284,646     |                   |   | 1,219,284,646     |

## NOTES TO THE FINANCIAL STATEMENTS

| <u>Investment Type</u>                                     | <u>Category 1</u>        | <u>Category 3</u>    | <u>Category<br/>Rating Not<br/>Required</u> | <u>Total</u>             |
|--|--------------------------|----------------------|---|--------------------------|
| <b>Not Categorized:</b>                                    |                          |                      |   |                          |
| Investments Held by Broker-Dealers                         |                          |                      |   |                          |
| Under Securities Loans:                                    |                          |                      |   |                          |
| Domestic Equities  |                          |                      | 53,550                                      | 53,550                   |
| International Equities                                     |                          | 152,550              | 7,857,777                                   | 8,010,327                |
| U.S. Government Obligations                                |                          |                      | 49,276,980                                  | 49,276,980               |
| Securities Purchased Pending Settlement:                   |                          |                      |   |                          |
| U.S. Government Agency Obligations                         |                          |                      | 5,070,050                                   | 5,070,050                |
| U.S. Government Mortgage Backed<br>Obligations             |                          |                      | 19,470,693                                  | 19,470,693               |
| Corporate Obligations                                      |                          |                      | 10,587,400                                  | 10,587,400               |
| Domestic Equities  |                          |                      | 75,033,411                                  | 75,033,411               |
| International Equities                                     |                          |                      | 2,952,608                                   | 2,952,608                |
| Alternative Investments:                                   |                          |                      |   |                          |
| Domestic   |                          |                      | 1,557,455,092                               | 1,557,455,092            |
| International  |                          |                      | 27,662,646                                  | 27,662,646               |
| High Yield Limited Partnership                             |                          |                      | 839,892,713                                 | 839,892,713              |
| Real Estate Held for Sale                                  |                          |                      | 5,300,000                                   | 5,300,000                |
| Mutual Fund Short-Term                                     |                          |                      | 134,003,789                                 | 134,003,789              |
| Private Placements   |                          |                      | 185,314,564                                 | 185,314,564              |
| <b>Total Investments (Exhibit I)</b>                       | <b>\$ 67,921,097,965</b> | <b>\$ 152,550</b>    | <b>\$ 2,919,931,273</b>                     | <b>\$ 70,841,181,788</b> |
| <b>Categorized Securities Lending</b>                      |                          |                      |   |                          |
| <b>Collateral:</b>   |                          |                      |   |                          |
| Corporate Obligations                                      | \$                       | \$ 50,000,000        | \$  | \$ 50,000,000            |
| <b>Not Categorized Securities Lending</b>                  |                          |                      |   |                          |
| <b>Collateral:</b>   |                          |                      |   |                          |
| Mutual Funds   |                          |                      | 13,407,088                                  | 13,407,088               |
| <b>Total Securities Lending<br/>Collateral (Exhibit I)</b> | <b>\$ -0-</b>            | <b>\$ 50,000,000</b> | <b>\$ 13,407,088</b>                        | <b>\$ 63,407,088</b>     |
| <b>Health Insurance Trust Fund - Retired Plan</b>          |                          |                      |   |                          |
| <b>Not Categorized:</b>                                    |                          |                      |   |                          |
| Mutual Funds   | \$                       | \$                   | \$ 72,145,403                               | \$ 72,145,403            |
| <b>Total Investments (Exhibit A)</b>                       | <b>\$ -0-</b>            | <b>\$ -0-</b>        | <b>\$ 72,145,403</b>                        | <b>\$ 72,145,403</b>     |
| <b>Health Insurance Trust Fund - Active Plan</b>           |                          |                      |   |                          |
| <b>Not Categorized:</b>                                    |                          |                      |   |                          |
| Mutual Funds   | \$                       | \$                   | \$ 23,694,032                               | \$ 23,694,032            |
| <b>Total Investments (Exhibit A)</b>                       | <b>\$ -0-</b>            | <b>\$ -0-</b>        | <b>\$ 23,694,032</b>                        | <b>\$ 23,694,032</b>     |

**NOTES TO THE FINANCIAL STATEMENTS**

**Derivative Investing**

In accordance with investment policy and fiduciary principles, the system invests in mortgage-backed securities, including certain agency collateralized mortgage obligations (CMO). CMO selections are chosen from a conservative segment which offers low volatility. CMO securities are included in aggregate with other U. S. Government Agency Mortgages in the disclosure of custodial risk.

**Covered Call Options**

TRS employs a covered call strategy. Premium income from writing covered call options is presented in the liabilities section of the statement of net assets and subsequently adjusted to the current market value. If a covered call option expires, TRS realizes a gain to the extent of the premium received. If a covered call option is exercised, the difference between the proceeds of the sale plus the amount of the premium and the cost of the security are realized as a gain or loss. If a covered call option is repurchased, the difference between the premium income received and the amount paid to close the option contract is realized as a gain or loss.

Premiums received from writing covered call options during the fiscal year were \$20,448,875, and the fair value of the options' liabilities as of August 31, 2002 was \$3,617,958.

**International Currency Contracts**

At the time the system is notified that an international trade has been consummated, the system trader will buy or sell a forward contract in the currency native to the security transaction for settlement date. This hedges against the risk of currency changes between trade and settlement dates. Risks associated with such contracts include movement in the value of the foreign currency related to the U.S. dollar and the ability of the counterparty to perform. At August 31, 2002, the system had forward contracts outstanding of \$3,454,675. Transactions involving foreign currency are accounted for in accordance with American Institute of Certified Public Accountants' Statement of Position 93-4, *Foreign Currency Accounting and Financial Statement Presentation for Investment Companies*.

**Securities Lending**

The system is authorized by state statute to contractually lend securities to investment brokers in accordance with policy established by the board of trustees. The system reports securities lending transactions in accordance with GASB Statement 28, *Accounting and Financial Reporting for Securities Lending Transactions*.

The contract with the system's custodian provides for lending a specific security from the system's holdings in return for cash or government securities as collateral. The collateral is based upon the lent security's fair value plus accrued income and received at 102% for domestic

securities and American Depository Receipts (ADR's) and 105% for international. Collateral is marked to market daily, and in the case it falls below 100% for domestic or 105% for international, is reinstated to the original requirements by the borrower. The system earns income from fees paid by the brokers and interest earned on collateral investments. The contract requires the custodian to indemnify the system if the borrower fails to return the securities or income distributions made while the securities are on loan. The system cannot pledge or sell securities collateral unless the borrower defaults. The maturities of the cash collateral investments are closely matched to the loan terms in order to minimize risk and more closely match cash flows. There were no violations of legal or contractual provisions, no borrower or lending agent default losses, and no recoveries of prior period losses during the year. At fiscal year end, there was no credit risk exposure to borrowers because the amounts owed to borrowers exceeded the amounts the borrowers owed the system. Some of the contractual restrictions for securities lending include:

1. Loans are to authorized borrowers who meet minimum requirements and execute a master securities lending agreement. Authorized borrowers have specific limits which vary from \$100 million to \$2.7 billion.
2. All loan originations are for less than one year.
3. Total market value of all loans cannot exceed 25% of the portfolio.

At August 31, 2002, the fair value of the securities on loan at Northern Trust was \$57,340,857 with the fair value of the collateral pledged by brokers of \$63,599,460. The system earned income of \$44,576,176 for fiscal year 2002. During the fiscal year, the average monthly fair value of loans outstanding ranged from \$12,611,425,580 to \$4,268,013,175 with a yearly average outstanding balance of \$11,152,291,912.

**G. ALTERNATIVE INVESTMENTS**

The following table presents the categories of investments within the alternative investment asset class at August 31, 2002.

|  | <u>Fair Value at<br/>August 31, 2002</u> |
|--|--|
| Limited Partnerships:                        |  |
| Private Equity Domestic                      | \$ 351,612,115                           |
| Private Equity International                 | 27,662,646                               |
| Real Estate Domestic                         | 419,492,507                              |
| Strategically Traded Domestic                | <u>786,350,470</u>                       |
| Total Alternative<br>Investments (Exhibit I) | <u>\$ 1,585,117,738</u>                  |

## NOTES TO THE FINANCIAL STATEMENTS

### H. CONTINGENT COMMITMENTS

At August 31, 2002, the pension trust fund had a potential obligation to fund private equity investments in the amount of U.S. dollars \$1,269,857,895 and EUROS 126,952,677 (\$124,503,208).

### III. FRINGE BENEFITS PAID BY THE STATE OF TEXAS

The state has a joint contributory retirement plan for substantially all its employees. The employees of TRS participate in the same plan they administer (note X).

For the fiscal year ended August 31, 2002, the state provided retirement contributions totaling \$63,638 on behalf of employees of the Health Insurance and Other Benefits trust funds. Although not paid by these funds, GASB Statement No. 24 requires recognition of this benefit as an expense of the program, and an offsetting revenue is recorded.

### IV. DEFERRED COMPENSATION

Employees of the system may elect to defer a portion of their earnings for income tax and investment purposes pursuant to authority granted in the Tex. Gov. Code Ann., Sec. 609.001. Two plans are available for employees. Both plans are administered by the Employees Retirement System. The system has no additional or unfunded liability for this program.

### V. CONTINGENT LIABILITIES

Sick leave, the accumulation of which is unlimited, is earned at the rate of eight hours per month and is taken only in the event of illness or paid to the estate of an employee in the event of death. The maximum sick leave that may be paid an employee's estate is one-half of the employee's accumulated entitlement or 336 hours, whichever is less. The system's policy is to recognize the cost of any sick leave when paid.

The system is contingently liable for benefits payable to retiring members who remain in a pending status longer than 30 days after fiscal year end.

In addition, under Tex. Ins. Code Ann. art. 3.51-7, the system was contingently liable to pay a lump sum death benefit not to exceed \$5,000, when added to the death benefit authorized under Tex. Gov. Code, Title 8, Chapter 824, to the beneficiaries of deceased, retired employees.

### VI. CONTINUANCE SUBJECT TO REVIEW

As provided by Tex. Gov. Code, Title 8, Sec. 825.006, "The board of trustees of the Teacher Retirement System of Texas is subject to review under Chapter 325 (Texas Sunset Act), but is not abolished under that Chapter. The

board shall be reviewed during the period in which state agencies abolished in 2007 are reviewed."

### VII. POST-EMPLOYMENT HEALTH CARE BENEFITS

#### TRS Employees

Employees of the system who retire with 10 or more years of service continue to receive health care and life insurance benefits through the Employees Life, Accident and Health Insurance and Benefits Fund, in accordance with Article 3.50-2, Texas Insurance Code. This fund is maintained and administered through the Employees Retirement System of Texas.

For the year ended August 31, 2002, the system contributed up to a maximum monthly amount on a pay-as-you-go basis toward a retiree's health and life insurance premiums as follows: Retiree Only, \$276; Retiree & Spouse, \$433; Retiree & Children, \$381; and Retiree & Family, \$539. The system covers 100% of a Retiree Only premium and 50% of additional premiums for family coverage. The basic plan includes up to \$2,500 for life insurance for the retiree. The retiree contributes any premium over and above the system's contribution for other coverage. The board has adopted contributions based on rates set by the Legislature on a biennial basis. At August 31, 2002, there were 124 retirees and their beneficiaries receiving post-employment health care and life insurance benefits. For the year ended August 31, 2002, the system recognized and paid actual expenditures of \$461,113 for these benefits.

#### Public School Employees

TRS, as trustee, administers the Texas Public School Employees Group Insurance Program - Retired Plan (TRS-Care) and the related fund in accordance with Article 3.50-4, Texas Insurance Code.

Eligibility, generally, includes TRS public school retirees with 10 or more years of service and their dependents. Retirees can receive a free basic level of coverage and optional coverage is also available. All dependent coverage is optional. Basic coverage is a comprehensive major medical group health insurance plan. During fiscal year 2002, deductibles were \$1,800 for those having Part A of Medicare or \$4,500 for those without Part A. At fiscal year end there were 147,973 participants in the plan, of which 19,780 were dependent spouses.

Funding for free basic coverage is provided by the program based upon public school district payroll. The state of Texas and active public school employee contribution rates are set by statute at .50% and .25% of public school payroll, respectively. Funding for optional coverage is provided by those participants selecting the optional coverage. Expenses for the Retired Insurance Plan (Exhibit B) are recognized as retirees report claims and include a provision for estimated claims incurred but

## NOTES TO THE FINANCIAL STATEMENTS

not yet reported.

Funding for the Retired Plan was originally projected to last 10 years through fiscal year 1995. Even with additional state appropriations of \$76.2 million received in September 2000, the fund ended fiscal year 2001 with a net asset deficit of (\$35.9) million. The fund received \$285.5 million in fiscal year 2002 and ended the year with \$71.9 million in net assets. The fund will receive \$124.7 million in additional appropriations during fiscal year 2003 for the program to continue operations.

### VIII. RISK MANAGEMENT

The Texas Public School Employees Group Insurance Program - Active Plan became effective September 1, 1996. The plan provides an optional health insurance program for school district employees. A school district may elect to participate in this program, and participation by an employee of a participating school district is optional. The risk associated with this program is retained by the plan and the participating district's risk is limited to the current year's premiums. Since September 1, 2000, no districts have been enrolled in the plan. During fiscal year 2002, there were no claims payments for claims incurred in prior fiscal years. As of August 31, 2002, we are aware of no unpaid claims related to this plan.

The 77th Texas Legislature enacted the Texas School Employees Uniform Group Health Coverage Act, establishing a new statewide health coverage program for public school employees and their dependents. The Teacher Retirement System will administer this program. Enrollment commences in September 2002. This new plan begins September 1, 2002 and will include employees of most small to mid-size districts, charter schools, education service centers and certain other employers.

### IX. CORPORATIONS

TRS establishes corporations for the purpose of holding title to property acquired through foreclosure or deed in lieu of foreclosure. The corporations must remit profits from the management and sale of the property to the system. Corporate directors are subject to appointment and removal by the board of trustees. For financial reporting purposes, the properties are classified as long-term investments and the net results of operations are included in investment income. At August 31, 2002, the system had three corporations with one corporation holding title to commercial real estate with \$6.2 million in assets. Separate financial statements for the corporations are available by contacting the TRS Communications Department. A summary of operations is as follows:

|  | <u>2002</u>         | <u>2001</u>           |
|--|---------------------|-----------------------|
| <b>REVENUES:</b>                                     |                     |                       |
| Rental Income  | \$ 2,249,727        | \$ 3,567,090          |
| Expense Reimbursement                                | 164,194             | 134,908               |
| Interest Income                                      | 42,841              | 283,386               |
| Total Revenues                                       | <u>\$ 2,456,762</u> | <u>\$ 3,985,384</u>   |
| <b>EXPENSES:</b>                                     |                     |                       |
| Operating Expenses                                   | \$ 258,337          | \$ 683,919            |
| Plant Operations                                     | 1,330,559           | 1,481,040             |
| Taxes and Insurance                                  | 335,767             | 335,561               |
| Total Expenses                                       | <u>\$ 1,924,663</u> | <u>\$ 2,500,520</u>   |
| <b>NET INCOME FROM OPERATIONS</b>                    |                     |                       |
| (Exhibit II)   | <u>\$ 532,099</u>   | <u>\$ 1,484,864</u>   |
| <b>NET DEPRECIATION IN FAIR VALUE</b>                |                     |                       |
|  | <u>\$ (665,586)</u> | <u>\$ (2,689,385)</u> |
| <b>TOTAL NET LOSS AND DEPRECIATION IN FAIR VALUE</b> |                     |                       |
|  | <u>\$ (133,487)</u> | <u>\$ (1,204,521)</u> |

### X. PENSION DISCLOSURE

#### A. Plan Description

TRS is the administrator of a multiple-employer public employee retirement system (PERS). It is a cost-sharing PERS with one exception: risks and costs are generally not shared by the employing district (unless the employing district is a senior college, medical school, or state agency, in which case the employer is considered the state of Texas) but are the liability of the state of Texas. By statute, the state of Texas contributes to the retirement system an amount equal to the current authorized rate times the aggregate annual compensation of all members of the pension trust fund during that fiscal year. However, for fiscal year 2002 the pension trust fund paid the employer's share for its own employees.

For members of the system entitled to the minimum salary for certain school personnel under Section 21.402, Education Code, the employing district shall pay the state's contribution on the portion of the member's salary that exceeds the statutory minimum.

At August 31, 2002, the number of participating employing districts was the following:

|  |              |
|--|--------------|
| Public Schools, Service Centers<br>and Charter Schools | 1,241        |
| Community and Junior Colleges                          | 51           |
| Universities   | 43           |
| Medical Schools  | 8            |
| Other Entities   | 2            |
| Total  | <u>1,345</u> |



**NOTES TO THE FINANCIAL STATEMENTS**

All employees of public, state-supported educational institutions in Texas who are employed for one-half or more of the standard work load and who are not exempted from membership under Texas Government Code, Title 8, Section 822.002, are covered by the system.

At August 31, 2002, TRS gross membership before actuarial adjustments consisted of the following:

|  |                       |
|--|-----------------------|
| Retirees and beneficiaries currently receiving benefits              | 201,441               |
| Terminated employees entitled to benefits but not yet receiving them | <u>38,554</u>         |
| <b>Total</b>   | <b><u>239,995</u></b> |
| Current Active Members:  |                       |
| Fully-Vested   | 451,409               |
| Non-Vested   | <u>372,504</u>        |
| <b>Total</b>   | <b><u>823,913</u></b> |

A brief statement about benefits follows. Authority under which these benefits are established is located in note I.A.

The normal service retirement is at age 65 with 5 years of credited service or when the sum of the member's age and years of credited service equals or exceeds 80 years. Reduced service retirement is at age 55 with 5 years of credited service and any age below 50 with 30 years of credited service.

A member is fully vested after 5 years of creditable service and entitled to any benefit for which eligibility requirements have been met.

Effective September 1, 2001, the 77th Legislature, Regular Session, granted an ad hoc postretirement benefit increase which increased the monthly annuity payroll by \$28.7 million. Also enacted by the 77th Legislature and effective September 1, 2001, was an increase in the retirement annuity multiplier from 2.2 percent to 2.3 percent.

The state of Texas contribution rate is set at 6.0% for fiscal years 2001, 2002, and 2003. The member contribution rate is set at 6.4% for fiscal years 2001, 2002, and 2003. These rates are set by state statutes. In certain instances, the reporting district (public school, college, university, medical school or other entity) is required to make all or a portion of the state's contribution.

**B. Contributions Required and Contributions Made**

Contribution requirements are not actuarially determined but are established pursuant to the following state funding policy: (1) The state constitution requires the legislature to establish a member contribution rate of not less than 6% of the member's annual compensation and a state contribution rate of not less than 6% and not more than 10% of the aggregate annual compensation of all members of the system during that fiscal year. (2) A state statute prohibits benefit improvements or contribution reductions if, as a result of the particular

action, the time required to amortize TRS' unfunded actuarial liabilities would be increased to a period that exceeds 31 years, or, if the amortization period already exceeds 31 years, the period would be increased by such action.

Actuarial implications of the funding provided in this manner are determined by the system's actuary. Current contribution rates are indicated in section A. of this note. Total contributions paid to the pension plan in 2002 based on a 6% contribution rate amounted to \$2,809,350,637 of which \$1,450,311,521 was from members, \$1,201,257,586 was from the state of Texas, and \$157,781,530 was from reporting employers.

Based on the actuarial valuation as of August 31, 2002, the system has reverted to an underfunded status and the unfunded actuarial accrued liability (UAAL) is now \$3,287,442,769. This valuation shows a normal cost equal to 12.67% of pay. Since the state contribution rate of 6.00% of pay plus the member contribution rate of 6.40% of pay total 12.40% of pay, and since this total contribution rate is less than the normal cost rate, there are no contributions available to amortize the UAAL.

Using Governmental Accounting Standards Board (GASB) Statement No. 25 as a guide, the state contribution rate would need to increase from 6.00% of pay to 7.15% of pay. This rate would fund the normal cost and amortize the UAAL as of August 31, 2002 over the 30-year period called for by GASB Statement No. 25.

**C. Six-Year Historical Trend Information**

This Required Supplementary Information, located immediately following the Notes, provides indicators and trends which may be useful in assessing progress made in accumulating sufficient assets to pay benefits when due.

## Required Supplementary Information

PENSION TRUST FUND - FISCAL YEARS 1997 - 2002

### SCHEDULE OF FUNDING PROGRESS

Taking into account only the dollar amounts of aggregate actuarial accrued liabilities and unfunded actuarial accrued liabilities (UAAL) can be misleading. The dollar amounts of these two items can be increasing at a time when their actual substance may be decreasing. Dividing valuation asset dollars by aggregate actuarial accrued liability dollars and dividing UAAL dollars by active member payroll dollars provide clarifying indices. The larger the ratio of valuation assets to aggregate actuarial accrued liabilities, the stronger the system. Observation of these relative indices over a period of years will give an indication of whether the system is becoming stronger or weaker.

(MONEY AMOUNTS SHOWN IN MILLIONS)

| (1)<br>Valuation<br>as of<br>August 31 | (2)<br>Actuarial<br>Valuation<br>of Assets | (3)<br>Actuarial<br>Accrued<br>Liability<br>(AAL) | (4)<br>Unfunded<br>AAL<br>(3)-(2) | (5)<br>Funding Ratio<br>Assets as a<br>% of AAL<br>(2)/(3) | (6)<br>Annual<br>Covered<br>Payroll | (7)<br>Unfunded<br>AAL as<br>a % of<br>Covered<br>Payroll<br>(4)/(6) |
|--|--|---|-----------------------------------|--|-------------------------------------|--|
| 1997                                   | \$ 53,760                                  | \$ 53,906   | \$ 146                            | 99.7%  | \$ 17,044                           | 0.9%   |
| 1998                                   | 60,357                                     | 57,893  | (2,463)                           | 104.3  | 18,325                              | (13.4)   |
| 1999                                   | 69,435                                     | 67,245  | (2,190)                           | 103.3  | 19,529                              | (11.2)   |
| 2000                                   | 79,328                                     | 73,882  | (5,446)                           | 107.4  | 21,920                              | (24.8)   |
| 2001                                   | 86,352                                     | 84,217  | (2,135)                           | 102.5  | 23,365                              | (9.1)  |
| 2002                                   | 86,035                                     | 89,322  | 3,287                             | 96.3   | 24,818                              | 13.2   |

### SCHEDULE OF CONTRIBUTIONS FROM EMPLOYERS AND OTHER CONTRIBUTING ENTITIES

#### Employer and State Contributions Annual Required Contributions

| Year<br>Ended | Rate  | Dollars        |                |                | Percentage<br>Contributed |
|---------------|-------|----------------|----------------|----------------|---------------------------|
|               |       | From State     | From Employers | Total          |                           |
| 1997          | 6.00% | \$ 869,726,704 | \$ 86,940,233  | \$ 956,666,937 | 100%                      |
| 1998          | 6.00  | 931,234,586    | 91,478,817     | 1,022,713,403  | 100                       |
| 1999          | 6.00  | 977,345,552    | 108,892,209    | 1,086,237,761  | 100                       |
| 2000          | 6.00  | 1,090,716,271  | 119,060,600    | 1,209,776,871  | 100                       |
| 2001          | 6.00  | 1,142,792,114  | 136,247,871    | 1,279,039,985  | 100                       |
| 2002          | 7.15  | 1,431,498,623  | 188,022,990    | 1,619,521,613  | 84                        |

### NOTES TO REQUIRED SUPPLEMENTARY INFORMATION

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows:

|                                      |                        |   |                 |
|--------------------------------------|------------------------|---|-----------------|
| <b>Valuation Date</b>                | August 31, 2002        | <b>Actuarial Assumptions:</b>                       |                 |
| <b>Actuarial Cost Method</b>         | Entry Age Normal       | <b>Investment Rate of Return *</b>                  | 8.00%           |
| <b>Amortization Method</b>           | Level Percent, Open    | <b>Projected Salary Increases *</b>                 | 4.00% to 26.15% |
| <b>Remaining Amortization Period</b> | Infinite               | <b>Weighted Average Projected Salary Increases*</b> | 6.83%           |
| <b>Asset Valuation Method</b>        | 5-Year Smoothed Market | <b>Cost-of-Living Adjustments</b>                   | None            |
|                                      |                        | <b>*Includes Inflation at 3.00%</b>                 |                 |



## Combining Statement of Fiduciary Net Assets

HEALTH INSURANCE AND OTHER BENEFITS TRUST FUNDS  
 AUGUST 31, 2002 (With Comparative Totals for August 31, 2001)

EXHIBIT



|   | Health Insurance and Other Benefits Trust Funds |                       |
|---|---|-----------------------|
|   | Retired Insurance Plan                          | Active Insurance Plan |
| <b>ASSETS</b>   |   |                       |
| <b>Cash:</b>  |   |                       |
| Cash in State Treasury  | \$ 66,856,021                                   | \$ 1,164,885          |
| Cash on Hand  | 409   |                       |
| <b>TOTAL CASH</b>   | <b>\$ 66,856,430</b>                            | <b>\$ 1,164,885</b>   |
| <b>Legislative Appropriations</b>                                       | <b>\$</b>                                       | <b>\$ 483,287</b>     |
| <b>Accounts Receivable:</b>   |   |                       |
| Interest  | \$ 116,091                                      | \$ 38,127             |
| Member and Retiree  | 15,255,612                                      |                       |
| Due from State's General Revenue Fund                                   | 4,332,402                                       |                       |
| Certification Fees  |   |                       |
| Other   | 1,000,000                                       |                       |
| <b>TOTAL ACCOUNTS RECEIVABLE</b>  | <b>\$ 20,704,105</b>                            | <b>\$ 38,127</b>      |
| <b>Short-Term Investments</b>   | <b>\$ 72,145,403</b>                            | <b>\$ 23,694,032</b>  |
| <b>Fixed Assets</b>   | <b>\$</b>                                       | <b>\$</b>             |
| <b>TOTAL ASSETS</b>   | <b>\$ 159,705,938</b>                           | <b>\$ 25,380,331</b>  |
| <b>LIABILITIES</b>  |   |                       |
| Accounts Payable  | \$ 9,035,764                                    | \$ 524,739            |
| Benefits Payable  | 78,724,190                                      |                       |
| <b>TOTAL LIABILITIES</b>  | <b>\$ 87,759,954</b>                            | <b>\$ 524,739</b>     |
| <b>NET ASSETS HELD IN TRUST FOR HEALTH INSURANCE AND OTHER BENEFITS</b> | <b>\$ 71,945,984</b>                            | <b>\$ 24,855,592</b>  |

| Health Insurance<br>and Other Benefits<br>Trust Funds |  | TOTALS |  |
|---|--|--------|--|
| 403(b) Certification<br>Program                       | 2002<br>(Exhibit I)  |        | 2001   |
| \$ 201,044  | \$ 68,221,950<br>409   | \$     | 14,930,517<br>6,133                              |
| \$ 201,044  | \$ 68,222,359  | \$     | 14,936,650                                       |
| \$  | \$ 483,287   | \$     |  |
| \$  | \$ 154,218<br>15,255,612<br>4,332,402<br>10,000<br>1,000,000 | \$     | 110,937<br>14,013,922<br>10,698,875<br>1,015,589 |
| \$ 10,000   | \$ 20,752,232  | \$     | 25,839,323                                       |
| \$  | \$ 95,839,435  | \$     | 24,217,161                                       |
| \$  | \$   | \$     | 31,884   |
| \$ 211,044  | \$ 185,297,313   | \$     | 65,025,018                                       |
| \$ 5,045  | \$ 9,565,548<br>78,724,190                                   | \$     | 9,475,681<br>67,320,000                          |
| \$ 5,045  | \$ 88,289,738  | \$     | 76,795,681                                       |
| \$ 205,999  | \$ 97,007,575  | \$     | (11,770,663)                                     |

## Combining Statement of Changes in Fiduciary Net Assets

HEALTH INSURANCE AND OTHER BENEFITS TRUST FUNDS  
 YEAR ENDED AUGUST 31 (With Comparative Totals for August 31, 2001)

EXHIBIT



|   | Health Insurance and Other Benefits Trust Funds |                       |
|---|---|-----------------------|
|   | Retired Insurance Plan                          | Active Insurance Plan |
| <b>Additions:</b>   |   |                       |
| Contributions:  |   |                       |
| Premiums  | \$ 143,797,748                                  | \$                    |
| Member Contributions  | 47,378,092                                      |                       |
| State Contributions   | 380,271,220                                     |                       |
| On Behalf Fringe Benefits Paid by the State (Note III.)                                     | 35,842  | 23,843                |
| Investment Income:  |   |                       |
| Interest  | 7,140,513                                       | 590,967               |
| Securities Lending  | 47  |                       |
| Net Appreciation in Fair Value  |   |                       |
| Other Additions:  |   |                       |
| Administrative/Certification Fees   |   | 108,198               |
| Legislative Appropriations  |   | 2,674,579             |
| <b>TOTAL ADDITIONS</b>  | <b>\$ 578,623,462</b>                           | <b>\$ 3,397,587</b>   |
| <b>Deductions:</b>  |   |                       |
| Claims  | \$ 451,709,670                                  | \$ (34,455)           |
| Claims Processing   | 16,828,256                                      |                       |
| Internal Administration   | 2,163,441                                       | 2,750,107             |
| <b>TOTAL DEDUCTIONS</b>   | <b>\$ 470,701,367</b>                           | <b>\$ 2,715,652</b>   |
| <b>Net Increase (Decrease)</b>  | <b>\$ 107,922,095</b>                           | <b>\$ 681,935</b>     |
| <b>Net Assets Held in Trust for Health Insurance and Other Benefits - Beginning of Year</b> | <b>\$ (35,950,516)</b>                          | <b>\$ 24,179,853</b>  |
| <b>Restatements</b>   | <b>(25,595)</b>                                 | <b>(6,196)</b>        |
| <b>Beginning of Year, As Restated</b>   | <b>\$ (35,976,111)</b>                          | <b>\$ 24,173,657</b>  |
| <b>Net Assets Held in Trust for Health Insurance and Other Benefits - End of Year</b>       | <b>\$ 71,945,984</b>                            | <b>\$ 24,855,592</b>  |

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

| Health Insurance<br>and Other Benefits<br>Trust Funds |                      | TOTALS |              |
|---|----------------------|--------|--------------|
| 403(b) Certification<br>Program                       | 2002<br>(Exhibit II) |        | 2001         |
| \$  | \$ 143,797,748       | \$     | 131,213,445  |
|   | 47,378,092           |        | 45,059,393   |
|   | 380,271,220          |        | 166,366,888  |
| 3,953   | 63,638               |        | 39,062       |
| 1,164   | 7,732,644            |        | 7,179,597    |
|   | 47                   |        | 3,197        |
|   |                      |        | 55,070       |
| 325,000   | 433,198              |        | 70,340       |
|   | 2,674,579            |        |              |
| \$ 330,117  | \$ 582,351,166       | \$     | 349,986,992  |
| \$  | \$ 451,675,215       | \$     | 390,507,811  |
|   | 16,828,256           |        | 16,017,259   |
| 124,118   | 5,037,666            |        | 2,695,557    |
| \$ 124,118  | \$ 473,541,137       | \$     | 409,220,627  |
| \$ 205,999  | \$ 108,810,029       | \$     | (59,233,635) |
| \$  | \$ (11,770,663)      | \$     | 47,462,972   |
|   | (31,791)             |        |              |
| \$ -0-  | \$ (11,802,454)      | \$     | 47,462,972   |
| \$ 205,999  | \$ 97,007,575        | \$     | (11,770,663) |

## Combining Statement of Changes in Assets and Liabilities

AGENCY FUNDS

YEAR ENDED AUGUST 31, 2002

EXHIBIT



|  | Balances<br>September 1,<br>2001 | Additions             | Deductions            | Balances<br>August 31,<br>2002 |
|--|----------------------------------|-----------------------|-----------------------|--------------------------------|
| <b>UNAPPROPRIATED RECEIPTS</b>   |                                  |                       |                       |                                |
| <b>Collections on Behalf<br/>of the State's<br/>General Revenue Fund</b> |                                  |                       |                       |                                |
| <b>Assets:</b>   |                                  |                       |                       |                                |
| Cash in State Treasury   | \$                               | \$133,889,420         | \$133,889,420         | \$                             |
| Accounts Receivable -<br>Reporting Employers                             | 7,692,071                        | 8,358,434             | 7,692,071             | 8,358,434                      |
| <b>TOTAL ASSETS</b>  | <b>\$ 7,692,071</b>              | <b>\$142,247,854</b>  | <b>\$141,581,491</b>  | <b>\$ 8,358,434</b>            |
| <b>Liabilities:</b>  |                                  |                       |                       |                                |
| Accounts Payable - General<br>Revenue Fund                               | \$ 7,692,071                     | \$ 8,358,434          | \$ 7,692,071          | \$ 8,358,434                   |
| <br><b>OTHER AGENCY FUNDS</b>  |                                  |                       |                       |                                |
| <b>Employees' Savings<br/>Bond Account</b>                               |                                  |                       |                       |                                |
| <b>Assets:</b>   |                                  |                       |                       |                                |
| Cash in State Treasury   | \$ 1,705                         | \$ 19,925             | \$ 20,455             | \$ 1,175                       |
| <b>Liabilities:</b>  |                                  |                       |                       |                                |
| Funds Held for Others  | \$ 1,705                         | \$ 19,870             | \$ 20,400             | \$ 1,175                       |
| <br><b>Direct Deposit Correction<br/>Account Fund</b>                    |                                  |                       |                       |                                |
| <b>Assets:</b>   |                                  |                       |                       |                                |
| Cash in State Treasury   | \$ 5,380                         | \$ 1,769,221          | \$ 1,763,313          | \$ 11,288                      |
| <b>Liabilities:</b>  |                                  |                       |                       |                                |
| Funds Held for Others  | \$ 5,380                         | \$ 1,763,841          | \$ 1,757,933          | \$ 11,288                      |
| <br><b>TOTALS - ALL AGENCY FUNDS</b>                                     |                                  |                       |                       |                                |
|  |                                  |                       |                       | <b>(Exhibit I)</b>             |
| <b>Assets:</b>   |                                  |                       |                       |                                |
| Cash in State Treasury   | \$ 7,085                         | \$ 135,678,566        | \$ 135,673,188        | \$ 12,463                      |
| Accounts Receivable -<br>Reporting Employers                             | 7,692,071                        | 8,358,434             | 7,692,071             | 8,358,434                      |
| <b>TOTAL ASSETS</b>  | <b>\$ 7,699,156</b>              | <b>\$ 144,037,000</b> | <b>\$ 143,365,259</b> | <b>\$ 8,370,897</b>            |
| <b>Liabilities:</b>  |                                  |                       |                       |                                |
| Accounts Payable - General<br>Revenue Fund                               | \$ 7,692,071                     | \$ 8,358,434          | \$ 7,692,071          | \$ 8,358,434                   |
| Funds Held for Others  | 7,085                            | 1,783,711             | 1,778,333             | 12,463                         |
| <b>TOTAL LIABILITIES</b>   | <b>\$ 7,699,156</b>              | <b>\$ 10,142,145</b>  | <b>\$ 9,470,404</b>   | <b>\$ 8,370,897</b>            |



## Comparative Statement of Changes in Account Balance

PENSION TRUST FUND

YEAR ENDED AUGUST 31 (With Comparative Totals for August 31, 2001)

SCHEDULE



| <b>INTEREST ACCOUNT</b>  | <b>2002</b>               | <b>2001</b>               |
|--|---------------------------|---------------------------|
| <b>Additions:</b>  |                           |                           |
| Interest, Dividends and Other Income:  |                           |                           |
| Short-Term   | \$ 27,474,628             | \$ 49,000,511             |
| Equity Securities  | 747,112,394               | 683,335,807               |
| Fixed Income   | 1,549,712,877             | 1,891,786,284             |
| Alternative Investments  | 43,787,966                | 39,256,213                |
| Net Income on Operations of Real Estate Held for Sale                                    | 532,099                   | 1,484,864                 |
| Securities Lending Program   | 44,576,129                | 45,463,906                |
| Miscellaneous  | 3,270,805                 | 3,251,816                 |
| Net Depreciation in Fair Value of Investments  | (8,477,880,514)           | (12,070,530,812)          |
| <b>TOTAL ADDITIONS</b>   | <b>\$ (6,061,413,616)</b> | <b>\$ (9,356,951,411)</b> |
| <b>Deductions:</b>   |                           |                           |
| Operating Transfers Out:   |                           |                           |
| Allocation of Interest to:   |                           |                           |
| Member Savings Account   | \$ 791,661,372            | \$ 727,098,340            |
| State Contribution Account   | (1,332,164,480)           | (575,999,306)             |
| Retired Reserve Account  | 2,907,149,420             | 2,516,925,601             |
| Deferred Retirement Option Account Expense Account                                       | 9,820,586                 | 11,554,766                |
| 40,000,000   | 40,000,000                | 34,000,000                |
| Transfer to State Contribution Account for Net Depreciation in Fair Value of Investments | (8,477,880,514)           | (12,070,530,812)          |
| <b>TOTAL DEDUCTIONS</b>  | <b>\$ (6,061,413,616)</b> | <b>\$ (9,356,951,411)</b> |
| <b>Net Increase in Account Balance</b>   | <b>\$ -0-</b>             | <b>\$ -0-</b>             |
| <b>Account Balance - Beginning September 1</b>   | <b>-0-</b>                | <b>-0-</b>                |
| <b>Account Balance - Ending August 31</b>  | <b>\$ -0-</b>             | <b>\$ -0-</b>             |

## Comparative Statement of Changes in Account Balance

PENSION TRUST FUND

YEAR ENDED AUGUST 31 (With Comparative Totals for August 31, 2001)

SCHEDULE



| <b>MEMBER SAVINGS ACCOUNT</b>                               | <b>2002</b>              | <b>2001</b>              |
|---|--------------------------|--------------------------|
| <b>Additions:</b>   |                          |                          |
| Member Deposits:  |                          |                          |
| Eligible for State Contributions                            | \$ 1,450,311,521         | \$ 1,364,689,388         |
| Not Eligible for State Contributions                        | 64,705,929               | 33,587,118               |
| Operating Transfers In:                                     |                          |                          |
| Allocation from Interest Account                            | 791,661,372              | 727,098,340              |
| <b>TOTAL ADDITIONS</b>                                      | <b>\$ 2,306,678,822</b>  | <b>\$ 2,125,374,846</b>  |
| <b>Deductions:</b>  |                          |                          |
| Withdrawal of Member Accounts                               | \$ 186,421,065           | \$ 214,434,792           |
| Operating Transfers Out:                                    |                          |                          |
| Transfer to Retired Reserve Account<br>for Dormant Accounts | 5,130,631                | 9,193,732                |
| Transfer to Retired Reserve Account<br>to Fund Benefits     | 1,047,094,782            | 832,300,538              |
| <b>TOTAL DEDUCTIONS</b>                                     | <b>\$ 1,238,646,478</b>  | <b>\$ 1,055,929,062</b>  |
| <b>Net Increase in Account Balance</b>                      | <b>\$ 1,068,032,344</b>  | <b>\$ 1,069,445,784</b>  |
| <b>Account Balance - Beginning September 1</b>              | <b>15,355,696,119</b>    | <b>14,286,250,335</b>    |
| <b>Account Balance - Ending August 31</b>                   | <b>\$ 16,423,728,463</b> | <b>\$ 15,355,696,119</b> |

## Comparative Statement of Changes in Account Balance

PENSION TRUST FUND

YEAR ENDED AUGUST 31 (With Comparative Totals for August 31, 2001)

SCHEDULE



| <b>STATE CONTRIBUTION ACCOUNT</b>  | <b>2002</b>                | <b>2001</b>                |
|--|----------------------------|----------------------------|
| <b>Additions:</b>  |                            |                            |
| State Contributions - General Revenue  | \$ 1,201,257,586           | \$ 1,142,792,114           |
| State Contributions - School Districts   | 106,196,643                | 95,182,401                 |
| State Contributions - Higher Education   | 51,584,889                 | 41,065,470                 |
| Reinstatement Fees   | 45,682,652                 | 34,761,307                 |
| Operating Transfers In:  |                            |                            |
| Transfer from Retired Reserve Account<br>Based on Actuarial Valuation as of<br>August 31                                 | 224,411,041                |                            |
| Allocation from Interest Account   | (1,332,164,480)            | (575,999,306)              |
| Transfer from Interest Account for<br>Net Depreciation in Fair Value<br>of Investments                                   | (8,477,880,514)            | (12,070,530,812)           |
| Retirement Benefits Forfeited While<br>Member Returned to Teaching   | 5,873,379                  | 7,521,024                  |
| Retirement Benefits Waived by Member   | 302,913                    | 358,256                    |
| <b>TOTAL ADDITIONS</b>   | <b>\$ (8,174,735,891)</b>  | <b>\$ (11,324,849,546)</b> |
| <b>Deductions:</b>   |                            |                            |
| Operating Transfers Out:   |                            |                            |
| Transfer to Retired Reserve Account Based<br>on Actuarial Valuation as of August 31                                      | \$                         | \$ 159,696,774             |
| Transfer to Retired Reserve Account<br>to Fund Benefits  | 3,077,578,614              | 2,490,774,970              |
| Transfer to Retired Reserve Account for<br>Retirement Increases per S.B. 273,<br>77th Legislature, Regular Session, 2001 |                            | 2,610,460,766              |
| <b>TOTAL DEDUCTIONS</b>  | <b>\$ 3,077,578,614</b>    | <b>\$ 5,260,932,510</b>    |
| <b>Net Decrease in Account Balance</b>   | <b>\$ (11,252,314,505)</b> | <b>\$ (16,585,782,056)</b> |
| <b>Account Balance - Beginning September 1</b>   | <b>27,489,238,274</b>      | <b>44,075,020,330</b>      |
| <b>Account Balance - Ending August 31</b>  | <b>\$ 16,236,923,769</b>   | <b>\$ 27,489,238,274</b>   |

## Comparative Statement of Changes in Account Balance

PENSION TRUST FUND

YEAR ENDED AUGUST 31 (With Comparative Totals for August 31, 2001)

SCHEDULE



| <b>RETIRED RESERVE ACCOUNT</b>  | <b>2002</b>              | <b>2001</b>              |
|---|--------------------------|--------------------------|
| <b>Additions:</b>   |                          |                          |
| Transfers from Employees Retirement System of Texas   | \$ 3,091,464             | \$ 2,068,339             |
| Operating Transfers In:   |                          |                          |
| Transfer from State Contribution Account Based on Actuarial Valuation as of August 31                                   |                          | 159,696,774              |
| Allocation from Interest Account  | 2,907,149,420            | 2,516,925,601            |
| Transfer from Member Savings Account for Dormant Accounts   | 5,130,631                | 9,193,732                |
| Transfer from Member Savings Account to Fund Benefits   | 1,047,094,782            | 832,300,538              |
| Transfer from State Contribution Account to Fund Benefits   | 3,077,578,614            | 2,490,774,970            |
| Transfer from State Contribution Account for Retirement Increases per S.B. 273, 77th Legislature, Regular Session, 2001 |                          | 2,610,460,766            |
| <b>TOTAL ADDITIONS</b>  | <b>\$ 7,040,044,911</b>  | <b>\$ 8,621,420,720</b>  |
| <b>Deductions:</b>  |                          |                          |
| Benefits Paid:  |                          |                          |
| Service Retirement Annuities  | \$ 3,591,219,348         | \$ 3,047,338,739         |
| Partial Lump Sums   | 386,442,648              | 280,942,321              |
| Disability Retirement Annuities   | 119,913,327              | 107,030,338              |
| Death and Survivor Benefits   |                          |                          |
| Accumulated Savings   | 1,504,798                | 908,801                  |
| Annual Salary   | 43,685,098               | 39,887,958               |
| Survivor Annuities  | 71,664,740               | 63,441,321               |
| Life Annuities  | 72,919,628               | 65,154,382               |
| 60 Monthly Payments   | 5,649,671                | 4,475,175                |
| Remainder of Contributions  | 2,558,781                | 2,651,578                |
| Transfers to Employees Retirement System of Texas   | 24,183,510               | 20,663,196               |
| Operating Transfers Out:  |                          |                          |
| Transfer to State Contribution Account Based on Actuarial Valuation as of August 31                                     | 224,411,041              |                          |
| Transfer to Deferred Retirement Option Account to Fund Benefits   | 29,473,781               | 99,035,352               |
| Retirement Benefits Forfeited While Member Returned to Teaching   | 5,873,379                | 7,521,024                |
| Retirement Benefits Waived by Member  | 302,913                  | 358,256                  |
| <b>TOTAL DEDUCTIONS</b>   | <b>\$ 4,579,802,663</b>  | <b>\$ 3,739,408,441</b>  |
| <b>Net Increase in Account Balance</b>  | <b>\$ 2,460,242,248</b>  | <b>\$ 4,882,012,279</b>  |
| <b>Account Balance - Beginning September 1</b>  | <b>36,253,497,091</b>    | <b>31,371,484,812</b>    |
| <b>Account Balance - Ending August 31</b>   | <b>\$ 38,713,739,339</b> | <b>\$ 36,253,497,091</b> |

## Comparative Statement of Changes in Account Balance

PENSION TRUST FUND

YEAR ENDED AUGUST 31 (With Comparative Totals for August 31, 2001)

SCHEDULE



### DEFERRED RETIREMENT OPTION ACCOUNT

|   | 2002                  | 2001                  |
|---|-----------------------|-----------------------|
| <b>Additions:</b>   |                       |                       |
| Operating Transfers In:                                   |                       |                       |
| Transfer from Retired Reserve Account<br>to Fund Benefits | \$ 29,473,781         | \$ 99,035,352         |
| Allocation from Interest Account                          | 9,820,586             | 11,554,766            |
| <b>TOTAL ADDITIONS</b>                                    | <b>\$ 39,294,367</b>  | <b>\$ 110,590,118</b> |
| <b>Deductions:</b>  |                       |                       |
| Benefits Paid   | \$ 48,697,687         | \$ 36,929,725         |
| <b>Net Increase (Decrease) in Account Balance</b>         | <b>\$ (9,403,320)</b> | <b>\$ 73,660,393</b>  |
| <b>Account Balance - Beginning September 1</b>            | <b>312,012,188</b>    | <b>238,351,795</b>    |
| <b>Account Balance - Ending August 31</b>                 | <b>\$ 302,608,868</b> | <b>\$ 312,012,188</b> |

## Comparative Statement of Changes in Account Balance

PENSION TRUST FUND

YEAR ENDED AUGUST 31 (With Comparative Totals for August 31, 2001)

SCHEDULE



| EXPENSE ACCOUNT                                | 2002                   | 2001                 |
|--|------------------------|----------------------|
| <b>Additions:</b>                              |                        |                      |
| Legislative Appropriations (Lapsed)            | \$                     | \$ (38,522)          |
| Miscellaneous Revenues                         | 491                    | 6,733                |
| Operating Transfers In:                        |                        |                      |
| Allocation from Interest Account               | 40,000,000             | 34,000,000           |
| <b>TOTAL ADDITIONS</b>                         | <b>\$ 40,000,491</b>   | <b>\$ 33,968,211</b> |
| <b>Deductions:</b>                             |                        |                      |
| Administrative Expenses:                       |                        |                      |
| Salaries and Other Personnel Services          | \$ 25,701,099          | \$ 22,287,757        |
| Employment Agency Workers                      | 47,522                 | 120,188              |
| Professional Services                          | 623,261                | 1,773,605            |
| Office Supplies                                | 78,634                 | 69,691               |
| Printing/Video Supplies and Services           | 476,212                | 314,258              |
| EDP Services                                   | 1,454,865              | 319,430              |
| Microfilm Supplies and Services                |                        | 2,452                |
| Postage and Mailing Services                   | 1,716,204              | 1,286,284            |
| Telephone                                      | 722,271                | 456,991              |
| Dues, Fees and Staff Development               | 219,681                | 244,747              |
| Office Equipment Maintenance and Repairs       | 242,554                | 298,483              |
| Travel   | 340,352                | 283,200              |
| Rentals  | 170,971                | 64,392               |
| Subscriptions and Reference Materials          | 134,445                | 178,637              |
| Miscellaneous                                  | 116,072                | 61,709               |
| Investments Custody and Clearing               |                        | 10,000               |
| Software Purchases, Rental and Maintenance     | 1,512,580              | 1,480,293            |
| Fiduciary Liability and Employee Surety Bond   | 2,361                  | 742,259              |
| Other Operating Expenses - Plant               | 797,196                | 786,302              |
| Compensable Absences                           | 367,737                | 305,798              |
| Depreciation                                   | 1,809,221              | 1,828,254            |
| Nonbudgeted Expenses                           | 502,478                | 216,592              |
| <b>TOTAL DEDUCTIONS</b>                        | <b>\$ 37,035,716 *</b> | <b>\$ 33,131,322</b> |
| <b>Net Increase in Account Balance</b>         | <b>\$ 2,964,775</b>    | <b>\$ 836,889</b>    |
| <b>Account Balance - Beginning September 1</b> | <b>\$ 16,887,826</b>   | <b>\$ 16,050,937</b> |
| <b>Restatements</b>                            |                        | <b>(1,050,679)</b>   |
| <b>Beginning September 1, As Restated</b>      | <b>\$ 15,837,147</b>   | <b>\$ 16,050,937</b> |
| <b>Account Balance - Ending August 31</b>      | <b>\$ 18,801,922</b>   | <b>\$ 16,887,826</b> |

\* This amount includes investing activity expenses of \$12,921,671 (Schedule 4). Administrative expenses net of investing activity expenses are \$24,597,361 (Exhibit II).



## Schedule of Administrative Expenses and Capital Outlay - Budget and Actual on Budgetary Basis

AUGUST 31, 2002

SCHEDULE



PENSION TRUST FUND

|   | Budget               | Actual              | Variance - Favorable (Unfavorable) |
|---|----------------------|---------------------|------------------------------------|
| <b>Expenses:</b>                                |                      |                     |                                    |
| Salaries  | \$ 20,834,283        | \$ 20,755,498       | \$ 78,785                          |
| Other Personnel Services:                       |                      |                     |                                    |
| Employment Agency Workers                       | \$ 90,300            | \$ 47,422           | \$ 42,878                          |
| Employer Retirement Contributions               | 1,241,551            | 1,229,517           | 12,034                             |
| Group Health and Life Insurance                 | 2,219,769            | 2,215,818           | 3,951                              |
| Other Employee Benefits                         | 40,000               | 35,524              | 4,476                              |
| FICA Taxes                                      | 1,490,472            | 1,464,742           | 25,730                             |
| Compensable Absences                            | 375,000              | 367,737             | 7,263                              |
| <b>TOTAL OTHER PERSONNEL SERVICES</b>           | <b>\$ 5,457,092</b>  | <b>\$ 5,360,760</b> | <b>\$ 96,332</b>                   |
| Professional Services                           | \$ 1,879,897         | \$ 848,061          | \$ 1,031,836                       |
| Other Operating Expenses - General:             |                      |                     |                                    |
| Office Supplies                                 | \$ 89,100            | \$ 82,689           | \$ 6,411                           |
| Printing Supplies and Services                  | 564,316              | 498,065             | 66,251                             |
| EDP Services                                    | 1,733,468            | 1,452,865           | 280,603                            |
| Postage   | 1,670,075            | 1,553,143           | 116,932                            |
| Telephone                                       | 813,700              | 722,271             | 91,429                             |
| Mailing Services                                | 180,954              | 151,795             | 29,159                             |
| Dues, Fees and Staff Development                | 332,028              | 219,936             | 112,092                            |
| Office Equipment Maintenance and Repairs        | 505,768              | 234,340             | 271,428                            |
| Travel  | 446,550              | 340,352             | 106,198                            |
| Rentals   | 273,400              | 170,971             | 102,429                            |
| Subscriptions and Reference Materials           | 244,720              | 133,296             | 111,424                            |
| Miscellaneous                                   | 177,255              | 114,070             | 63,185                             |
| Software Purchases, Rental and Maintenance      | 2,003,009            | 1,500,659           | 502,350                            |
| Fiduciary Liability and Employee Surety Bond    | 2,500                | 2,361               | 139                                |
| Depreciation                                    | 2,625,000            | 1,812,179           | 812,821                            |
| Equipment Purchases                             |                      |                     |                                    |
| <b>TOTAL OTHER OPERATING EXPENSES - GENERAL</b> | <b>\$ 11,661,843</b> | <b>\$ 8,988,992</b> | <b>\$ 2,672,851</b>                |



| HEALTH INSURANCE TRUST FUNDS |              |  |
|------------------------------|--------------|--|
| RETIRED PLAN                 |              |  |
| Budget                       | Actual       | Variance -<br>Favorable<br>(Unfavorable) |
| \$ 600,815                   | \$ 597,374   | \$ 3,441                                 |
| \$ 36,829                    | \$ 35,842    | \$ 987                                   |
| 56,322                       | 56,009       | 313                                      |
| 45,251                       | 44,232       | 1,019                                    |
| \$ 138,402                   | \$ 136,083   | \$ 2,319                                 |
| \$ 1,167,000                 | \$ 1,149,947 | \$ 17,053                                |
| \$ 1,200                     | \$ 842       | \$ 358                                   |
| 263,800                      | 212,563      | 51,237                                   |
| 15,000                       | 12,900       | 2,100                                    |
| 271,000                      | 183,511      | 87,489                                   |
| 11,200                       | 8,219        | 2,981                                    |
| 81,700                       | 39,629       | 42,071                                   |
| 5,650                        | 3,897        | 1,753                                    |
| 1,200                        | 701          | 499                                      |
| 7,750                        | 5,088        | 2,662                                    |
| 46,267                       | 46,017       | 250                                      |
| 1,500                        | 559          | 941                                      |
| 1,200                        | 1,031        | 169                                      |
| 2,928                        | 562          | 2,366                                    |
| \$ 710,395                   | \$ 515,519   | \$ 194,876                               |

(to next page)

## Schedule of Administrative Expenses and Capital Outlay - Budget and Actual on Budgetary Basis

AUGUST 31, 2002

SCHEDULE



PENSION TRUST FUND

|   | Budget               | Actual               | Variance - Favorable (Unfavorable) |
|---|----------------------|----------------------|------------------------------------|
| <b>Other Operating Expenses - Plant:</b>                                  |                      |                      |                                    |
| Building Maintenance and Services   | \$ 357,259           | \$ 262,636           | \$ 94,623                          |
| Custodial Services and Supplies   | 199,668              | 153,867              | 45,801                             |
| Insurance   | 53,000               | 50,209               | 2,791                              |
| Utilities   | 460,000              | 321,245              | 138,755                            |
| <b>TOTAL OTHER OPERATING EXPENSES - PLANT</b>                             | <b>\$ 1,069,927</b>  | <b>\$ 787,957</b>    | <b>\$ 281,970</b>                  |
| <b>TOTAL OTHER OPERATING EXPENSES</b>                                     | <b>\$ 12,731,770</b> | <b>\$ 9,776,949</b>  | <b>\$ 2,954,821</b>                |
| <b>Nonbudgeted Expenses:</b>  |                      |                      |                                    |
| Statewide Cost Allocation   | \$                   | \$ 159,221           | \$ (159,221)                       |
| Loss on Disposal of Fixed Assets  |                      | 16,814               | (16,814)                           |
| Depreciation  |                      |                      |                                    |
| Compensable Absences  |                      |                      |                                    |
| <b>TOTAL NONBUDGETED EXPENSES</b>   | <b>\$</b>            | <b>\$ 176,035</b>    | <b>\$ (176,035)</b>                |
| <b>TOTAL ADMINISTRATIVE EXPENSES</b>                                      | <b>\$ 40,903,042</b> | <b>\$ 36,917,303</b> | <b>\$ 3,985,739</b>                |
| <b>Expenses</b>   |                      |                      |                                    |
| <b>Pension Trust Fund:</b>  |                      |                      |                                    |
| Total From Expense Account - Schedule 1                                   |                      | \$ 37,035,716        |                                    |
| Add (Less) Differences Between GAAP and Budgetary Basis Payables:         |                      |                      |                                    |
| Professional Services   |                      | 224,800              |                                    |
| Other Personnel Services  |                      | (100)                |                                    |
| Other Operating Expenses - General  |                      | (10,389)             |                                    |
| Other Operating Expenses - Plant  |                      | (9,239)              |                                    |
| Add Depreciation on Leased Office Space                                   |                      | 2,958                |                                    |
| Add Gain on Reclass of Fixed Assets                                       |                      | 483,316              |                                    |
| Less Equipment Purchases Expensed in Current Year                         |                      | (809,759)            |                                    |
| <b>TOTAL ADMINISTRATIVE EXPENSES PER ABOVE - BUDGETARY BASIS SCHEDULE</b> |                      | <b>\$ 36,917,303</b> |                                    |
| <b>Capital Outlay:</b>  |                      |                      |                                    |
| Equipment Purchases   | \$ 437,050           | \$ 333,268           | \$ 103,782                         |
| Building Improvements   | 5,000                | (320)                | 5,320                              |
| Capital Projects  | 3,020,700            | 1,078,701            | 1,941,999                          |
| <b>TOTAL CAPITAL OUTLAY</b>   | <b>\$ 3,462,750</b>  | <b>\$ 1,411,649</b>  | <b>\$ 2,051,101</b>                |

| HEALTH INSURANCE TRUST FUNDS |              |                                    |
|------------------------------|--------------|------------------------------------|
| RETIRED PLAN                 |              |                                    |
| Budget                       | Actual       | Variance - Favorable (Unfavorable) |
| \$                           | \$           | \$                                 |
| \$ -0-                       | \$ -0-       | \$ -0-                             |
| \$ 710,395                   | \$ 515,519   | \$ 194,876                         |
| \$                           | \$           | \$                                 |
|                              | 94           | (94)                               |
|                              | 7,446        | (7,446)                            |
| \$                           | \$ 7,540     | \$ (7,540)                         |
| \$ 2,616,612                 | \$ 2,406,463 | \$ 210,149                         |

|   | <u>Expenses</u>     |
|---|---------------------|
| <b>Health Insurance Trust Fund - Retired Plan</b>                         |                     |
| Total Administrative Expenses - Exhibit B                                 | \$ 2,163,441        |
| Add Differences Between GAAP and Budgetary Basis Payables:                |                     |
| Professional Services   | 226,829             |
| Other Operating Expenses - General  | <u>16,193</u>       |
| <b>TOTAL ADMINISTRATIVE EXPENSES PER ABOVE - BUDGETARY BASIS SCHEDULE</b> | <b>\$ 2,406,463</b> |

(to next page)

## Schedule of Administrative Expenses and Capital Outlay - Budget and Actual on Budgetary Basis

AUGUST 31, 2002

SCHEDULE



|   | HEALTH INSURANCE TRUST FUNDS |                   |                                    |
|---|------------------------------|-------------------|------------------------------------|
|   | ACTIVE PLAN                  |                   |                                    |
|   | Budget                       | Actual            | Variance - Favorable (Unfavorable) |
| <b>Expenses:</b>                                |                              |                   |                                    |
| Salaries  | \$ 531,489                   | \$ 403,808        | \$ 127,681                         |
| Other Personnel Services:                       |                              |                   |                                    |
| Employment Agency Workers                       | \$ 12,000                    | \$ 3,417          | \$ 8,583                           |
| Employer Retirement Contributions               | 41,755                       | 23,843            | 17,912                             |
| Group Health and Life Insurance                 | 53,986                       | 33,340            | 20,646                             |
| Other Employee Benefits                         |                              |                   |                                    |
| FICA Taxes                                      | 57,848                       | 29,723            | 28,125                             |
| Compensable Absences                            |                              |                   |                                    |
| <b>TOTAL OTHER PERSONNEL SERVICES</b>           | <b>\$ 165,589</b>            | <b>\$ 90,323</b>  | <b>\$ 75,266</b>                   |
| Professional Services                           | \$ 2,671,492                 | \$ 2,106,800      | \$ 564,692                         |
| Other Operating Expenses - General:             |                              |                   |                                    |
| Office Supplies                                 | \$ 22,973                    | \$ 3,245          | \$ 19,728                          |
| Printing Supplies and Services                  | 56,875                       | 5,730             | 51,145                             |
| EDP Services                                    | 38,000                       | 4,300             | 33,700                             |
| Postage   | 74,366                       | 14,864            | 59,502                             |
| Telephone                                       | 3,910                        | 2,064             | 1,846                              |
| Mailing Services                                | 5,220                        | 1,256             | 3,964                              |
| Dues, Fees and Staff Development                | 1,525                        | 1,075             | 450                                |
| Office Equipment Maintenance and Repairs        | 12,000                       | 155               | 11,845                             |
| Travel  | 36,000                       | 6,863             | 29,137                             |
| Rentals   | 35,877                       | 32,672            | 3,205                              |
| Subscriptions and Reference Materials           | 1,210                        | 90                | 1,120                              |
| Miscellaneous                                   | 5,526                        | 16                | 5,510                              |
| Software Purchases, Rental and Maintenance      |                              |                   |                                    |
| Fiduciary Liability and Employee Surety Bond    |                              |                   |                                    |
| Depreciation                                    |                              |                   |                                    |
| Equipment Purchases                             | 66,116                       | 61,109            | 5,007                              |
| <b>TOTAL OTHER OPERATING EXPENSES - GENERAL</b> | <b>\$ 359,598</b>            | <b>\$ 133,439</b> | <b>\$ 226,159</b>                  |

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403(b) ADMINISTRATIVE TRUST FUND

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403(b) CERTIFICATION PROGRAM

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| Budget    | Actual    | Variance -<br>Favorable<br>(Unfavorable) |
|-----------|-----------|--|
| \$ 71,441 | \$ 69,611 | \$ 1,830                                 |
| \$ 4,274  | \$ 3,953  | \$ 321                                   |
| 3,234     | 3,234     |  |
| 5,300     | 5,200     | 100                                      |
| \$ 12,808 | \$ 12,387 | \$ 421                                   |
| \$ 65,751 | \$ 52,000 | \$ 13,751                                |
| \$        | \$        | \$                                       |

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\$ -0-      \$ -0-      \$ -0-

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(to next page)

## Schedule of Administrative Expenses and Capital Outlay - Budget and Actual on Budgetary Basis

AUGUST 31, 2002

(concluded)

SCHEDULE



|   | HEALTH INSURANCE TRUST FUNDS |                 |                                    |
|---|------------------------------|-----------------|------------------------------------|
|   | ACTIVE PLAN                  |                 |                                    |
|   | Budget                       | Actual          | Variance - Favorable (Unfavorable) |
| Other Operating Expenses - Plant:   |                              |                 |                                    |
| Building Maintenance and Services   | \$                           | \$              | \$                                 |
| Custodial Services and Supplies   |                              |                 |                                    |
| Insurance   |                              |                 |                                    |
| Utilities   |                              |                 |                                    |
| <b>TOTAL OTHER OPERATING EXPENSES - PLANT</b>                             | \$ -0-                       | \$ -0-          | \$ -0-                             |
| <b>TOTAL OTHER OPERATING EXPENSES</b>                                     | \$ 359,598                   | \$ 133,439      | \$ 226,159                         |
| Nonbudgeted Expenses:   |                              |                 |                                    |
| Statewide Cost Allocation   | \$                           | \$              | \$                                 |
| Loss on Disposal of Fixed Assets  |                              |                 |                                    |
| Depreciation  |                              |                 |                                    |
| Compensable Absences  |                              | 13,930          | (13,930)                           |
| <b>TOTAL NONBUDGETED EXPENSES</b>   | \$                           | \$ 13,930       | \$ (13,930)                        |
| <b>TOTAL ADMINISTRATIVE EXPENSES</b>                                      | \$ 3,728,168                 | \$ 2,748,300    | \$ 979,868                         |
|   |                              | <b>Expenses</b> |                                    |
| <b>Health Insurance Trust Fund - Active Plan</b>                          |                              |                 |                                    |
| Total Administrative Expenses - Exhibit B                                 |                              | \$ 2,750,107    |                                    |
| Less Differences Between GAAP and Budgetary Basis Payables:               |                              |                 |                                    |
| Professional Services   |                              |                 |                                    |
| Other Operating Expenses - General  |                              | (1,807)         |                                    |
| <b>TOTAL ADMINISTRATIVE EXPENSES PER ABOVE - BUDGETARY BASIS SCHEDULE</b> |                              | \$ 2,748,300    |                                    |

| 403(b) ADMINISTRATIVE TRUST FUND |            |                                    |
|----------------------------------|------------|------------------------------------|
| 403(b) CERTIFICATION PROGRAM     |            |                                    |
| Budget                           | Actual     | Variance - Favorable (Unfavorable) |
| \$                               | \$         | \$                                 |
| \$ -0-                           | \$ -0-     | \$ -0-                             |
| \$ -0-                           | \$ -0-     | \$ -0-                             |
| \$                               | \$         | \$                                 |
|                                  | 1,600      | (1,600)                            |
| \$                               | \$ 1,600   | \$ (1,600)                         |
| \$ 150,000                       | \$ 135,598 | \$ 14,402                          |

|   | Expenses          |
|---|-------------------|
| <b>403(b) Certification Program</b>                                       |                   |
| Total Administrative Expenses - Exhibit B                                 | \$ 124,118        |
| Add Differences Between GAAP and Budgetary Basis Payables:                |                   |
| Other Operating Expenses - General  | 11,480            |
| <b>TOTAL ADMINISTRATIVE EXPENSES PER ABOVE - BUDGETARY BASIS SCHEDULE</b> | <b>\$ 135,598</b> |

## Comparative Schedule of Investment Portfolio

### PENSION TRUST FUND

SCHEDULE

3

|   | TOTAL                     | SHORT-<br>TERM          |
|---|---------------------------|-------------------------|
| <i>YEAR ENDED AUGUST 31, 2002</i>             |                           |                         |
| Purchases                                     | \$ 75,688,117,650         | \$ 3,803,572,305        |
| Sales   | (71,266,581,089)          | (173,945,895)           |
| Calls and Maturities                          | (3,833,605,182)           | (3,825,767,000)         |
| Net Appreciation (Depreciation) in Fair Value | (8,477,880,514)           | (1,497)                 |
| <b>Net Increase (Decrease)</b>                | <b>\$ (7,889,949,135)</b> | <b>\$ (196,142,087)</b> |
| <b>Fair Value - September 1, 2001</b>         | <b>78,731,130,923</b>     | <b>351,308,482</b>      |
| <b>Fair Value - August 31, 2002 (Exh. I)</b>  | <b>\$ 70,841,181,788</b>  | <b>\$ 155,166,395</b>   |
| <i>YEAR ENDED AUGUST 31, 2001</i>             |                           |                         |
| Purchases                                     | \$ 61,788,380,613         | \$ 17,529,903,842       |
| Sales   | (40,562,279,894)          | (186,342,223)           |
| Calls and Maturities                          | (18,478,421,772)          | (17,195,120,000)        |
| Net Appreciation (Depreciation) in Fair Value | (12,070,530,812)          | (1,240,869)             |
| <b>Net Increase (Decrease)</b>                | <b>\$ (9,322,851,865)</b> | <b>\$ 147,200,750</b>   |
| <b>Fair Value - September 1, 2000</b>         | <b>88,053,982,788</b>     | <b>204,107,732</b>      |
| <b>Fair Value - August 31, 2001</b>           | <b>\$ 78,731,130,923</b>  | <b>\$ 351,308,482</b>   |

## Comparative Schedule of Investing Activity Expenses

### PENSION TRUST FUND - YEAR ENDED AUGUST 31

SCHEDULE

4

|   | 2002                 | 2001                 |
|---|----------------------|----------------------|
| <b>Direct Expenses:</b>                             |                      |                      |
| Salaries and Benefits                               | \$ 7,333,988         | \$ 6,080,823         |
| Temporary Employment Services                       | 16,181               | 13,089               |
| Professional Services                               | 1,115,340            | 1,342,559            |
| Office Supplies                                     | 7,676                | 12,351               |
| Mailing Services                                    | 163                  | 292                  |
| Dues, Fees and Staff Development                    | 29,394               | 40,473               |
| Office Equipment Maintenance and Repairs            | 1,743                | 1,740                |
| Travel  | 177,146              | 129,516              |
| Subscriptions and Reference Materials               | 30,827               | 95,460               |
| Investments Custody and Clearing                    |                      | 10,000               |
| Equipment Purchases                                 | 50,432               | 6,773                |
| <b>Total Direct Expenses</b>                        | <b>\$ 8,762,890</b>  | <b>\$ 7,733,076</b>  |
| <b>Indirect Expenses:</b>                           |                      |                      |
| Depreciation, Utilities and Building Maintenance    | \$ 462,493           | \$ 570,640           |
| Legal, Audit and Human Resources Support            | 1,135,363            | 992,207              |
| Information Technology Support                      | 1,045,111            | 841,810              |
| Fiscal Management Support                           | 753,702              | 1,087,254            |
| Security and Staff Services Support                 | 339,275              | 315,207              |
| Executive Management Support                        | 348,066              | 279,925              |
| Other Support Services                              | 74,771               | 32,758               |
| <b>Total Indirect Expenses</b>                      | <b>\$ 4,158,781</b>  | <b>\$ 4,119,801</b>  |
| <b>Total Investing Activity Expenses* (Exh. II)</b> | <b>\$ 12,921,671</b> | <b>\$ 11,852,877</b> |

\*During fiscal year 2002, the system paid commissions of \$36,963,902, of which \$6,515,203 was paid to soft dollars brokers. Soft dollars from commissions were used to acquire on-line data services, professional services and other research services totaling \$5,530,978. These soft dollar expenditures are not included in the above investing activity expenses.



| EQUITY<br>SECURITIES                                      | FIXED<br>INCOME   | ALTERNATIVE<br>INVESTMENTS                       | REAL ESTATE<br>HELD FOR<br>SALE             |
|---|---|--|---|
| \$ 14,901,186,950<br>(9,220,938,355)<br>(8,688,497,655)   | \$ 56,422,305,303<br>(61,602,581,510)<br>(7,838,182)<br>313,736,892       | \$ 560,934,449<br>(269,115,329)<br>(102,673,611) | \$ 118,643<br><br>(444,643)                 |
| \$ (3,008,249,060)<br>50,166,933,864                      | \$ (4,874,377,497)<br>26,811,290,348                                      | \$ 189,145,509<br>1,395,972,229                  | \$ (326,000)<br>5,626,000                   |
| <b>\$ 47,158,684,804</b>                                  | <b>\$ 21,936,912,851</b>  | <b>\$ 1,585,117,738</b>                          | <b>\$ 5,300,000</b>                         |
| \$ 21,845,566,770<br>(15,638,120,226)<br>(13,820,089,356) | \$ 21,489,723,308<br>(24,600,603,060)<br>(1,283,301,772)<br>1,764,822,893 | \$ 918,269,217<br>(105,597,604)<br>(11,334,095)  | \$ 4,917,476<br>(31,616,781)<br>(2,689,385) |
| \$ (7,612,642,812)<br>57,779,576,676                      | \$ (2,629,358,631)<br>29,440,648,979                                      | \$ 801,337,518<br>594,634,711                    | \$ (29,388,690)<br>35,014,690               |
| <b>\$ 50,166,933,864</b>                                  | <b>\$ 26,811,290,348</b>  | <b>\$ 1,395,972,229</b>                          | <b>\$ 5,626,000</b>                         |

## Schedule of Payments to Consultants - Budgetary Basis

FIDUCIARY FUND TYPES - YEAR ENDED AUGUST 31, 2002

SCHEDULE



|                               | Health Insurance and Other Benefits Trust Funds |                    |                    |                              | Total              |
|-------------------------------|---|--------------------|--------------------|------------------------------|--------------------|
|                               | Pension Trust Fund                              | Retired Plan       | Active Plan        | 403(b) Certification Program |                    |
| <b>Nature of Service:</b>     |   |                    |                    |                              |                    |
| Health Care Consultant        | \$  | \$ 455,790         | \$ 974,790         | \$                           | \$1,430,580        |
| Legal Counsel                 | 138,296   | 339,000            | 458,000            |                              | 935,296            |
| Investment Advisors           | 672,833   |                    |                    | 52,000                       | 724,833            |
| TRS-ActiveCare Implementation |   |                    | 444,000            |                              | 444,000            |
| Medical Board                 | 100,803   |                    |                    |                              | 100,803            |
| Investment Audit              | 92,500  |                    |                    |                              | 92,500             |
| Financial Audit Services      | 79,900  | 9,990              | 510                |                              | 90,400             |
| Computer/Technical            |   |                    | 73,000             |                              | 73,000             |
| Consulting Actuary            | 68,208  |                    |                    |                              | 68,208             |
| Fiduciary Counsel             | 61,247  |                    |                    |                              | 61,247             |
| Actuarial Audit               | 58,000  |                    |                    |                              | 58,000             |
| TRS-Care Credentialing        |   | 45,167             |                    |                              | 45,167             |
| Miscellaneous                 | 22,444  |                    |                    |                              | 22,444             |
| Audit Training Services       | 10,330  |                    |                    |                              | 10,330             |
| Administrative Services       | (456,500)                                       | 300,000            | 156,500            |                              |                    |
| <b>TOTAL</b>                  | <b>\$ 848,061</b>                               | <b>\$1,149,947</b> | <b>\$2,106,800</b> | <b>\$ 52,000</b>             | <b>\$4,156,808</b> |

# Investment Section

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TEACHER RETIREMENT SYSTEM OF TEXAS

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## INVESTMENT OVERVIEW

### Authority and Mission

The TRS Board of Trustees holds system assets in trust and oversees the investment of the system's funds in accordance with applicable constitutional and statutory provisions. The Investment Division follows a clear philosophy and a well-defined style and process to achieve desired long-term investment returns while controlling risk and managing costs.

### Policy and Portfolio Structure

The board governs the investment process by adopting investment policies and objectives and monitoring performance. The TRS Investment Policy Statement, adopted by the board and amended as needed, has specific guidelines for performance expectation, eligible holdings and portfolio characteristics. Further, the board relies on the advice of external advisors to assist in establishing investment objectives and in reviewing performance and compliance with investment policy.

The guiding principle for investment strategy is risk control through diversification, prudently setting and modestly deviating from normal positions to enhance returns. The key to determining investment direction is asset allocation, a crucial decision made by the board after consideration of expected returns for asset classes in the context of risk tolerance for the fund. TRS investment staff manages the investment portfolios based on this allocation. An asset/liability study is performed by an external actuarial advisor every five years and presented to the board with recommendations for adoption. TRS staff and external advisors assist the board in setting investment objectives given the adopted asset allocation, monitoring compliance with investment policy and monitoring performance. Risk is diversified at both the asset class and security level. The major asset classes, equity and fixed income, each are segmented with sub-asset classes that are further diversified with very broad security selection. The alternative asset classes of private equity and strategically traded securities have been added to provide an additional degree of risk reduction and return enhancement.

TRS uses both passive and active investing styles. This approach enables the system to effectively manage the size of the trust in a manner that both tracks the performance of key benchmarks and provides opportunity to add value through active portfolios.

TRS's equity portfolio matches closely the characteristics of its composite benchmark, while seeking returns exceeding those of the index through securi-

ties analysis. The style thus has risk control similar to passive or index management, but allows for generation of excess return associated with active management. It is a disciplined, balanced approach with a strong quantitative foundation that focuses on long-term returns and objectives rather than on short-term market movements. The process to implement this style includes frequent updating of statistical risk and return models constructed by TRS investment staff that incorporates economic conditions, interest rate changes and industry factors. The equity portfolios, which normally comprise more than 60 percent of the total fund, seek to add value through security selection that emphasizes attractive industries.

The fixed income portfolio is managed similarly in that staff replicates the dominant factors that drive benchmark returns in order to control risk, while deriving excess returns from careful security and sector selection.

### Economic Conditions and Outlook

The U.S. economy and equity market deteriorated at an accelerating rate towards the end of the 2001 fiscal year, primarily as a result of the ongoing hangover from the deflating stock market bubble of the late 1990s. The terrorist attacks of September 11 exacerbated the decline, virtually halting the world's economic activity during the month. The Federal Reserve aggressively cut interest rates helping to provide liquidity and confidence to the markets. Nevertheless, stock market investors continued to experience enormous stock market volatility. Confidence in corporate America weakened still further as major accounting scandals emerged, first at energy giant Enron, and later at numerous other major corporations. The broad equity market and the economy attempted to recover as the Fed cuts took hold. In the summer months of 2002, however, the weight of corporate scandals, a string of major bankruptcies, and a lack of general visibility of earnings growth caused a capitulating downturn in the worldwide equity markets.

From the peak of the market in March 2000 to the near term trough in July 2002, the S&P 500 experienced a price decline of just over 50%. This broad stock market measure recovered somewhat late in the fiscal year but still was down 19.2% during FY2002. Notably the technology-heavy Nasdaq market declined 27.2% during the year, but has experienced a peak to trough decline of over 75%. Stock market valuations have begun to appear reasonable on several measures and particularly relative to bonds. However, corporate governance reforms,

## INVESTMENT OVERVIEW

deflation and constrained economic growth will likely moderate the potential for a meaningful rebound in earnings. Increased confidence in improving corporate profitability, as reported, will be required for a sustained recovery in equity prices.

The decline in international equity markets was not quite as acute as these were buffered by strengthening currencies relative to the dollar and a resurgence in emerging markets. Still, non-US equities experienced a fall of 14.8% during the fiscal year. Valuations in international markets have become very attractive but many risks remain. Deepening deficits, high oil prices and the possibility of war have kept a lid on many overseas markets that are less able to withstand these pressures. As these risks abate, foreign markets should perform better.

Fixed Income markets, but more specifically U.S. Treasuries were the only real safe haven during the year. The broad bond market as measured by the Salomon Large Pension Fund Index rose 8.5%, but the U.S. treasury component experienced a total return of 10.9%. Due in large part to fraud-induced bankruptcies, the corporate bond component rose only 4.8% despite the higher yields offered in the segment.

Alternative or non-traditional assets experienced mixed but generally positive results during the year providing the diversification aspect desired by investors. Strategically traded securities, or hedge funds, performed as expected in the highly volatile capital markets, returning 2.2% during the year as measured by CS/Tremont Hedge Fund Index. Private equity funds experienced further retrenchment and buyout funds remained active while the real estate market remained healthy. If the equity market continues to swoon or fails to achieve its historic annual rates of return, institutional investors may seek alternatives out of necessity of both added return and risk reduction.

Weak economic data in the summer of 2002 began to cast doubt upon the sustainability of the ongoing economic recovery. Market participants began to speculate that a further round of aggressive Fed easing would be necessary to forestall a Japanese-style deflationary spiral and economic malaise. By the end of the fiscal year, capital markets rallied in anticipation of the Fed move and the resultant boost in economic activity. Nevertheless, uncertainty remained high about the viability of the recovery and the sustainability of corporate earnings growth. In any event, the near-term outlook for global equities may remain clouded with returns expected to be in line with very modest growth in earnings. After a

solid run in the fixed income markets, bond returns are unlikely to repeat those seen in the prior year. Bond income returns are expected to be in line with the yields unless economic growth is surprisingly strong. The overall outlook for capital market returns is therefore expected to be moderately favorable, but with higher than normal volatility.

### Investment Portfolio Performance

The total value of the fund on August 31, 2002 was \$71.3 billion. The fund's annual rates of return for the one-, three-, five- and 10-year periods ending August 31, 2002 were -7.81%, -2.07%, 4.20% and 8.82% respectively. The fund's \$7.4 billion decline in value over the last year is explained primarily by the broad based deterioration in global equity markets.

As a result of the board's asset allocation modifications made in June 2000, several asset classes and sub-asset classes became more fully implemented in the fiscal year. The allocations to these assets were made with the expectation of generating somewhat higher risk-adjusted returns. Each of the fully implemented asset classes, including small and mid-capitalization stocks, emerging market equities, high-yield debt and strategically traded securities, added relative value and improved upon the risk-adjusted returns of the previous normal portfolio. The one asset class not yet fully implemented, private equity, proceeded with its very long funding period and is not expected to contribute meaningfully for several years.

Additional information about performance is included on the "Total Time Weighted Returns and Asset Allocation" chart on page 67. This information is for the time period through the second quarter of the calendar year ended June 30, 2002, and includes comparisons with established benchmarks for the same time period.

Investment performance is calculated using a time-weighted rate of return based on the market rate of return in accordance with the Association for Investment Management and Research Performance Presentation Standards.

## Total Time Weighted Returns and Asset Allocation

PENSION TRUST FUND - FOR PERIODS ENDED JUNE 30

|  | 1997  | 1998  | 1999  | 2000  | 2001   | 2002   | 3<br>Years | 5<br>Years | 10<br>Years |
|--|-------|-------|-------|-------|--------|--------|------------|------------|-------------|
| <b>Total Portfolio</b>                         |       |       |       |       |        |        |            |            |             |
| TRS  | 21.1% | 21.3% | 12.1% | 7.9%  | -5.0%  | -6.4%  | -1.4%      | 5.5%       | 9.6%        |
| Custom Index <sup>1</sup>                      | 21.1% | 20.3% | 12.2% | 7.8%  | -5.4%  | -6.6%  | -1.6%      | 5.3%       | 9.2%        |
| <b>Equities</b>                                |       |       |       |       |        |        |            |            |             |
| TRS  | 28.7% | 25.8% | 18.2% | 9.9%  | -13.1% | -13.3% | -6.1%      | 4.3%       | 11.1%       |
| Equity Composite Index <sup>2</sup>            | 29.8% | 25.0% | 19.4% | 10.0% | -13.2% | -13.8% | -6.3%      | 4.1%       | 11.0%       |
| <b>Fixed Income</b>                            |       |       |       |       |        |        |            |            |             |
| TRS  | 9.3%  | 14.9% | 1.2%  | 4.0%  | 11.9%  | 8.7%   | 8.1%       | 8.0%       | 8.1%        |
| Debt Securities Composite Index <sup>3</sup>   | 9.1%  | 13.8% | 1.3%  | 4.2%  | 11.4%  | 8.3%   | 7.9%       | 7.7%       | 7.8%        |
| <b>Alternative Assets</b>                      |       |       |       |       |        |        |            |            |             |
| TRS  | n/a   | n/a   | n/a   | n/a   | 9.1%   | -2.6%  | n/a        | n/a        | n/a         |
| Alternative Asset Composite Index <sup>4</sup> | n/a   | n/a   | n/a   | n/a   | 10.2%  | 0.0%   | n/a        | n/a        | n/a         |
| <b>Asset Allocation (Average)</b>              |       |       |       |       |        |        |            |            |             |
| Equities                                       | 64.2% | 63.3% | 65.1% | 64.5% | 64.4%  | 64.3%  | 64.5%      | 64.3%      | 59.5%       |
| Fixed Income                                   | 31.6% | 33.3% | 32.6% | 34.0% | 30.5%  | 30.4%  | 31.6%      | 32.2%      | 35.6%       |
| Alternative Assets                             | 2.1%  | 1.3%  | 1.0%  | 0.7%  | 4.5%   | 4.5%   | 3.2%       | 2.4%       | 3.4%        |
| Short-Term                                     | 2.1%  | 2.1%  | 1.3%  | 0.8%  | 0.6%   | 0.8%   | 0.7%       | 1.1%       | 1.5%        |

<sup>1</sup> The Custom Index is based upon the long-term normal policy investment allocation, currently 42% S&P 500, 7.5% S&P 400, 3% S&P 600, 13% MS ACWI Free Ex-US, 28.5% SB Large Pension Fund, 1% SB High Yield Market Index, 3% Zero, 1.5% 6 Month T-Bill + 300 bps and 0.5% 3 month T-Bill.

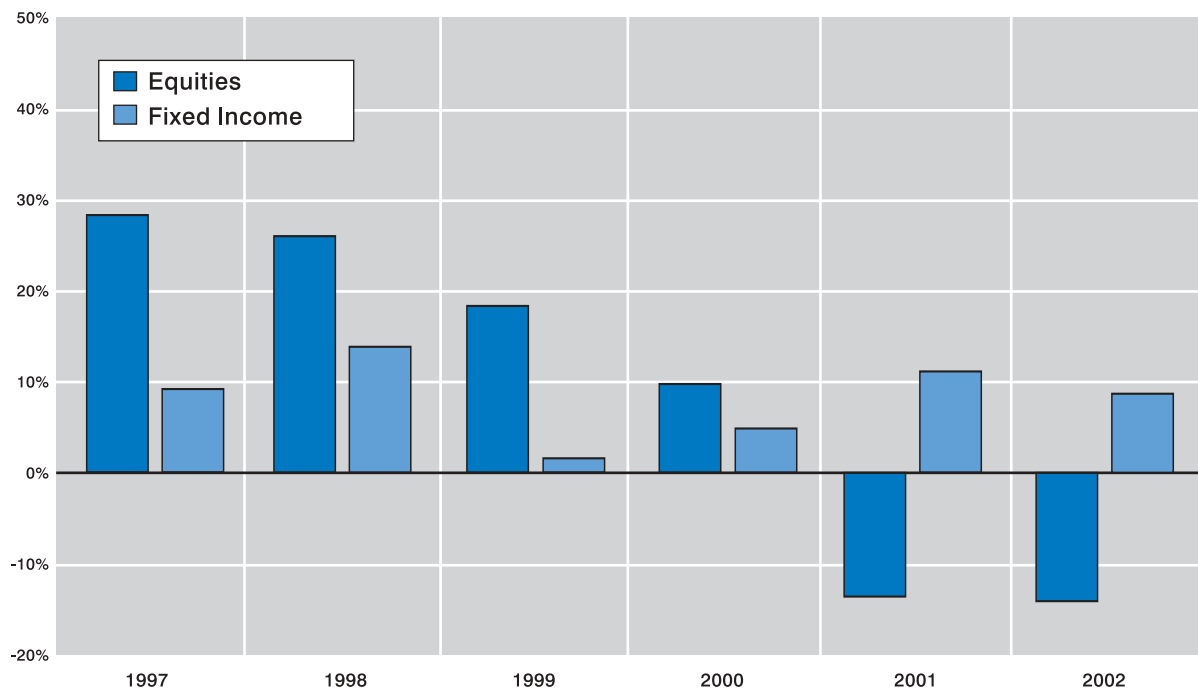
<sup>2</sup> The Equity Composite Index is based upon the long-term normal policy investment allocation, currently 64.1% S&P 500, 11.5% S&P 400, 4.6% S&P 600, and 19.8% MS ACWI Free Ex-US.

<sup>3</sup> The Debt Securities Composite Index is based upon the long-term normal policy investment allocation, currently 96.6% SB Large Pension Fund, and 3.4% SB High Yield Market Index.

<sup>4</sup> The Alternative Asset Composite Index is based upon actual ending period weightings of each Alternative Asset investment type.

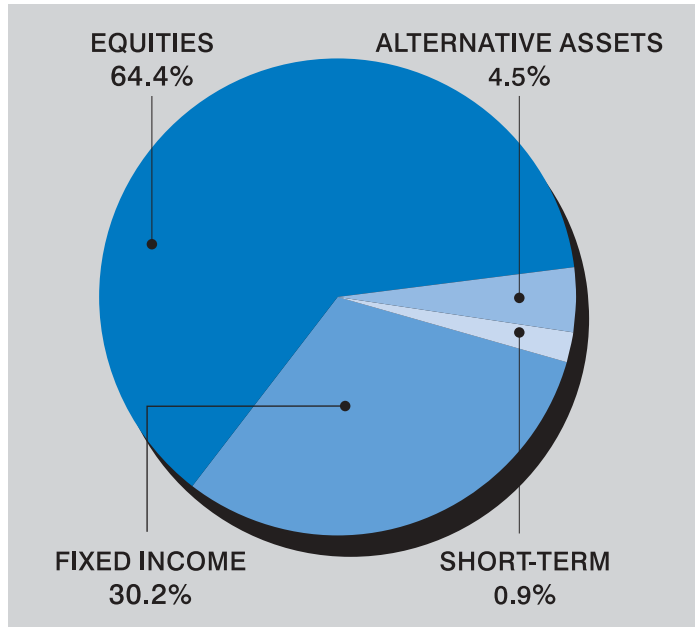
### Time Weighted Returns - Equities and Fixed Income

For the periods ended June 30



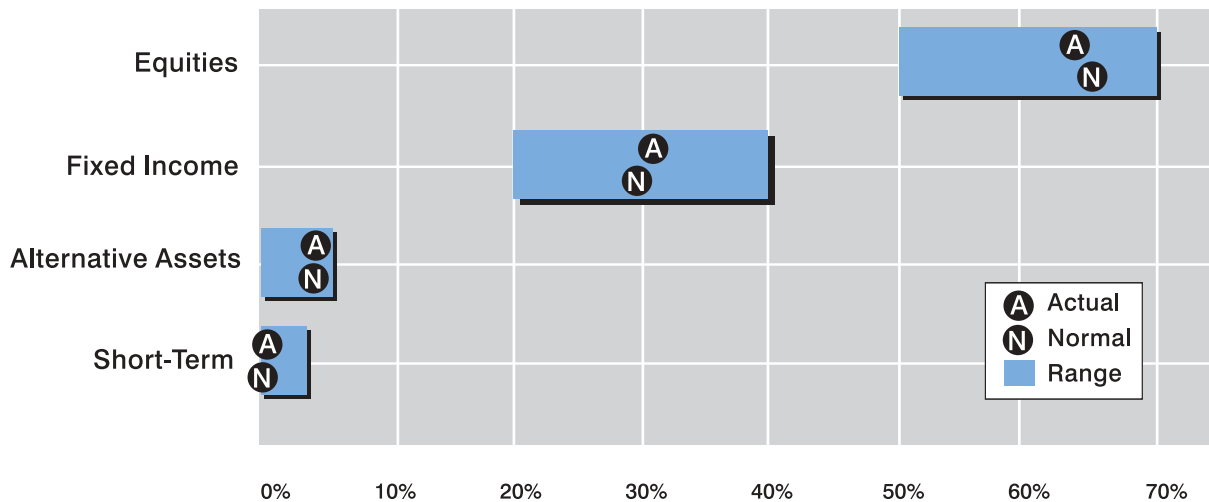
## Asset Allocation

PENSION TRUST FUND - AUGUST 31, 2002



|  | POLICY RANGES |       |        | Actual        | Market Value<br>As of 8/31/02<br>(in billions) |
|--|---------------|-------|--------|---------------|--|
|  | Low           | High  | Normal |               |  |
| <b>Equities</b>                        | 50.0%         | 70.0% | 65.5%  | 64.4%         | \$ 45.920                                      |
| <b>Fixed Income</b>                    | 20.0%         | 40.0% | 29.5%  | 30.2%         | 21.566   |
| <b>Alternative Assets <sup>1</sup></b> | 0.0%          | 5.0%  | 4.5%   | 4.5%          | 3.217  |
| <b>Short-Term</b>                      | 0.0%          | 3.0%  | 0.5%   | 0.9%          | 0.627  |
| <b>Total</b>                           |               |       |        | <u>100.0%</u> | <u>\$ 71.330</u>                               |

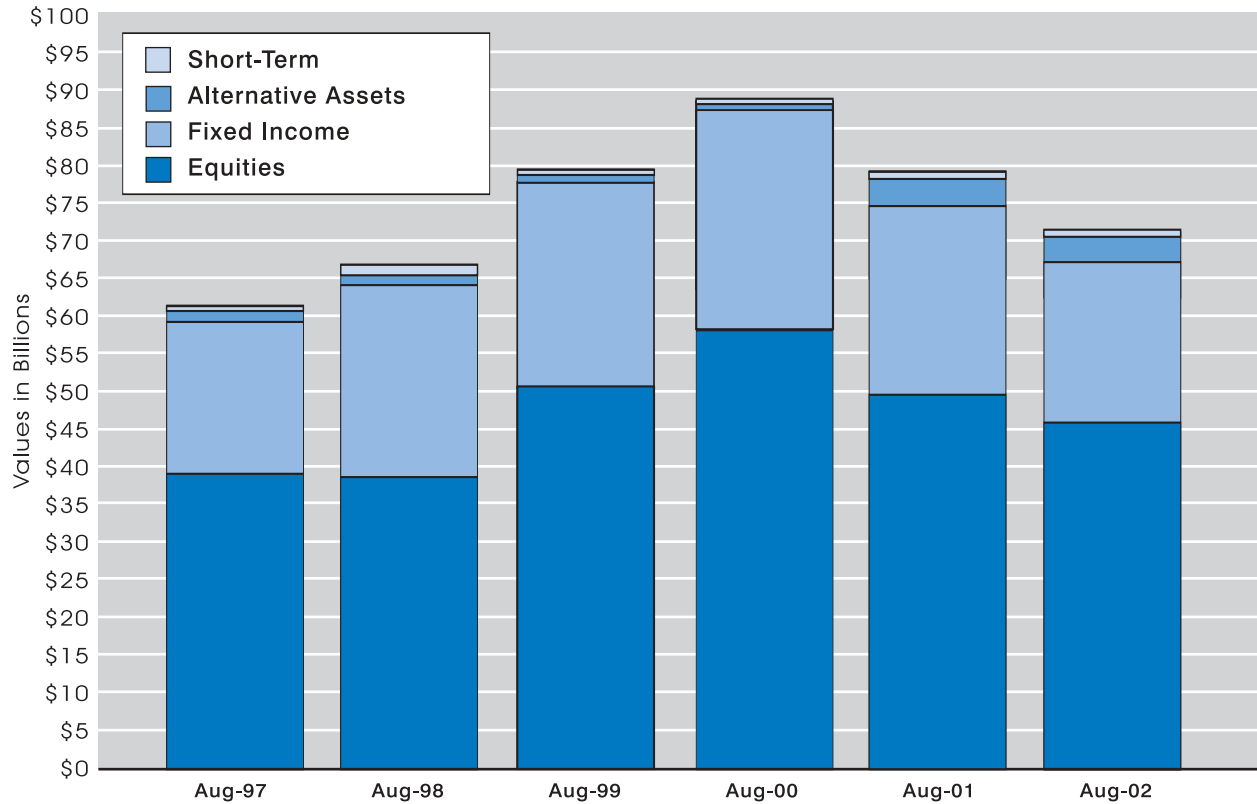
<sup>1</sup> The components of the Alternative Asset portfolio are listed on the following page.





# Total Investment Market Values

PENSION TRUST FUND - AUGUST 31



**MARKET VALUES - AUGUST 31 (in billions)**

|                                       | 1997             | 1998             | 1999             | 2000             | 2001*            | 2002*            |
|---------------------------------------|------------------|------------------|------------------|------------------|------------------|------------------|
| <b>Equities</b>                       | \$ 38.985        | \$ 38.903        | \$ 51.111        | \$ 57.780        | \$ 49.707        | \$ 45.920        |
| <b>Fixed Income</b>                   | 20.594           | 24.462           | 26.798           | 29.441           | 25.130           | 21.566           |
| <b>Alternative Assets<sup>2</sup></b> | 1.292            | 1.081            | 0.836            | 0.629            | 3.543            | 3.217            |
| <b>Short-Term<sup>1</sup></b>         | 0.705            | 1.267            | 0.331            | 0.388            | 0.857            | 0.627            |
| <b>Total</b>                          | <u>\$ 61.576</u> | <u>\$ 65.713</u> | <u>\$ 79.076</u> | <u>\$ 88.238</u> | <u>\$ 79.237</u> | <u>\$ 71.330</u> |

\* Market values for 2001 and 2002 are presented on an accrual basis which is used for calculating performance yields.

<sup>1</sup> Beginning in FY 2000, Short-Term includes cash in the treasury operations investment pool of the State Comptroller.

<sup>2</sup> The components of the Alternative Asset portfolio are as follows:

|  | 1997            | 1998            | 1999            | 2000            | 2001            | 2002            |
|--|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| <b>Private Equities</b>                    | \$              | \$              | \$ 0.001        | \$ 0.007        | \$ 0.108        | \$ 0.218        |
| <b>Strategically Traded</b>                |                 |                 |                 |                 | 0.615           | 0.786           |
| <b>Real Estate</b>                         | 1.254           | 1.036           | 0.768           | 0.515           | 0.519           | 0.425           |
| <b>Equity Transition<sup>3</sup></b>       |                 |                 |                 |                 | 0.460           | 1.235           |
| <b>Fixed Income Transition<sup>3</sup></b> |                 |                 |                 |                 | 1.681           | 0.392           |
| <b>Legacy</b>                              | 0.038           | 0.045           | 0.067           | 0.107           | 0.160           | 0.161           |
| <b>Total</b>                               | <u>\$ 1.292</u> | <u>\$ 1.081</u> | <u>\$ 0.836</u> | <u>\$ 0.629</u> | <u>\$ 3.543</u> | <u>\$ 3.217</u> |

<sup>3</sup> The Equity and Fixed Income Transition portfolios are used to fund alternative asset partnership commitments and to meet the asset allocation policy target for Alternative Assets.

## Largest Holdings

PENSION TRUST FUND - AUGUST 31, 2002

### Top Ten Domestic Equity Market Holdings

| <u>Issuer Name</u>                    | <u>Market Value</u>     | <u>Total Shares</u> |
|---------------------------------------|-------------------------|---------------------|
| General Electric Co.                  | \$ 1,063,401,053        | 35,270,350          |
| Microsoft Corp.                       | 943,072,200             | 19,215,000          |
| Exxon Mobil Corp.                     | 853,175,150             | 24,067,000          |
| Wal-Mart Stores Inc.                  | 839,475,560             | 15,697,000          |
| Pfizer Inc.                           | 736,658,520             | 22,269,000          |
| Citigroup Inc.                        | 598,268,354             | 18,267,736          |
| American International Group Inc.     | 582,350,115             | 9,273,091           |
| Johnson & Johnson                     | 575,930,395             | 10,604,500          |
| International Business Machines Corp. | 457,375,688             | 6,067,600           |
| Coca Cola Co.                         | 448,723,500             | 8,798,500           |
|                                       | <u>\$ 7,098,430,535</u> | <u>169,529,777</u>  |

### Top Ten International Equity Market Holdings

| <u>Issuer Name</u>              | <u>Market Value</u>     | <u>Total Shares</u> |
|---------------------------------|-------------------------|---------------------|
| BP Amoco Plc.                   | \$ 177,801,035          | 22,965,080          |
| Vodafone Group Plc.             | 144,965,110             | 90,544,255          |
| Novartis AG-REG SHS             | 142,785,593             | 3,518,410           |
| HSBC HLDGS Plc.                 | 124,297,498             | 10,924,900          |
| Glaxosmithkline Plc.            | 116,852,580             | 6,212,158           |
| Toyota Motor Corp.              | 97,430,917              | 3,936,000           |
| Royal Bank Scot Grp Ord         | 93,057,727              | 3,898,740           |
| Shell Transprt & Trading Co. Pl | 89,672,794              | 13,372,400          |
| UBS AG Registered               | 88,367,640              | 1,875,656           |
| Totalfinaelf SA                 | 87,193,958              | 611,485             |
|                                 | <u>\$ 1,162,424,852</u> | <u>157,859,084</u>  |

## Largest Holdings

PENSION TRUST FUND - AUGUST 31, 2002

### Top Ten Fixed Income Market Holdings<sup>1</sup>

| <u>Description</u>                                   | <u>Market Value</u>      | <u>Par Value</u>        |
|--|--------------------------|-------------------------|
| U.S. Treasury 11.25% due 2/15/2015                   | \$ 5,867,898,835         | \$ 4,229,750,000        |
| FNMA 9.25% due 1/1/2005                              | 2,957,898,120            | 2,828,542,019           |
| FHLMC 11.25% due 6/1/2006                            | 1,909,028,807            | 1,824,246,501           |
| FHLMC 5.75% due 3/15/2009                            | 1,111,719,778            | 1,017,250,000           |
| FNMA 6% due 5/15/2008                                | 673,335,244              | 588,650,000             |
| GNMA 8% due 10/15/2006                               | 620,583,453              | 583,737,005             |
| Province of Quebec 7.5% due 7/15/2023                | 247,191,702              | 205,850,000             |
| Residential Funding Mortgage 6.25%<br>due 12/25/2013 | 245,627,486              | 235,834,562             |
| FHLMC 5.125% due 8/20/2012                           | 239,100,000              | 240,000,000             |
| Federal Home Loan Bank 5.375% due 2/15/2007          | 191,684,640              | 178,000,000             |
|  | <b>\$ 14,064,068,065</b> | <b>\$11,931,860,087</b> |

*Note: A complete listing of portfolio holdings is available by contacting the TRS Communications Department.*

### Fixed Income Portfolio as of August 31, 2002<sup>1</sup>

| <u>Quality Distribution</u> |        | <u>Maturity Analysis</u> |        |
|-----------------------------|--------|--------------------------|--------|
| Treasury                    | 27.8%  | 0 - 4 Years              | 1.7%   |
| Agency                      | 41.8%  | 4 - 6 Years              | 4.5%   |
| AAA                         | 0.8%   | 6 - 10 Years             | 14.7%  |
| AA                          | 2.3%   | 10 - 20 Years            | 38.1%  |
| A                           | 11.8%  | 20 - 30 Years            | 40.0%  |
| BBB                         | 12.8%  | 30+ Years                | 1.0%   |
| Other                       | 2.7%   |                          | 100.0% |
|                             | 100.0% |                          |        |

<sup>1</sup> Excludes High Yield Fixed Income Securities



# Actuarial Section

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TEACHER RETIREMENT SYSTEM OF TEXAS

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**GABRIEL, ROEDER, SMITH & COMPANY**

**Consultants & Actuaries**

5605 N. MacArthur Blvd. • Suite 870 • Irving, Texas 75038-2631 • 469-524-0000 • fax 469-524-0003

November 6, 2002

**BOARD OF TRUSTEES**

Teacher Retirement System of Texas  
1000 Red River Street  
Austin, TX 78701-2698

**Subject: Actuary's Certification of the Actuarial Valuation as of August 31, 2002**

We certify that the information included herein and contained in the 2002 Actuarial Valuation Report is accurate and fairly presents the actuarial position of the Teacher Retirement System of Texas (TRS) as of August 31, 2002.

All calculations have been made in conformity with generally accepted actuarial principles and practices, and with the Actuarial Standards of Practice issued by the Actuarial Standards Board. In our opinion, the results presented comply with the requirements of the Texas statutes and, where applicable, the Internal Revenue Code, ERISA, and the Statements of the Governmental Accounting Standards Board. The undersigned are independent actuaries. Mr. Carter is a member of the American Academy of Actuaries, and is also an Enrolled Actuary. Both are experienced in performing valuations for large public retirement systems.

***Actuarial Valuations***

The primary purpose of the valuation report is to determine the adequacy of the current State contribution rate through measuring the resulting funding period, to describe the current financial condition of the System, and to analyze changes in the System's condition. In addition, the report provides information required by the System in connection with Governmental Accounting Standards Board Statement No. 25 (GASB No. 25), and it provides various summaries of the data.

Valuations are prepared annually, as of August 31 of each year, the last day of the System's plan and fiscal year.

***Financing Objective of the Plan***

Contribution rates are established by Law that, over time, are intended to remain level as a percent of payroll. The employee and State contribution rates have been set by Law and are intended to provide for the normal cost plus the level percentage of payroll required to amortize the unfunded actuarial accrued liability over a period not in excess of 31 years.

***Progress Toward Realization of Financing Objective***

The actuarial accrued liability, the unfunded actuarial accrued liability (UAAL), and the calculation of the resulting funding period illustrate the progress toward the realization of financing objectives. Based on this actuarial valuation as of August 31, 2002, the System has reverted to an underfunded status because of the very poor investment markets over the last two years, and the UAAL is now \$3.287 billion.

This valuation shows a normal cost equal to 12.67% of pay. Since the State contribution rate of 6.00% of pay plus the member contribution rate of 6.40% of pay total 12.40% of pay, and since this total contribution rate is less than the normal cost rate, there are no contributions available to amortize the UAAL. Therefore the funding period corresponding to the 6.00% State contribution rate is "never" or infinite, which is greater than the statutory limit of 31 years.

The actuarial valuation report as of August 31, 2002 reveals that while the System now has an unfunded liability, it still has a funded ratio (the ratio of actuarial assets to actuarial accrued liability) of 96.3%. The combination of the normal cost rate exceeding the total contribution rate and the System reverting to an underfunded status due to the very poor investment markets has put the System in a new actuarial position.

If there is not a significant recovery in the investment markets in the near future, the long term actuarial soundness of the System will be challenged in the absence of an increase in the State contribution rate. Using GASB Statement

No. 25 as a guide, the State contribution rate would need to increase from 6.00% of pay to 7.15% of pay. This rate would fund the normal cost and amortize the UAAL as of August 31, 2002 over the 30-year period called for by GASB Statement No. 25.

While it may not be appropriate to immediately increase the State contribution rate to 7.15% of pay, caution is warranted over the next few years. There should be no benefit increases passed by the Legislature over the next several Legislative Sessions without adequate funding, and the funded status should be carefully monitored. As noted above, if there is no significant market recovery over the near term, an increase in the State contribution rate will be necessary to maintain the actuarial soundness of the System.

**Plan Provisions**

The plan provisions used in the actuarial valuation are described in Table 20 of the valuation report. This valuation reflects the changes to plan provisions as enacted by the 77th Texas Legislature.

**Disclosure of Pension Information**

Effective for the fiscal year ending August 31, 1996, the Board of Trustees has adopted compliance with the requirements of Governmental Accounting Standards Board (GASB) Statement No. 25.

**Actuarial Methods and Assumptions**

The actuarial methods and assumptions have been selected by the Board of Trustees of the Teacher Retirement System of Texas based upon our analysis and recommendations. These assumptions and methods are detailed in Table 21 of the valuation report. The Board of Trustees has sole authority to determine the actuarial assumptions used for the plan. The actuarial methods and assumptions are based on a study of actual experience for the four year period ending August 31, 1999 and were adopted on March 31, 2000. Further modifications were made based on the recommendation of the actuary. These changes were adopted by the Board on September 27, 2002.

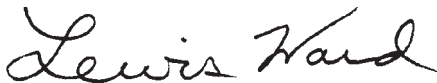
In our opinion, the actuarial assumptions used are appropriate for purposes of the valuation and are internally consistent and reasonably related to the experience of the System and to reasonable expectations.

**Data**

In preparing the August 31, 2002 actuarial valuation, we have relied upon member and asset data provided by the Teacher Retirement System of Texas. We have not subjected this data to any auditing procedures, but have examined the data for reasonableness and for consistency with prior year's data.

The schedules shown in the actuarial section and the trend data schedules in the financial section of the TRS financial report include selected actuarial information prepared by TRS staff. Six year historical information included in these schedules was based upon our work. For further information please see the full actuarial valuation report.

Respectfully submitted,



Lewis Ward  
Consultant



W. Michael Carter, FSA, EA, MAAA  
Senior Consultant

**GABRIEL, ROEDER, SMITH & COMPANY**



## Actuarial Present Value of Future Benefits

ACTUARIAL VALUATION - AUGUST 31, 2002

|   | August 31,                |                           |
|---|---------------------------|---------------------------|
|   | 2002                      | 2001                      |
| <b>Present Value of Benefits Presently Being Paid:</b>                              |                           |                           |
| Service Retirement Benefits   | \$ 36,157,908,033         | \$ 33,152,033,572         |
| Disability Retirement Benefits  | 818,188,000               | 817,054,000               |
| Death Benefits  | 768,243,000               | 754,692,000               |
| Present Survivor Benefits   | 193,210,000               | 193,248,000               |
| <b>TOTAL PRESENT VALUE OF BENEFITS PRESENTLY BEING PAID</b>                         | <b>\$ 37,937,549,033</b>  | <b>\$ 34,917,027,572</b>  |
| <b>Present Value of Benefits Payable in the Future to Present Active Members:</b>   |                           |                           |
| Service Retirement Benefits   | \$ 70,896,102,172         | \$ 71,290,589,397         |
| Disability Retirement Benefits  | 1,288,660,934             | 766,447,953               |
| Termination Benefits  | 4,499,838,330             | 3,704,974,914             |
| Death and Survivor Benefits   | 1,714,253,958             | 1,409,636,740             |
| <b>TOTAL ACTIVE MEMBER LIABILITIES</b>  | <b>\$ 78,398,855,394</b>  | <b>\$ 77,171,649,004</b>  |
| <b>Present Value of Benefits Payable in the Future to Present Inactive Members:</b> |                           |                           |
| Inactive Vested Participants  |                           |                           |
| Retirement Benefits   | \$ 936,311,478            | \$ 999,907,000            |
| Death Benefits  | 30,569,400                | 16,184,000                |
| <b>TOTAL INACTIVE VESTED BENEFITS</b>   | <b>\$ 966,880,878</b>     | <b>\$ 1,016,091,000</b>   |
| Refunds of Contributions to Inactive Non-vested Members                             | \$ 143,745,906            | \$ 11,516,418             |
| Future Survivor Benefits Payable on Behalf of Present Annuitants                    | \$ 652,645,000            | \$ 546,258,000            |
| <b>TOTAL INACTIVE LIABILITIES</b>   | <b>\$ 1,763,271,784</b>   | <b>\$ 1,573,865,418</b>   |
| <b>TOTAL ACTUARIAL PRESENT VALUE OF FUTURE BENEFITS</b>                             | <b>\$ 118,099,676,211</b> | <b>\$ 113,662,541,994</b> |

## Summary of Cost Items

|   | 2002                    | 2001                      |
|---|-------------------------|---------------------------|
| Actuarial Present Value of Future Benefits  | \$ 118,099,676,211      | \$ 113,662,541,994        |
| Present Value of Future Normal Costs        | (28,777,270,609)        | (29,445,757,377)          |
| Actuarial Accrued Liability                 | 89,322,405,602          | 84,216,784,617            |
| Actuarial Value of Assets                   | (86,034,962,833)        | (86,351,960,060)          |
| <b>UNFUNDED ACTUARIAL ACCRUED LIABILITY</b> | <b>\$ 3,287,442,769</b> | <b>\$ (2,135,175,443)</b> |

# Actuarial Information

AS OF AUGUST 31, 2002

The actuarial valuation of TRS is prepared by Gabriel, Roeder, Smith & Company. The actuary relies on membership data and asset information provided by TRS staff. While not verifying the data at their source, the actuary performs such tests for consistency and reasonableness as deemed necessary to be satisfied with the appropriateness of using the data supplied.

A summary of the actuarial assumptions and methods used by the actuary are as follows:

The entry age normal actuarial cost method of valuation was used in determining liabilities and normal cost. Differences in the past between assumed experience and actual experience ("actuarial gains and losses") become part of the actuarial accrued liabilities. Unfunded actuarial accrued liabilities are amortized to produce payments (principal and interest) which are level percents of payroll contributions.

**Disability Annuitants** - Investment Return: 8% per annum, compounded annually. Mortality: Rates developed in the actuarial investigation as of August 31, 1999.

**Active and Inactive Members** - Investment Return: 8% per annum, compounded annually. Mortality, Withdrawal, Disability Retirement and Service Retirement Rates: Rates and scales developed in the actuarial investigation as of August 31, 1999 with values at specimen ages shown in the tables below:

| Age | PROBABILITY OF DECREMENT DUE TO |            |            |                |         |                       |
|-----|---------------------------------|------------|------------|----------------|---------|-----------------------|
|     | MALE MEMBERS                    |            |            | FEMALE MEMBERS |         |                       |
|     | Death                           | Disability | Retirement | Age            | Death   | Disability Retirement |
| 20  | .000430                         |            | .000003    | 20             | .000242 | .000007               |
| 30  | .000727                         |            | .000050    | 30             | .000294 | .000081               |
| 40  | .000891                         |            | .000448    | 40             | .000512 | .000293               |
| 50  | .001899                         |            | .001514    | 50             | .001033 | .001570               |
| 60  | .005581                         |            | .002888    | 60             | .002563 | .003045               |
| 70  | .018034                         |            | .000000    | 70             | .009694 | .000000               |

| Age | PROBABILITY OF DECREMENT DUE TO WITHDRAWAL |        |        |        |        |        |        |        |        |        |        |
|-----|--|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
|     | Years of Service                           |        |        |        |        |        |        |        |        |        |        |
|     | 0  | 1      | 2      | 3      | 4      | 5      | 6      | 7      | 8      | 9      | 10+    |
| 20  | 0.1831                                     | 0.1825 | 0.1675 | 0.1532 | 0.1294 | 0.1148 | 0.1103 | 0.1155 | 0.1148 | 0.1039 | 0.0874 |
| 30  | 0.1510                                     | 0.1433 | 0.1385 | 0.1334 | 0.1088 | 0.0867 | 0.0789 | 0.0769 | 0.0734 | 0.0651 | 0.0591 |
| 40  | 0.1432                                     | 0.1363 | 0.1335 | 0.1182 | 0.0930 | 0.0740 | 0.0648 | 0.0555 | 0.0464 | 0.0419 | 0.0198 |
| 50  | 0.1230                                     | 0.1172 | 0.1055 | 0.0803 | 0.0673 | 0.0497 | 0.0445 | 0.0401 | 0.0352 | 0.0323 | 0.0097 |
| 60  | 0.1346                                     | 0.1282 | 0.1185 | 0.0942 | 0.0708 | 0.0473 | 0.0397 | 0.0378 | 0.0335 | 0.0277 | 0.0096 |
| 70  | 0.2043                                     | 0.1945 | 0.1927 | 0.1550 | 0.1062 | 0.0580 | 0.0351 | 0.0344 | 0.0379 | 0.0325 | 0.0152 |

| Age | Years of Service |        |        |        |        |        |        |        |        |        |        |
|-----|------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
|     | FEMALE MEMBERS   |        |        |        |        |        |        |        |        |        |        |
|     | 0                | 1      | 2      | 3      | 4      | 5      | 6      | 7      | 8      | 9      | 10+    |
| 20  | 0.1578           | 0.1503 | 0.1404 | 0.1141 | 0.0935 | 0.0694 | 0.0655 | 0.0672 | 0.0658 | 0.0644 | 0.0631 |
| 30  | 0.1448           | 0.1385 | 0.1293 | 0.1038 | 0.0840 | 0.0661 | 0.0587 | 0.0539 | 0.0498 | 0.0446 | 0.0427 |
| 40  | 0.0932           | 0.0864 | 0.0832 | 0.0753 | 0.0677 | 0.0534 | 0.0476 | 0.0438 | 0.0379 | 0.0332 | 0.0151 |
| 50  | 0.0979           | 0.0932 | 0.0813 | 0.0653 | 0.0514 | 0.0378 | 0.0356 | 0.0296 | 0.0261 | 0.0206 | 0.0085 |
| 60  | 0.1249           | 0.1189 | 0.1114 | 0.0946 | 0.0768 | 0.0489 | 0.0370 | 0.0332 | 0.0308 | 0.0258 | 0.0074 |
| 70  | 0.2287           | 0.2178 | 0.2119 | 0.1735 | 0.1108 | 0.0550 | 0.0384 | 0.0353 | 0.0388 | 0.0338 | 0.0114 |

| Age | PROBABILITY OF DECREMENT DUE TO RETIREMENT |        |        |        |        |        |        |  |
|-----|--|--------|--------|--------|--------|--------|--------|--|
|     | Years of Service                           |        |        |        |        |        |        |  |
|     | MALE MEMBERS                               |        |        |        |        |        |        |  |
| Age | 5-9  | 10-14  | 15-18  | 19     | 20-24  | 25-29  | 30+    |  |
| 50  | 0.0000                                     | 0.0000 | 0.0000 | 0.0000 | 0.0000 | 0.0000 | 0.2292 |  |
| 55  | 0.0052                                     | 0.0165 | 0.0214 | 0.0708 | 0.1202 | 0.1881 | 0.1903 |  |
| 60  | 0.0073                                     | 0.0393 | 0.0474 | 0.1048 | 0.1622 | 0.1754 | 0.1535 |  |
| 65  | 0.0609                                     | 0.2593 | 0.2997 | 0.3213 | 0.3429 | 0.3263 | 0.2475 |  |
| 70  | 0.0518                                     | 0.2083 | 0.1692 | 0.1861 | 0.2030 | 0.2165 | 0.2048 |  |
| 74  | 1.0000                                     | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 |  |

| Age | Years of Service |        |        |        |        |        |        |     |
|-----|------------------|--------|--------|--------|--------|--------|--------|-----|
|     | FEMALE MEMBERS   |        |        |        |        |        |        |     |
|     | Age              | 5-9    | 10-14  | 15-18  | 19     | 20-24  | 25-29  | 30+ |
| 50  | 0.0000           | 0.0000 | 0.0000 | 0.0000 | 0.0000 | 0.0000 | 0.2432 |     |
| 55  | 0.0242           | 0.0320 | 0.0324 | 0.0384 | 0.1211 | 0.2010 | 0.2257 |     |
| 60  | 0.0267           | 0.0566 | 0.0686 | 0.0726 | 0.1733 | 0.1816 | 0.2463 |     |
| 65  | 0.1123           | 0.2174 | 0.2225 | 0.2305 | 0.2898 | 0.2956 | 0.3369 |     |
| 70  | 0.0976           | 0.1655 | 0.1702 | 0.1833 | 0.2371 | 0.2633 | 0.2909 |     |
| 74  | 1.0000           | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 |     |

| Years of Service | RATES OF SALARY INCREASE                           |         |   |         |
|------------------|--|---------|---|---------|
|                  | Annual Step Rate/<br>Promotional Rates of Increase |         | Total Annual Rate of Increase<br>(Including 4% General Increase Rate) |         |
|                  | Males  | Females | Males   | Females |
| 1                | 22.15%   | 20.00%  | 26.15%  | 24.00%  |
| 2                | 3.50   | 3.10    | 7.50  | 7.10    |
| 3                | 3.00   | 2.40    | 7.00  | 6.40    |
| 4                | 2.75   | 2.20    | 6.75  | 6.20    |
| 5                | 2.40   | 2.00    | 6.40  | 6.00    |
| 6                | 2.20   | 1.75    | 6.20  | 5.75    |
| 7                | 2.00   | 1.65    | 6.00  | 5.65    |
| 8                | 1.50   | 1.50    | 5.50  | 5.50    |
| 9                | 1.40   | 1.40    | 5.40  | 5.40    |
| 10               | 1.20   | 1.20    | 5.20  | 5.20    |
| 11-19            | 1.00   | 1.00    | 5.00  | 5.00    |
| 20 or more       | 0.00   | 0.00    | 4.00  | 4.00    |

**Service Retirement Annuitants, Nominees and Survivors** - Investment Return: 8% per annum, compounded annually. Mortality: 1994 Group Annuity Male Mortality Table with a four-year setback and the 1994 Group Annuity Female Mortality with a two-year setback; used for service retirement annuitants, beneficiaries and survivors. These tables are selected to best reflect the experience developed in the actuarial investigation as of August 31, 1999.

**Actuarial Value of Assets** - The actuarial value of assets is equal to the market value of assets less a five-year phase in of the excess (shortfall) between expected investment return and actual income with the resulting value not being less than 80% or more than 120% of the market value of assets.

**Funding of Unfunded Actuarial Accrued Liability** - Funded by the excess of future State contributions required by Law over the amount of such contributions required to fund the normal cost of benefits. Based on a study of all new entrants hired in the period from 1995 through 1999 and taking into account all changes in benefit provisions, the normal cost for benefits provided by the System is 12.67% of payroll (6.40% by members plus 6.27% by the State), which is 0.27% of payroll more than the total contributions required by Law. It is intended that the shortfall amount of 0.27% of payroll will be paid for by a reduction in any overfunded position of the System, assuming that total payroll increases by 3.00% per year.

As long as the funding surplus (the negative UAAL) is sufficient to offset the 0.27% contribution shortfall, the System remains actuarially funded. In this case, the funding period will be deemed to be 0.0 years if the funding surplus will support the contribution shortfall indefinitely into the future, based on the current actuarial assumptions.

As of the valuation as of August 31, 2002, there is no negative UAAL, i.e., there is a positive unfunded actuarial accrued liability. Since there are no contributions available to amortize this UAAL, it will never be funded. Future funding of the UAAL will be dependent on either the generation of actuarial experience gains sufficient in size to return the System to an overfunded status or on an increase in the State contribution rate.

**Assumed State Contribution Rate** - The Appropriations Act, established an actual contribution rate of 6.00% for fiscal years 2000, 2001, and 2002. The contribution rate valuation results are determined assuming that the current 6.00% state contribution rate is the ultimate rate.

SCHEDULE OF ACTIVE MEMBER VALUATION DATA

| Valuation Year | Number   | Annual Payroll In Thousands | Average Annual Pay | Annual Percentage Increase In Average Pay |
|----------------|----------|-----------------------------|--------------------|---|
| 1997           | 678,749  | \$17,044,480                | \$25,112           | 2.5%                                      |
| 1998           | 705,447  | 18,324,935                  | 25,977             | 3.4%                                      |
| 1999           | 736,058  | 19,529,343                  | 26,533             | 2.1%                                      |
| 2000           | 766,906  | 21,920,132                  | 28,583             | 7.7%                                      |
| 2001           | 797,339  | 23,364,661                  | 29,303             | 2.5%                                      |
| 2002           | 745,923* | 24,818,417*                 | 33,272             | 13.5%                                     |

\* The number of active members and the annual payroll exclude active noncontributing members.

## Actuarial Information

AS OF AUGUST 31, 2001

### SOLVENCY TEST

A short-term solvency test is one means of checking a retirement system's progress under its funding program. The schedule below provides an historical illustration of a short-term solvency test for TRS wherein present assets are compared with: (1) active member contributions on deposit; (2) the liabilities for future benefits to present annuitants; (3) the liabilities for active members under the entry age normal actuarial cost method including a projection of future salary increases and anticipated future service.

Under the level percent of payroll financing followed by TRS, liabilities for active member contributions on deposit and the liabilities for future benefits to present retirees and beneficiaries will be fully covered by present assets except in rare circumstances. In addition, liabilities for active member benefits earned or to be earned in the future will be partially covered by the remainder of present assets. Generally, if the system has been using level cost financing, the funded portion of active member benefits will increase over time.

(MONEY AMOUNTS SHOWN IN MILLIONS)

| Valuation<br>As Of<br>August 31 | Aggregate Actuarial Accrued<br>Liabilities For |  |   | Portion of Aggregate Actuarial Accrued Liabilities Covered By<br>Valuation Assets |                                       |   |
|---------------------------------|--|--|---|---|---------------------------------------|---|
|                                 | 1  | 2                                      | 3   | 1   | 2                                     | 3   |
|                                 | Active*<br>Member<br>Contri-<br>butions        | Retirees*<br>And<br>Benefi-<br>ciaries | Active Members<br>(State Financed<br>Portion) | Active<br>Member<br>Contri-<br>butions  | Retirees<br>And<br>Benefi-<br>ciaries | Active Members<br>(State Financed<br>Portion) |
| 1997                            | \$11,707                                       | \$21,936                               | \$20,263                                      | \$53,760  | 100%                                  | 99.3%   |
| 1998                            | 12,517   | 22,557                                 | 22,820  | 60,357  | 100                                   | 110.8   |
| 1999                            | 13,359   | 27,366                                 | 26,520  | 69,435  | 100                                   | 108.3   |
| 2000                            | 14,231   | 29,604                                 | 30,047  | 79,328  | 100                                   | 118.1   |
| 2001                            | 15,339   | 34,917                                 | 33,960  | 86,352  | 100                                   | 106.3   |
| 2002                            | 16,387   | 37,938                                 | 34,998  | 86,035  | 100                                   | 90.6  |

\*Adjusted for pending transfers to retired reserve at August 31 for pending retirements.

A Schedule of Funding Progress including a 6-Year Summary of Actuarial Accrued Liabilities and Unfunded Actuarial Accrued Liabilities can be found in the Required Supplementary Information found immediately following the Notes to the Financial Statements.

## Analysis of Financial Experience

### Changes in Unfunded Actuarial Accrued Liabilities (UAAL) Resulting from Differences Between Assumed Experience and Actual Experience

|                               | Increase/(Decrease) for Year (in Billions) |            |            |            |            |            |
|-------------------------------|--|------------|------------|------------|------------|------------|
|                               | 2002                                       | 2001       | 2000       | 1999       | 1998       | 1997       |
| Investment (Gains)/Losses     | \$ 5.527                                   | \$ (1.894) | \$ (5.417) | \$ (4.812) | \$ (2.832) | \$ (2.836) |
| Legislative Benefit Increases |  | 4.553      |            | 5.611      |            | 1.762      |
| March 2000 Experience Study   |  |            | 1.123      |            |            |            |
| Contribution Experience       | .017                                       | (.292)     | (0.115)    | .292       | (0.059)    | 0.117      |
| Assumption Changes            | (.848)                                     |            |            |            |            | (0.196)    |
| Liability Experience          | .726                                       | .944       | 1.153      | (.818)     | (0.246)    | (0.514)    |
| Other Changes                 |  |            |            |            | 0.528      |            |
| Net Increase/(Decrease)       | \$ 5.422                                   | \$ 3.311   | \$ (3.256) | \$ .273    | \$ (2.609) | \$ (1.667) |
| Beginning UAAL                | (2.135)                                    | (5.446)    | (2.190)    | (2.463)    | 0.146      | 1.813      |
| Ending UAAL                   | \$ 3.287                                   | \$ (2.135) | \$ (5.446) | \$ (2.190) | \$ (2.463) | \$ 0.146   |

# Benefits Section

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TEACHER RETIREMENT SYSTEM OF TEXAS

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## SUMMARY OF BENEFITS

The Teacher Retirement System of Texas administers a defined benefit plan that is a qualified pension trust under Section 401(a) of the Internal Revenue Code. The pension trust provides service and disability retirement as well as death and survivor benefits to eligible employees of public education in Texas. A current general information booklet, *TRS Benefits Handbook*, is provided to each TRS member and annuitant. Benefits are financed by member and state contributions and through investment earnings of the pension trust fund.

TRS administers TRS-ActiveCare which will offer health care coverage to over 150,000 active public school employees in over 970 school districts and other participating education entities beginning September 1, 2002. During the 2002-2003 plan year (FY03) eligible employees may choose health care coverage for themselves and their eligible dependents from three TRS-ActiveCare plans providing access to a state-wide provider network. In the future, additional school districts will be eligible to participate in TRS-ActiveCare and coverage choices may be expanded to meet the changing needs of the Texas public school employees and their families.

The system administers a separate trust that provides comprehensive health care coverage for retired members through the Texas Public School Retired Employees Group Insurance Program. The health care coverage is financed by contributions from the state, contributions from active public school employees, premium payments from plan participants, and investment earnings of the insurance trust fund.

TRS also administers an optional long-term care insurance program for eligible retirees and public school employees, respectively. Certain family members are also eligible. The plan is available on an enrollee-pay-all basis.

The major retirement benefit provisions are:

### Service Retirement

*Normal Retirement Eligibility:* Age 65 with five years of credited service,  
or when the sum of member's age and years of credited service equals or exceeds 80 years.

*Standard Annuity:* A monthly benefit payable throughout the retiree's lifetime.

*Benefit Formula:* 2.3 percent times the average of three highest annual salaries times years of credited service equals an annual standard annuity.

*Minimum Benefit:* \$150 per month.

*Early Retirement Eligibility:* Age 55 with at least five years of credited service,  
or any age below 50 with 30 or more years of credited service.

*Early Retirement Benefit:* The standard annuity calculated under the benefit formula (or the minimum benefit, if applicable) reduced actuarially for early payment.

### Disability Retirement

*Eligibility:* Physical or mental disability precludes the member's continued performance of current duties and the disability is probably permanent, certified by the TRS Medical Board.

*Benefit:* For disabled members with at least 10 years of credited service, standard annuity unreduced for early payment, or \$150 per month minimum benefit.  
For disabled members with fewer than 10 years of credited service, a flat amount of \$150 per month.

*Duration:* For retirees with 10 or more years of credited service, payments continue for as long as disability continues. For those with fewer than 10 years of credited service, payments continue for the duration of the disability or the number of months of creditable service, whichever is shorter.

### Annuity Payment Options

Service or disability retirees may select an optional form of payment that reduces the standard annuity by application of age-related actuarial reduction factors. Actuarial factors for disability retirees are different from those for service retirees because the

## SUMMARY OF BENEFITS

actuarial tables use different assumptions about life expectancy for the two groups. The available options include 100, 75 and 50 percent joint and survivor options, and five- and 10-year certain payments.

### The Pop-Up Provision

In the event that a designated beneficiary under any of the joint and survivor options dies while the retiree is still living, the retiree's future monthly payment increases to the amount of the standard annuity.

### Partial Lump Sum Option (PLSO)

In 1999, the 76th Texas Legislature approved the establishment of a partial lump sum option for eligible TRS members. Through this option, at the time of retirement qualifying active members may elect to receive an actuarially reduced service annuity plus a cash lump sum distribution.

Members may participate in the Partial Lump Sum Option if they are eligible for service retirement benefits that are not reduced for early age retirement, are not participating in the Deferred Retirement Option Plan (DROP), and are not retiring with disability benefits.

Partial lump sum distributions equal to 12, 24 or 36 months of a standard service retirement annuity may be selected. When members select this option their annuity is actuarially reduced.

Flexible distribution options are available including rollover to another eligible retirement plan.

### Deferred Retirement Option Plan (DROP)

Effective September 1, 1997, DROP was created as a pre-retirement benefit provision for active members who are eligible to retire with unreduced benefits and who have at least 25 years of credited service.

The program allows eligible active members to elect to freeze their standard annuity and to have a portion of the frozen standard annuity deposited into a DROP account while continuing to work for a TRS-covered employer. Interest on DROP accounts is credited at the rate of five percent per annum. Members are not considered to be retired while participating in DROP.

The law allows an irrevocable election to participate in 12-month increments, for up to five years. During DROP participation, the member does not accrue additional compensation or service credits to be considered in calculating the standard annuity. Also, during DROP participation, the member's statutory

contributions to TRS continue; however, contributions are not credited to the member's contribution account and are not subject to refund.

Participation in DROP ends at the earliest of the expiration of the election period, retirement, or death. The accumulated DROP account may be distributed at the member's election as a single lump sum or in monthly or yearly installments covering five or 10 years. Eligible distributions may be rolled over to another eligible retirement plan.

### Vesting of Benefits

A member who has completed at least five years of credited service has earned a nonforfeitable right to service retirement benefits, with payment deferred to normal retirement age, provided the member's contributions are not withdrawn from the system.

### Death and Survivor Benefits

Active Members — The primary beneficiary of an active member will receive one of the following benefits in the event of that member's death before retirement (even though the member may be absent from service because of illness or is within five years of being eligible to retire when leaving employment):

1. A lump sum payment equal to twice the member's annual compensation or \$80,000, whichever is less.
2. Sixty monthly payments equal to the member's standard annuity without reduction for age.
3. For a sole beneficiary, lifetime payments equal to a 100 percent joint and survivor annuity.
4. A return of the member's contributions with accumulated interest.
5. Survivor benefits of \$2,500 lump sum payment plus \$350 per month to beneficiary spouse with minor children, continuing until the youngest child reaches age 18. At age 65, the spouse would begin receiving \$250 per month for life.

In addition to these five options, a lump sum death benefit of \$160,000 is available if the active member is employed in a TRS-covered position and dies due to a physical assault during the performance of his or her regular duties.

Also, the DROP beneficiary of a DROP participant will receive the accumulated DROP account balance, payable as a lump sum or in periodic installments.

## SUMMARY OF BENEFITS

**Retired Members** — In addition to any joint and survivor or guaranteed period annuity that may be payable under an optional form of payment a retiree elected, the primary beneficiary of a service retiree is entitled to a \$10,000 lump sum payment. In certain circumstances, survivors may select alternate distribution options in lieu of the lump sum distribution.

In any event, if total payments to the retiree are less than accumulated contributions at retirement, any remainder is paid to the beneficiary. Should a retiree die prior to receiving all partial lump sum payments that are due, TRS will pay any remaining partial lump sum payments in a single lump sum payment to the designated beneficiary.

The major health care and long-term care provisions are:

### Health Care for Active Public School Employees

A statewide health care benefits program for employees of school districts, open enrollment charter schools, regional education service centers, and other educational districts whose employees are members of TRS was established. The new program, TRS-ActiveCare, is effective September 1, 2002, and will be administered by TRS. TRS retirees will continue to be covered by the existing TRS-Care program. The new initiative for active public school employees is designed to initially address the most critical areas of the state with regard to availability and affordability of health care for public school employees. Beginning in September 2002, the program will cover smaller districts, but it will broaden to include larger districts over a period of time.

The state will provide \$1,000 per year, payable monthly, for each active school employee who is a contributing member of TRS, whether or not the employee participates in either the state program or a local district insurance program. Employees may choose to use this compensation supplement to pay for additional employee coverage, dependent coverage, or receive it as compensation.

All districts, whether participating in the state health care program or not, will receive a monthly contribution from the state of \$75 per employee covered by either the state program or a local district program.

Districts must contribute at least an additional \$150 monthly per active employee for the employee's health coverage—part of which may be funded by state supplemental assistance.

### Retiree Health Coverage

In addition to the benefits described above, the Texas Public School Retired Employees Group Insurance Program known as TRS-Care, makes available a basic level of health coverage without cost to TRS public school retirees. Retirees and their eligible dependents may pay premiums and participate in an optional plan of more comprehensive benefits and coverage. Eligible members are those who have retired from a position in Texas public schools after 10 or more years of credited service and are not eligible for other statewide health insurance. Disability retirees with less than 10 years of credited service are eligible for insurance while they are receiving disability retirement benefits.

### Long-Term Care Insurance Program

Eligible active and retired members, their dependents, and certain other family members may participate in the TRS long-term care insurance program.

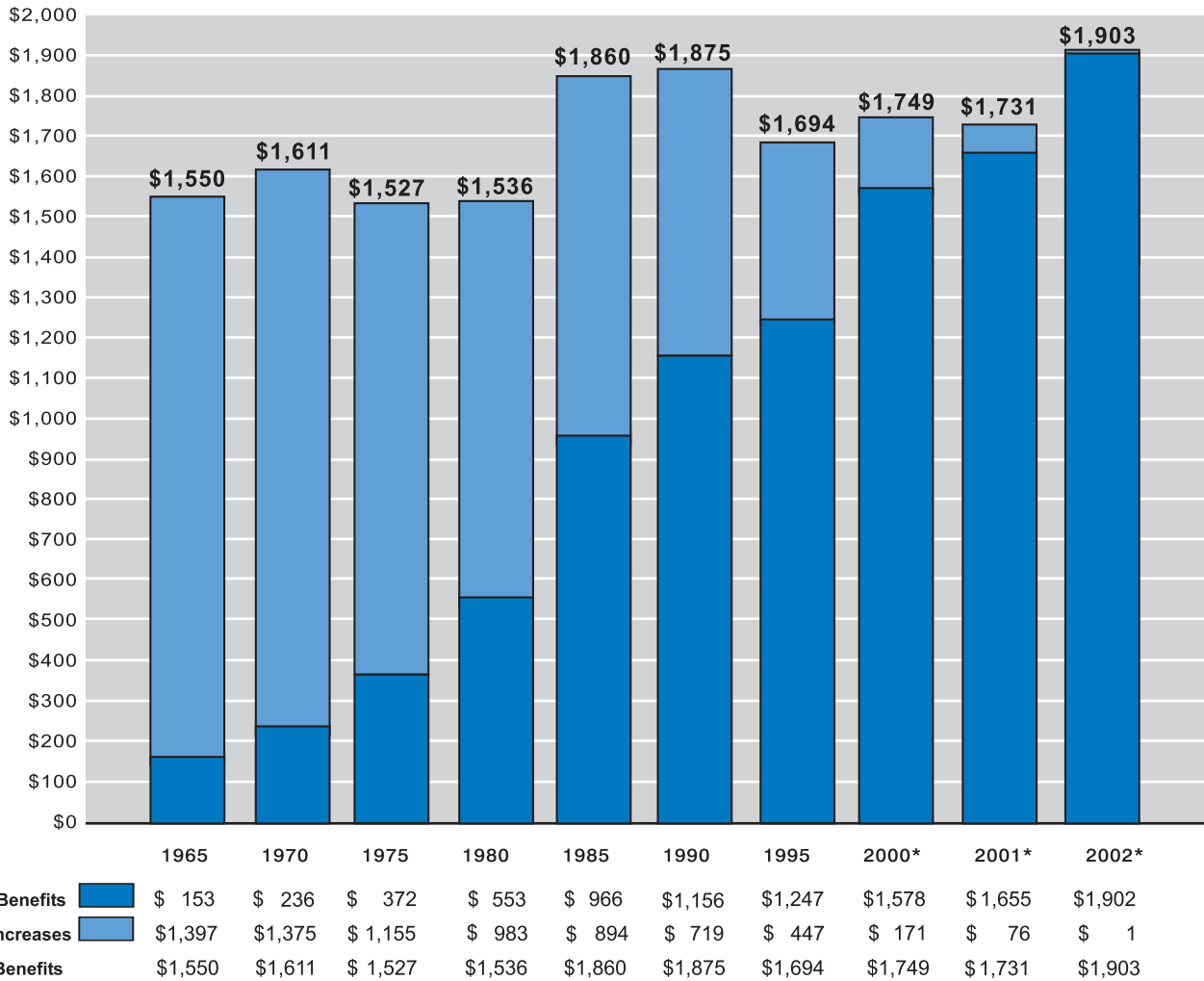
The term "long-term care" refers to the type of medical or personal care services needed if a person becomes unable to care for himself or herself because of chronic illness, disability, loss of function or mental impairment. The plan pays benefits if the member becomes unable to perform two of the following six activities of daily living without substantial assistance from another: bathing, eating, transferring (i.e., getting in and out of bed), dressing, continence, toileting. The plan also pays benefits as a result of a severe cognitive impairment that requires supervision or verbal direction from another person in order to protect the member or others from serious injury.

Members can select a Daily Benefit Amount (DBA) of \$100, \$125 or \$150. The plan will reimburse the member for the actual expenses incurred up to specified amounts depending on the type of care received.

The plan also provides for a cash benefit for certain types of care. Optional or automatic inflation protection is offered to help offset the effects of inflation. Other optional features are available for an additional premium. The plan is a tax-qualified, long-term care plan as defined by the Internal Revenue Code of 1986, Section 7702B(b).



**Current Average Monthly Benefit by Year of Retirement**  
 Service Retiree Accounts as of August 31, 2002



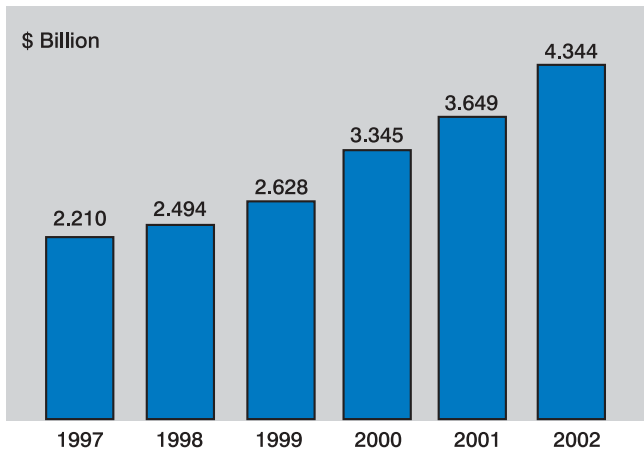
\* Note: Before adjustment for the Partial Lump Sum Option, average original benefits were \$1,709, \$1,803, and \$2,077 for fiscal years 2000, 2001, and 2002 respectively.

## GROWTH OF THE SYSTEM

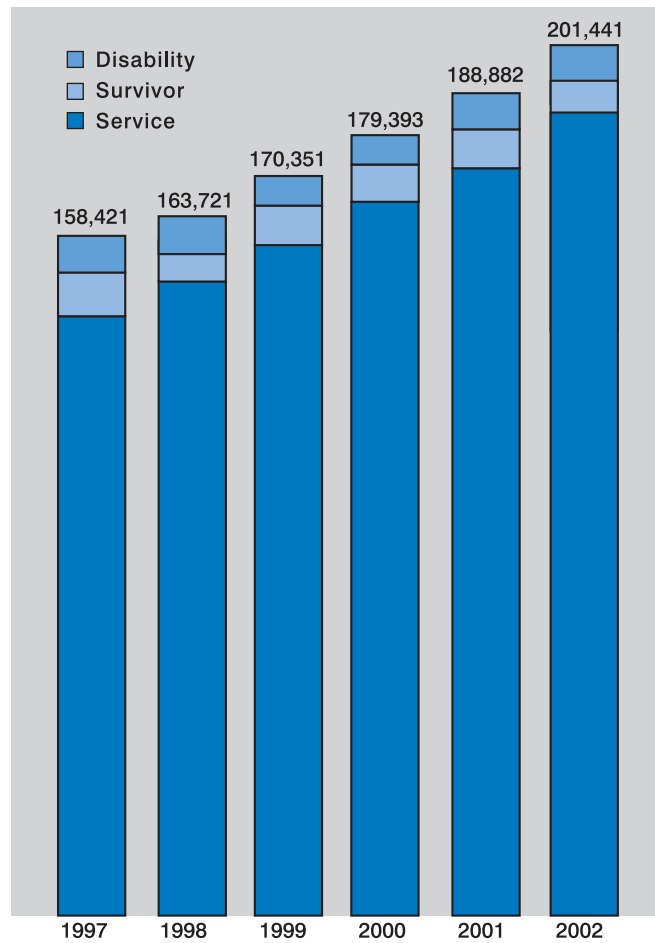
Benefit payments during fiscal year 2002 totaled over \$4.34 billion, an increase of \$695.5 million over the previous year. By August 2002, the monthly annuity payroll had grown to \$333.4 million, with over 188,500 annuitants receiving payments.

Annuities, including multiple payments to one person and payments deferred to a later date, totaled 201,441. The number of current member accounts increased by 29,352 and the number of retiree accounts increased by 12,559.

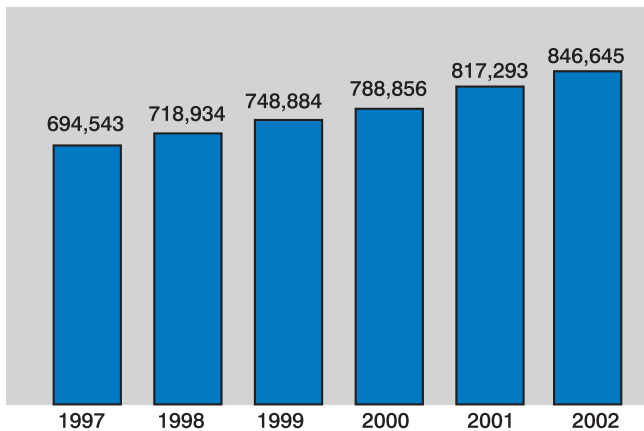
**Benefit Payments**



**Annuities**



**Member Accounts**



## PAYMENT INFORMATION

### Average Benefit Payments for Service Retirees

PENSION TRUST FUND

| Retirement Effective Dates   | Years Credited Service |          |           |             |             |             |
|------------------------------|------------------------|----------|-----------|-------------|-------------|-------------|
|                              | 5-10                   | 11-15    | 16-20     | 21-25       | 26-30       | 30+         |
| <b>9-1-96 to 8-31-97</b>     |                        |          |           |             |             |             |
| Average Monthly Benefit      | \$260.14               | \$440.59 | \$ 867.81 | \$ 1,389.66 | \$ 2,273.34 | \$ 3,220.17 |
| Average Final Average Salary | \$17,701               | \$20,605 | \$ 24,613 | \$ 29,909   | \$ 38,872   | \$ 45,962   |
| Number of Retirees           | 759                    | 867      | 1,127     | 1,683       | 1,997       | 2,084       |
| <b>9-1-97 to 8-31-98</b>     |                        |          |           |             |             |             |
| Average Monthly Benefit      | \$246.47               | \$442.14 | \$ 934.37 | \$ 1,418.93 | \$ 2,288.51 | \$ 3,133.68 |
| Average Final Average Salary | \$17,826               | \$21,718 | \$ 26,543 | \$ 31,057   | \$ 40,425   | \$ 46,326   |
| Number of Retirees           | 992                    | 991      | 1,251     | 1,970       | 2,987       | 2,220       |
| <b>9-1-98 to 8-31-99</b>     |                        |          |           |             |             |             |
| Average Monthly Benefit      | \$245.30               | \$452.81 | \$ 913.89 | \$ 1,433.80 | \$ 2,245.44 | \$ 3,138.49 |
| Average Final Average Salary | \$18,658               | \$22,051 | \$ 26,843 | \$ 31,978   | \$ 40,584   | \$ 47,334   |
| Number of Retirees           | 1,000                  | 975      | 1,241     | 1,960       | 2,399       | 1,817       |
| <b>9-1-99 to 8-31-00</b>     |                        |          |           |             |             |             |
| Average Monthly Benefit *    | \$245.87               | \$454.46 | \$ 919.39 | \$ 1,402.38 | \$ 2,182.08 | \$ 2,985.59 |
| Average Final Average Salary | \$19,273               | \$22,632 | \$ 28,305 | \$ 33,328   | \$ 42,806   | \$ 49,525   |
| Number of Retirees           | 1,086                  | 1,134    | 1,358     | 2,336       | 3,429       | 3,121       |
| <b>9-1-00 to 8-31-01</b>     |                        |          |           |             |             |             |
| Average Monthly Benefit *    | \$236.90               | \$426.62 | \$ 903.55 | \$ 1,377.10 | \$ 2,128.59 | \$ 2,895.60 |
| Average Final Average Salary | \$20,172               | \$23,311 | \$ 29,582 | \$ 34,846   | \$ 44,768   | \$ 51,273   |
| Number of Retirees           | 1,034                  | 1,145    | 1,387     | 2,361       | 3,711       | 3,277       |
| <b>9-1-01 to 8-31-02</b>     |                        |          |           |             |             |             |
| Average Monthly Benefit *    | \$236.70               | \$465.37 | \$ 945.78 | \$ 1,441.92 | \$ 2,208.44 | \$ 3,023.90 |
| Average Final Average Salary | \$20,394               | \$24,678 | \$ 31,177 | \$ 36,472   | \$ 46,472   | \$ 53,902   |
| Number of Retirees           | 1,065                  | 1,134    | 1,508     | 2,875       | 4,748       | 4,491       |

\* Average monthly benefits have been reduced for Partial Lump Sum Option payments of \$184.5, \$280.9, and \$386.4 million in fiscal years 2000, 2001, and 2002, respectively.

### Benefit Payments by Type

PENSION TRUST FUND

|                              | 1997            | 1998            | 1999            | 2000            | 2001            | 2002            |
|------------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Service Retirements          | \$1,979,837,227 | \$2,256,664,999 | \$2,362,283,798 | \$2,864,478,345 | \$3,047,338,739 | \$3,591,219,348 |
| Deferred Retirement Option*  |                 | \$ 1,630,705    | \$ 12,257,736   | \$ 18,785,833   | \$ 36,929,725   | \$ 48,697,687   |
| Partial Lump Sum Option**    |                 |                 |                 | \$ 184,452,896  | \$ 280,942,321  | \$ 386,442,648  |
| Disability Retirements       | \$ 80,414,696   | \$ 88,244,398   | \$ 89,615,768   | \$ 105,225,801  | \$ 107,030,338  | \$ 119,913,327  |
| Death and Survivor Benefits: |                 |                 |                 |                 |                 |                 |
| Accumulated Savings          | \$ 314,686      | \$ 512,683      | \$ 829,773      | \$ 780,487      | \$ 908,801      | \$ 1,504,798    |
| Annual Salary                | \$ 40,209,581   | \$ 34,459,094   | \$ 40,109,292   | \$ 36,761,945   | \$ 39,887,958   | \$ 43,685,098   |
| Survivor Annuities           | \$ 56,273,629   | \$ 53,692,115   | \$ 63,451,102   | \$ 63,895,597   | \$ 63,441,321   | \$ 71,664,740   |
| Life Annuities               | \$ 46,029,067   | \$ 53,044,483   | \$ 53,330,067   | \$ 63,479,659   | \$ 65,154,382   | \$ 72,919,628   |
| 60 Monthly Payments          | \$ 3,673,988    | \$ 3,809,152    | \$ 3,577,742    | \$ 4,011,753    | \$ 4,475,175    | \$ 5,649,671    |
| Remainder of Contributions   | \$ 2,818,372    | \$ 2,117,822    | \$ 2,286,288    | \$ 2,704,357    | \$ 2,651,578    | \$ 2,558,781    |
| Refunds                      | \$ 166,125,695  | \$ 183,430,398  | \$ 206,354,473  | \$ 214,999,991  | \$ 214,434,792  | \$ 186,421,065  |

\* Deferred Retirement Option Plan benefit effective September 1, 1997

\*\* Partial Lump Sum Option Plan benefit effective September 1, 1999

## Annuity Payments by Benefit Type

PENSION TRUST FUND

| Monthly Benefit  | Annuity Payments | Benefit Type * |               |              |                   |              |              |              |
|------------------|------------------|----------------|---------------|--------------|-------------------|--------------|--------------|--------------|
|                  |                  | Retirements    |               |              | Survivor Payments |              |              |              |
|                  |                  | 1              | 2             | 3            | 4                 | 5            | 6            | 7            |
| \$ 1 - 200       | 7,085            | 2,450          | 3,753         | 368          | 430               | 36           | 33           | 15           |
| \$ 201 - 400     | 23,771           | 4,667          | 8,621         | 438          | 1,040             | 1,202        | 493          | 7,310        |
| \$ 401 - 600     | 16,858           | 6,661          | 7,275         | 1,297        | 1,176             | 208          | 241          | 0            |
| \$ 601 - 800     | 14,156           | 6,961          | 4,373         | 1,300        | 1,028             | 257          | 237          | 0            |
| \$ 801 - 1,000   | 13,810           | 8,395          | 3,114         | 891          | 946               | 267          | 197          | 0            |
| \$ 1,001 - 1,200 | 11,076           | 6,872          | 2,327         | 651          | 842               | 213          | 171          | 0            |
| \$ 1,201 - 1,400 | 9,664            | 5,719          | 2,328         | 519          | 751               | 224          | 123          | 0            |
| \$ 1,401 - 1,600 | 10,049           | 5,892          | 2,699         | 481          | 647               | 230          | 100          | 0            |
| \$ 1,601 - 1,800 | 10,165           | 6,298          | 2,526         | 443          | 598               | 201          | 99           | 0            |
| \$ 1,801 - 2,000 | 10,340           | 6,825          | 2,456         | 358          | 445               | 192          | 64           | 0            |
| \$ over 2,000    | 74,467           | 58,862         | 10,425        | 1,173        | 2,936             | 938          | 133          | 0            |
| <b>Totals</b>    | <b>201,441</b>   | <b>119,602</b> | <b>49,897</b> | <b>7,919</b> | <b>10,839</b>     | <b>3,968</b> | <b>1,891</b> | <b>7,325</b> |

**\* Benefit Type**

- 1 - Normal Retirement of Age and Service
- 2 - Early Retirement
- 3 - Disability Retirement
- 4 - Survivor Payment, Joint Life or Guarantee

- 5 - Survivor Payment, Death in Service
- 6 - Survivor Payment, After Disability Retirement
- 7 - Survivor Payment, After Service Retirement

## Annuity Payments by Plan Selected

PENSION TRUST FUND

| Monthly Benefit  | Annuity Payments | Plan Selected * |               |               |              |               |              |
|------------------|------------------|-----------------|---------------|---------------|--------------|---------------|--------------|
|                  |                  | 1               | 2             | 3             | 4            | 5             | 6            |
| \$ 1 - 200       | 7,085            | 3,370           | 2,333         | 440           | 244          | 660           | 38           |
| \$ 201 - 400     | 23,771           | 7,866           | 4,105         | 1,107         | 596          | 1,396         | 8,701        |
| \$ 401 - 600     | 16,858           | 9,531           | 3,718         | 1,375         | 742          | 1,492         | 0            |
| \$ 601 - 800     | 14,156           | 7,697           | 3,302         | 1,443         | 667          | 1,047         | 0            |
| \$ 801 - 1,000   | 13,810           | 7,385           | 3,045         | 1,547         | 699          | 1,134         | 0            |
| \$ 1,001 - 1,200 | 11,076           | 5,639           | 2,574         | 1,507         | 525          | 831           | 0            |
| \$ 1,201 - 1,400 | 9,664            | 4,232           | 2,739         | 1,398         | 486          | 809           | 0            |
| \$ 1,401 - 1,600 | 10,049           | 4,202           | 2,948         | 1,467         | 536          | 896           | 0            |
| \$ 1,601 - 1,800 | 10,165           | 4,198           | 3,017         | 1,529         | 504          | 917           | 0            |
| \$ 1,801 - 2,000 | 10,340           | 4,096           | 3,132         | 1,668         | 505          | 939           | 0            |
| \$ over 2,000    | 74,467           | 26,407          | 26,167        | 12,949        | 3,195        | 5,749         | 0            |
| <b>Totals</b>    | <b>201,441</b>   | <b>84,623</b>   | <b>57,080</b> | <b>26,430</b> | <b>8,699</b> | <b>15,870</b> | <b>8,739</b> |

**\* Plan Selected**

- 1 - Life Annuity
- 2 - Joint to Survivor
- 3 - Joint to Survivor 50% / Joint to Survivor 75%

- 4 - 5-Year Guarantee
- 5 - 10-Year Guarantee
- 6 - Survivor Benefit

## Retirees and Beneficiaries Added to and Removed from Payroll

PENSION TRUST FUND - For Years 1997-2002\*

| Year Ended | Number of Retirees and Beneficiaries |         |             | Annual Allowances |            |
|------------|--------------------------------------|---------|-------------|-------------------|------------|
|            | Added                                | Removed | End of Year | End of Year       | % Increase |
| 1997       | 10,634                               | 4,753   | 158,421     | \$ 2,162,144,861  | 4.97%      |
| 1998       | 9,830                                | 4,530   | 163,721     | \$ 2,442,143,273  | 12.95%     |
| 1999       | 11,458                               | 4,828   | 170,351     | \$ 2,572,614,096  | 5.34%      |
| 2000       | 14,207                               | 5,165   | 179,393     | \$ 3,120,148,258  | 21.28%     |
| 2001       | 14,707                               | 5,218   | 188,882     | \$ 3,364,802,134  | 7.84%      |
| 2002       | 18,140                               | 5,581   | 201,441     | \$ 4,000,979,540  | 18.91%     |

\* This schedule is based on the August payroll and includes only monthly annuity and survivor benefits including multiple payments to one person. Monthly post-retirement benefit increases of approximately \$13.3 million, \$34.3 million and \$28.7 million became effective in fiscal years 1998, 2000 and 2002, respectively.

# Statistical Section

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TEACHER RETIREMENT SYSTEM OF TEXAS

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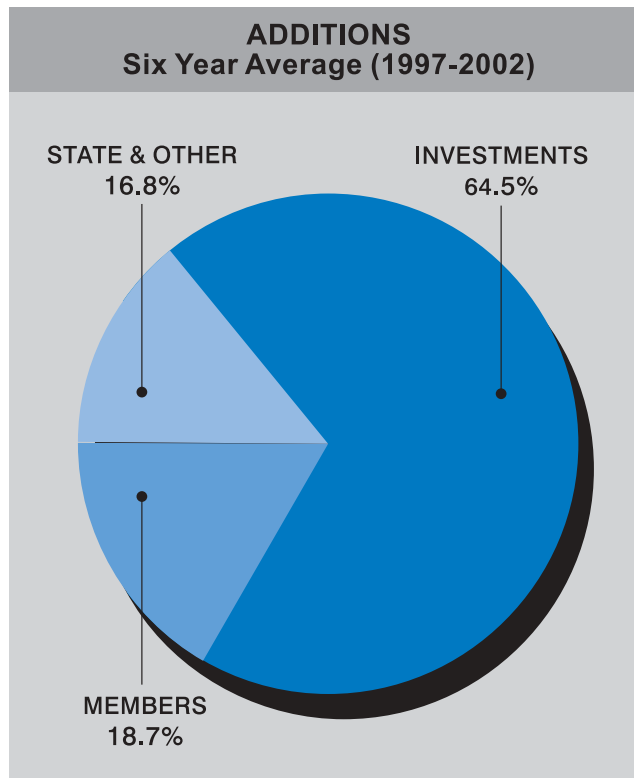
## Changes in Fiduciary Net Assets

### PENSION TRUST FUND

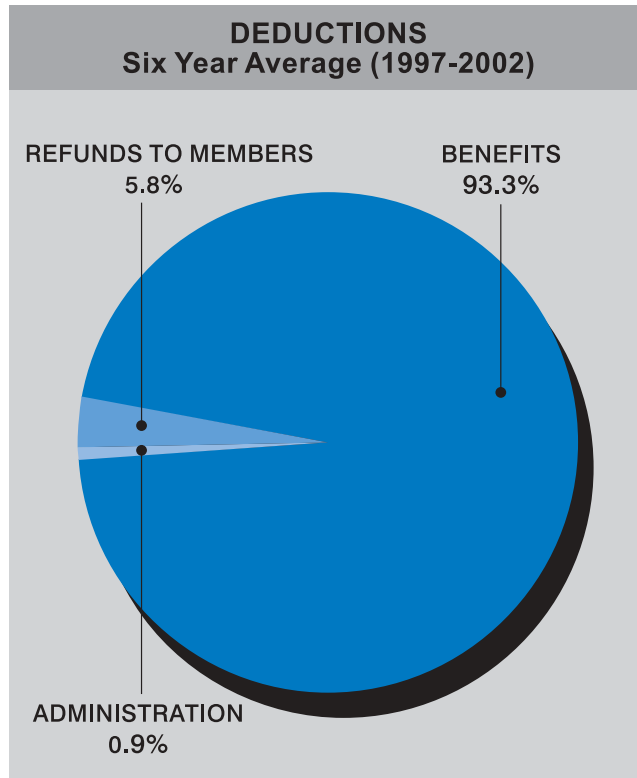
SUMMARY



|  | 2002                      | 2001                       |
|--|---------------------------|----------------------------|
| <b>Additions:</b>  |                           |                            |
| From Members   | \$ 1,560,700,102          | \$ 1,433,037,813           |
| From State   | 1,201,948,321             | 1,143,109,908              |
| From Reporting Employers   | 157,781,530               | 136,247,871                |
| From Investments:  |                           |                            |
| Investment Income  | 2,416,466,898             | 2,713,579,401              |
| Net Appreciation (Depreciation) in Fair Value                            | (8,477,880,514)           | (12,070,530,812)           |
| From Employees Retirement System   | 3,091,464                 | 2,068,339                  |
| From Other Sources   | 491                       | 6,733                      |
| <b>TOTAL ADDITIONS</b>   | <b>\$ (3,137,891,708)</b> | <b>\$ (6,642,480,747)</b>  |
| <b>Deductions:</b>   |                           |                            |
| For Benefits   | \$ 4,344,946,459          | \$ 3,649,116,654           |
| For Refunds to Members   | 186,421,065               | 214,434,792                |
| For Administration   | 37,519,032                | 32,648,006                 |
| For Employees Retirement System  | 24,183,510                | 20,663,196                 |
| <b>TOTAL DEDUCTIONS</b>  | <b>\$ 4,593,070,066</b>   | <b>\$ 3,916,862,648</b>    |
| <b>Net Increase (Decrease)</b>   | <b>\$ (7,730,961,774)</b> | <b>\$ (10,559,343,395)</b> |
| <b>Net Assets Held in Trust for Pension Benefits - Beginning of Year</b> | <b>79,427,814,814</b>     | <b>89,987,158,209</b>      |
| <b>Restatements</b>  | <b>(1,050,679)</b>        |                            |
| <b>Beginning of Year, As Restated</b>                                    | <b>\$ 79,426,764,135</b>  | <b>\$ 89,987,158,209</b>   |
| <b>Net Assets Held in Trust for Pension Benefits - End of Year</b>       | <b>\$ 71,695,802,361</b>  | <b>\$ 79,427,814,814</b>   |



| 2000                     | 1999                     | 1998                     | 1997                     |
|--------------------------|--------------------------|--------------------------|--------------------------|
| \$ 1,357,940,313         | \$ 1,221,288,036         | \$ 1,147,729,936         | \$ 1,070,235,761         |
| 1,092,217,514            | 1,004,017,265            | 958,268,679              | 895,085,344              |
| 119,060,600              | 108,892,209              | 91,478,817               | 86,940,233               |
| 2,835,498,681            | 2,553,133,610            | 2,479,035,112            | 2,255,862,387            |
| 8,278,136,788            | 11,441,848,248           | 2,333,003,731            | 10,171,242,898           |
| 1,686,990                | 1,108,401                | 914,620                  | 645,653                  |
| 15,101                   | 201,509                  | 45,753                   | 584                      |
| <b>\$ 13,684,555,987</b> | <b>\$ 16,330,489,278</b> | <b>\$ 7,010,476,648</b>  | <b>\$ 14,480,012,860</b> |
| \$ 3,344,798,735         | \$ 2,627,793,618         | \$ 2,494,214,045         | \$ 2,209,571,246         |
| 214,999,991              | 206,354,473              | 183,430,398              | 166,125,695              |
| 31,148,408               | 29,348,368               | 26,849,520               | 24,468,931               |
| 17,004,436               | 13,261,970               | 10,087,258               | 8,248,161                |
| <b>\$ 3,607,951,570</b>  | <b>\$ 2,876,758,429</b>  | <b>\$ 2,714,581,221</b>  | <b>\$ 2,408,414,033</b>  |
| <b>\$ 10,076,604,417</b> | <b>\$ 13,453,730,849</b> | <b>\$ 4,295,895,427</b>  | <b>\$ 12,071,598,827</b> |
| 79,910,553,792           | 66,456,822,943           | 62,160,927,516           | 50,089,328,689           |
| <b>\$ 79,910,553,792</b> | <b>\$ 66,456,822,943</b> | <b>\$ 62,160,927,516</b> | <b>\$ 50,089,328,689</b> |
| <b>\$ 89,987,158,209</b> | <b>\$ 79,910,553,792</b> | <b>\$ 66,456,822,943</b> | <b>\$ 62,160,927,516</b> |



## Changes in Fiduciary Net Assets

### HEALTH INSURANCE TRUST FUNDS

SUMMARY



|  | 2002                   | 2001                   |
|--|------------------------|------------------------|
| <b>RETIRED PLAN</b>  |                        |                        |
| <b>Additions:</b>  |                        |                        |
| Retiree Premiums   | \$ 143,797,748         | \$ 131,213,445         |
| State Contributions  | 380,307,062            | 166,400,568            |
| Member Contributions   | 47,378,092             | 45,059,393             |
| Investment Income:   |                        |                        |
| Interest   | 7,140,560              | 5,789,973              |
| Net Appreciation (Depreciation) in Fair Value                            |                        | 34,161                 |
| <b>TOTAL ADDITIONS</b>   | <b>\$ 578,623,462</b>  | <b>\$ 348,497,540</b>  |
| <b>Deductions:</b>   |                        |                        |
| Claims   | \$ 451,709,670         | \$ 390,466,745         |
| Claims Processing  | 16,828,256             | 16,017,167             |
| Internal Administration  | 2,163,441              | 2,220,596              |
| <b>TOTAL DEDUCTIONS</b>  | <b>\$ 470,701,367</b>  | <b>\$ 408,704,508</b>  |
| <b>Net Increase (Decrease)</b>   | <b>\$ 107,922,095</b>  | <b>\$ (60,206,968)</b> |
| <b>Net Assets Held in Trust for Health Insurance - Beginning of Year</b> | <b>(35,950,516)</b>    | <b>24,256,452</b>      |
| <b>Restatements</b>  | <b>(25,595)</b>        |                        |
| <b>Beginning of Year, As Restated</b>                                    | <b>\$ (35,976,111)</b> | <b>\$ 24,256,452</b>   |
| <b>Net Assets Held in Trust for Health Insurance - End of Year</b>       | <b>\$ 71,945,984</b>   | <b>\$ (35,950,516)</b> |
| <b>ACTIVE PLAN *</b>   |                        |                        |
| <b>Additions:</b>  |                        |                        |
| Membership Fees  | \$                     | \$                     |
| Active Premiums  |                        |                        |
| State Contributions  | 2,698,422              | 5,382                  |
| Administrative Fees  | 108,198                | 70,340                 |
| Investment Income:   |                        |                        |
| Interest   | 590,967                | 1,392,821              |
| Net Appreciation (Depreciation) in Fair Value                            |                        | 20,909                 |
| <b>TOTAL ADDITIONS</b>   | <b>\$ 3,397,587</b>    | <b>\$ 1,489,452</b>    |
| <b>Deductions:</b>   |                        |                        |
| Claims   | \$ (34,455)            | \$ 41,066              |
| Claims Processing  |                        | 92                     |
| Internal Administration  | 2,750,107              | 474,961                |
| <b>TOTAL DEDUCTIONS</b>  | <b>\$ 2,715,652</b>    | <b>\$ 516,119</b>      |
| <b>Net Increase</b>  | <b>\$ 681,935</b>      | <b>\$ 973,333</b>      |
| <b>Net Assets Held in Trust for Health Insurance - Beginning of Year</b> | <b>24,179,853</b>      | <b>23,206,520</b>      |
| <b>Restatements</b>  | <b>(6,196)</b>         |                        |
| <b>Beginning of Year, As Restated</b>                                    | <b>\$ 24,173,657</b>   | <b>\$ 23,206,520</b>   |
| <b>Net Assets Held in Trust for Health Insurance - End of Year</b>       | <b>\$ 24,855,592</b>   | <b>\$ 24,179,853</b>   |

\* Active Plan reserves were created by statute beginning September 1, 1994. Active Plan participation began in fiscal year 1997.

### Retired Plan (Six-Year Average 1997-2002)

| Additions           |       | Deductions              |       |
|---------------------|-------|-------------------------|-------|
| Retirees            | 36.8% | Claims                  | 95.0% |
| State               | 46.5% | Claims Processing       | 4.4%  |
| Members             | 13.3% | Internal Administration | 0.6%  |
| Investment Earnings | 3.4%  |                         |       |



| 2000            | 1999            | 1998            | 1997            |
|-----------------|-----------------|-----------------|-----------------|
| \$ 120,227,960  | \$ 96,474,107   | \$ 91,390,173   | \$ 87,657,784   |
| 85,505,637      | 76,488,424      | 72,210,190      | 67,616,395      |
| 42,738,069      | 38,244,213      | 36,105,095      | 33,808,197      |
| 6,775,986       | 10,893,741      | 14,399,195      | 16,125,973      |
| 147,499         | (1,131,000)     | 861,322         | 1,043,263       |
| \$ 255,395,151  | \$ 220,969,485  | \$ 214,965,975  | \$ 206,251,612  |
| \$ 313,933,218  | \$ 277,858,423  | \$ 232,794,071  | \$ 211,354,471  |
| 14,682,301      | 13,232,423      | 12,748,881      | 12,880,395      |
| 2,154,826       | 1,708,313       | 1,867,797       | 1,217,059       |
| \$ 330,770,345  | \$ 292,799,159  | \$ 247,410,749  | \$ 225,451,925  |
| \$ (75,375,194) | \$ (71,829,674) | \$ (32,444,774) | \$ (19,200,313) |
| 99,631,646      | 171,461,320     | 203,870,554     | 223,070,867     |
| \$ 99,631,646   | \$ 171,461,320  | \$ 203,870,554  | \$ 223,070,867  |
| \$ 24,256,452   | \$ 99,631,646   | \$ 171,425,780  | \$ 203,870,554  |
| \$ 152,001      | \$ 204,257      | \$ 548,119      | \$ 5,206,800    |
| 7,175           |                 |                 | 534,595         |
| 2,164           | 3,874           | 10,952          |                 |
| 1,425,548       | 1,108,460       | 1,126,333       | 1,605,147       |
| (20,840)        | (60,630)        | 91,362          | (30,801)        |
| \$ 1,566,048    | \$ 1,255,961    | \$ 1,776,766    | \$ 7,315,741    |
| \$ 142,569      | \$ 326,271      | \$ 1,107,287    | \$ 579,743      |
| 21,281          | 20,045          | 38,445          | 60,322          |
| 855,829         | 589,277         | 400,607         | 426,907         |
| \$ 1,019,679    | \$ 935,593      | \$ 1,546,339    | \$ 1,066,972    |
| \$ 546,369      | \$ 320,368      | \$ 230,427      | \$ 6,248,769    |
| 22,660,151      | 22,339,783      | 22,109,356      | 15,860,587      |
| \$ 22,660,151   | \$ 22,339,783   | \$ 22,109,356   | \$ 15,860,587   |
| \$ 23,206,520   | \$ 22,660,151   | \$ 22,339,783   | \$ 22,109,356   |

**Active Plan (Six-Year Average 1997-2002)**

| Additions           |       | Deductions              |       |
|---------------------|-------|-------------------------|-------|
| Investment Earnings | 43.1% | Claims                  | 27.7% |
| Active Premiums     | 8.6%  | Claims Processing       | 1.8%  |
| State Contributions | 16.1% | Internal Administration | 70.5% |
| Membership Fees     | 31.0% |                         |       |
| Administrative Fees | 1.2%  |                         |       |

# Participating Employers

## Community and Junior Colleges

Alamo Comm College Dist  
 Alvin Community College  
 Amarillo College  
 Angelina College  
 Austin Community College  
 Blinn College  
 Brazosport College  
 Central Texas College  
 Cisco Junior College  
 Clarendon College  
 Coastal Bend College  
 College of the Mainland  
 Collin Cty Comm College  
 Dallas Cty Comm Coll Dist  
 Del Mar College  
 El Paso Community College  
 Frank Phillips College  
 Galveston College  
 Grayson County College  
 Hill College  
 Houston Comm Coll System  
 Howard Cty Jr Coll Dist  
 Kilgore College  
 Laredo Community College  
 Lee College  
 McLennan Comm College  
 Midland College  
 N Harris Montgomery Cm Coll  
 Navarro College  
 North Central Tx College  
 Northeast Tx Comm College  
 Odessa College  
 Panola College  
 Paris Junior College  
 Ranger Junior College  
 San Jacinto College Dist  
 South Plains College  
 South Texas Comm College  
 Southwest Tx Jr College  
 Tarrant County Coll Dist  
 Temple College  
 Texarkana College  
 Texas Southmost College  
 Texas State Tech College  
 Trinity Valley Jr College  
 Tyler Junior College  
 Vernon College  
 Victoria College  
 Weatherford College  
 Western Texas College  
 Wharton County Jr College

## Universities

Angelo State University  
 Lamar Inst of Technology  
 Lamar St Coll at Orange  
 Lamar St Coll at Port Arthur  
 Lamar University  
 Midwestern State Univ  
 Prairie View A & M Univ  
 Sam Houston State Univ  
 Southwest Texas State U  
 Stephen F Austin State U  
 Sul Ross State University  
 Tarleton State University  
 Texas A & M at Galveston  
 Texas A & M Corpus Christi  
 Texas A & M U-Commerce  
 Texas A & M U-Kingsville  
 Texas A & M U-Texarkana  
 Texas A & M University  
 Texas Ag Exp Station  
 Texas Ag Ext Service  
 Texas Eng Exp Station  
 Texas Eng Ext Service

Texas Forest Service  
 Texas Southern University  
 Texas State Univ System  
 Texas Tech University  
 Texas Transportation Inst  
 Texas Womans University  
 Tx A & M International Univ  
 Tx A & M U Systems Office  
 U H at Houston  
 U of N Texas System Admin  
 U T at Arlington  
 U T at Austin  
 U T at Dallas  
 U T at El Paso  
 U T at San Antonio  
 U T at Tyler  
 U T Pan American  
 U T Permian Basin  
 Univ Tx at Brownsville  
 University of North Tx  
 West Texas A & M Univ

## Medical Schools

T A M U System H S C  
 U N T H S C at Fort Worth  
 U T H S C at Houston  
 U T H S C at San Antonio  
 U T Health Ctr at Tyler  
 U T M D Anderson Hospital  
 U T Med Br at Galveston  
 U T S W Medical Center

## School Districts

Abbott I S D  
 Abernathy I S D  
 Abilene I S D  
 Academy I S D  
 Adrian I S D  
 Agua Dulce I S D  
 Alamo Heights I S D  
 Alba Golden I S D  
 Albany I S D  
 Aldine I S D  
 Aledo I S D  
 Alice I S D  
 Alief I S D  
 Allen I S D  
 Allison I S D  
 Alpine I S D  
 Alto I S D  
 Alvarado I S D  
 Alvin I S D  
 Alvord I S D  
 Amarillo I S D  
 Amherst I S D  
 Anahuac I S D  
 Anderson Shiro Cons I S D  
 Andrews I S D  
 Angleton I S D  
 Anna I S D  
 Anson I S D  
 Anthony I S D  
 Anton I S D  
 Apple Springs I S D  
 Aquilla I S D  
 Aransas County I S D  
 Aransas Pass I S D  
 Archer City I S D  
 Argyle I S D  
 Arlington I S D  
 Arp I S D  
 Aspermont I S D  
 Athens I S D  
 Atlanta I S D  
 Aubrey I S D  
 Austin I S D  
 Austwell Tivoli I S D

Avalon I S D  
 Avery I S D  
 Avinger I S D  
 Axtell I S D  
 Azle I S D  
 Baird I S D  
 Ballinger I S D  
 Balmorhea I S D  
 Bandera I S D  
 Bangs I S D  
 Banquete I S D  
 Barbers Hill I S D  
 Bartlett I S D  
 Bastrop I S D  
 Bay City I S D  
 Beaumont I S D  
 Beckville I S D  
 Beeville I S D  
 Bellevue I S D  
 Bells I S D  
 Bellville I S D  
 Belton I S D  
 Ben Bolt Palito I S D  
 Benavides I S D  
 Benjamin I S D  
 Big Sandy I S D, Big Sandy  
 Big Sandy I S D, Dallardsville  
 Big Spring I S D  
 Birdville I S D  
 Bishop Cons I S D  
 Blackwell I S D  
 Blanco I S D  
 Bland I S D  
 Blanket I S D  
 Bloomburg I S D  
 Blooming Grove I S D  
 Bloomington I S D  
 Blue Ridge I S D  
 Bluff Dale I S D  
 Blum I S D  
 Boerne I S D  
 Boles I S D  
 Boling I S D  
 Bonham I S D  
 Booker I S D  
 Borden County I S D  
 Borger I S D  
 Bosqueville I S D  
 Bovina I S D  
 Bowie I S D  
 Boyd I S D  
 Boys Ranch I S D  
 Brackett I S D  
 Brady I S D  
 Brazos I S D  
 Brazosport I S D  
 Breckenridge I S D  
 Bremond I S D  
 Brenham I S D  
 Bridge City I S D  
 Bridgeport I S D  
 Broaddus I S D  
 Brock I S D  
 Bronte I S D  
 Brookeland I S D  
 Brooks County I S D  
 Brookesmith I S D  
 Brownfield I S D  
 Brownsboro I S D  
 Brownsville I S D  
 Brownwood I S D  
 Bruceville Eddy I S D  
 Bryan I S D  
 Bryson I S D  
 Buckholts I S D  
 Buena Vista I S D  
 Buffalo I S D  
 Bullard I S D  
 Buna I S D  
 Burk Burnett I S D  
 Burkeville I S D

Burleson I S D  
 Burnet Cons I S D  
 Burton I S D  
 Bushland I S D  
 Byers I S D  
 Bynum Cons I S D  
 Caddo Mills I S D  
 Calallen I S D  
 Caldwell I S D  
 Calhoun County I S D  
 Callisburg I S D  
 Calvert I S D  
 Cameron I S D  
 Campbell I S D  
 Canadian I S D  
 Canton I S D  
 Canutillo I S D  
 Canyon I S D  
 Carlisle I S D  
 Carrizo Springs C I S D  
 Carroll I S D  
 Carrollton Farmers Branch I S D  
 Carthage I S D  
 Castleberry I S D  
 Cayuga I S D  
 Cedar Hill I S D  
 Celeste I S D  
 Celina I S D  
 Center I S D  
 Center Point I S D  
 Centerville I S D, Centerville  
 Centerville I S D, Groveton  
 Central I S D  
 Central Heights I S D  
 Channelview I S D  
 Channing I S D  
 Chapel Hill I S D, Mt. Pleasant  
 Chapel Hill I S D, Tyler  
 Charlotte I S D  
 Cherokee I S D  
 Chester I S D  
 Chico I S D  
 Childress I S D  
 Chillicothe I S D  
 Chilton I S D  
 China Spring I S D  
 Chireno I S D  
 Chisum I S D  
 Christoval I S D  
 Cisco I S D  
 City View I S D  
 Clarendon Cons I S D  
 Clarksville I S D  
 Claude I S D  
 Clear Creek I S D  
 Cleburne I S D  
 Cleveland I S D  
 Clifton I S D  
 Clint I S D  
 Clyde I S D  
 Coahoma I S D  
 Coldspring Oakhurst I S D  
 Coleman I S D  
 College Station I S D  
 Collinsville I S D  
 Colmesneil I S D  
 Colorado I S D  
 Columbia Brazoria I S D  
 Columbus I S D  
 Comal I S D  
 Comanche I S D  
 Comfort I S D  
 Commerce I S D  
 Community I S D  
 Como Pickton I S D  
 Comstock I S D  
 Connally Cons I S D  
 Conroe I S D  
 Coolidge I S D  
 Cooper I S D  
 Coppel I S D

|                             |                           |                               |                           |
|-----------------------------|---------------------------|-------------------------------|---------------------------|
| Copperas Cove I S D         | Edna I S D                | Graham I S D                  | Iidalou I S D             |
| Corpus Christi I S D        | El Campo I S D            | Granbury I S D                | Industrial I S D          |
| Corrigan Camden C I S D     | El Paso I S D             | Grand Prairie I S D           | Ingleside I S D           |
| Corsicana I S D             | Electra I S D             | Grand Saline I S D            | Ingram I S D              |
| Cotton Center I S D         | Elgin I S D               | Grandfalls Royalty I S D      | Iola I S D                |
| Cotulla I S D               | Elkhart I S D             | Grandview I S D               | Iowa Park Cons I S D      |
| Coupland I S D              | Elysian Fields I S D      | Grandview Hopkins I S D       | Ira I S D                 |
| Covington I S D             | Ennis I S D               | Granger I S D                 | Iraan Sheffield I S D     |
| Crandall I S D              | Era I S D                 | Grape Creek I S D             | Iredell I S D             |
| Crane I S D                 | Etoile I S D              | Grapeland I S D               | Irion County I S D        |
| Cranfills Gap I S D         | Eula I S D                | Grapevine Colleyville ISD     | Irving I S D              |
| Crawford I S D              | Eustace I S D             | Greenville I S D              | Italy I S D               |
| Crockett Cty School Dist    | Evadale I S D             | Greenwood I S D               | Itasca I S D              |
| Crosby I S D                | Evant I S D               | Gregory Portland C I S D      | Jacksboro I S D           |
| Crosbyton Cons I S D        | Everman I S D             | Groesbeck I S D               | Jacksonville I S D        |
| Cross Plains I S D          | Excelsior I S D           | Groom I S D                   | Jarrell I S D             |
| Cross Roads I S D           | Ezzell I S D              | Groveton I S D                | Jasper I S D              |
| Crowell Cons I S D          | Fabens I S D              | Gruver I S D                  | Jayton-Girard I S D       |
| Crowley I S D               | Fairfield I S D           | Gunter I S D                  | Jefferson I S D           |
| Crystal City I S D          | Falls City I S D          | Gustine I S D                 | Jim Hogg County I S D     |
| Cuero I S D                 | Fannindel I S D           | Guthrie C S D                 | Jim Ned Cons I S D        |
| Culberson County I S D      | Farmersville I S D        | Hale Center I S D             | Joaquin I S D             |
| Cumby I S D                 | Farwell I S D             | Hallettsville I S D           | Johnson City I S D        |
| Cushing I S D               | Fayetteville I S D        | Hallsburg I S D               | Johnsonboro I S D         |
| Cypress Fairbanks I S D     | Ferris I S D              | Hallsville I S D              | Joshua I S D              |
| D Hanis I S D               | Flatonia I S D            | Hamilton I S D                | Jourdanton I S D          |
| Daingerfield I S D          | Florence I S D            | Hamlin I S D                  | Judson I S D              |
| Dalhart I S D               | Floresville I S D         | Hamshire Fannett I S D        | Junction I S D            |
| Dallas I S D                | Flour Bluff I S D         | Happy I S D                   | Karnack I S D             |
| Damon I S D                 | Floydada I S D            | Hardin I S D                  | Karnes City I S D         |
| Danbury I S D               | Follett I S D             | Hardin Jefferson I S D        | Katy I S D                |
| Darrouzett I S D            | Forestburg I S D          | Harlandale I S D              | Kaufman I S D             |
| Dawson I S D, Dawson        | Forney I S D              | Harleton I S D                | Keene I S D               |
| Dawson I S D, Welch         | Forsan I S D              | Harlingen I S D               | Keller I S D              |
| Dayton I S D                | Fort Bend I S D           | Harmony I S D                 | Kelton I S D              |
| De Kalb I S D               | Fort Davis I S D          | Harper I S D                  | Kemp I S D                |
| De Leon I S D               | Fort Elliott Cons I S D   | Harrold I S D                 | Kendleton I S D           |
| De Soto I S D               | Fort Hancock I S D        | Hart I S D                    | Kenedy I S D              |
| Decatur I S D               | Fort Sam Houston I S D    | Hartley I S D                 | Kenedy County School Dist |
| Deer Park I S D             | Fort Stockton I S D       | Harts Bluff I S D             | Kennard I S D             |
| Del Valle I S D             | Fort Worth I S D          | Haskell I S D                 | Kennedale I S D           |
| Dell City I S D             | Franklin I S D            | Hawkins I S D                 | Kerens I S D              |
| Denison I S D               | Frankston I S D           | Hawley I S D                  | Kermit I S D              |
| Denton I S D                | Fredericksburg I S D      | Hays Cons I S D               | Kerrville I S D           |
| Denver City I S D           | Freer I S D               | Hearne I S D                  | Kilgore I S D             |
| Detroit I S D               | Frenship I S D            | Hedley I S D                  | Killeen I S D             |
| Devers I S D                | Friendswood I S D         | Hemphill I S D                | Kingsville I S D          |
| Devine I S D                | Friona I S D              | Hempstead I S D               | Kirbyville Cons I S D     |
| Dew I S D                   | Frisco I S D              | Henderson I S D               | Klein I S D               |
| Deweyville I S D            | Frost I S D               | Henrietta I S D               | Klondike I S D            |
| Diboll I S D                | Fruitvale I S D           | Hereford I S D                | Knippa I S D              |
| Dickinson I S D             | Gainesville I S D         | Hermleigh I S D               | Knox City O Brien C I S D |
| Dilley I S D                | Galena Park I S D         | Hico I S D                    | Kopperl I S D             |
| Dime Box I S D              | Galveston I S D           | Hidalgo I S D                 | Kountze I S D             |
| Dimmitt I S D               | Ganado I S D              | Higgins I S D                 | Kress I S D               |
| Divide I S D                | Garland I S D             | High Island I S D             | Krum I S D                |
| Dodd City I S D             | Garner I S D              | Highland I S D                | La Feria I S D            |
| Donna I S D                 | Garrison I S D            | Highland Park I S D, Amarillo | La Gloria I S D           |
| Doss Cons C S D             | Gary I S D                | Highland Park I S D, Dallas   | La Grange I S D           |
| Douglass I S D              | Gatesville I S D          | Hillsboro I S D               | La Joya I S D             |
| Dripping Springs I S D      | Gause I S D               | Hitchcock I S D               | La Marque I S D           |
| Driscoll I S D              | George West I S D         | Holland I S D                 | La Porte I S D            |
| Dublin I S D                | Georgetown I S D          | Holliday I S D                | La Poyner I S D           |
| Dumas I S D                 | Gholson I S D             | Hondo I S D                   | La Pryor I S D            |
| Duncanville I S D           | Giddings I S D            | Honey Grove I S D             | La Vega I S D             |
| Eagle Mount Saginaw I S D   | Gilmer I S D              | Hooks I S D                   | La Vernia I S D           |
| Eagle Pass I S D            | Gladewater Cty Line I S D | Houston I S D                 | La Villa I S D            |
| Eanes I S D                 | Glasscock County I S D    | Howe I S D                    | Lackland I S D            |
| Early I S D                 | Glen Rose I S D           | Hubbard I S D, Hubbard        | Lago Vista I S D          |
| East Bernard I S D          | Godley I S D              | Hubbard I S D, New Boston     | Lake Dallas I S D         |
| East Central I S D          | Goldburg I S D            | Huckabay I S D                | Lake Travis I S D         |
| East Chambers I S D         | Goldthwaite I S D         | Hudson I S D                  | Lake Worth I S D          |
| Eastland I S D              | Goliad I S D              | Huffman I S D                 | Lamar Cons I S D          |
| Ector I S D                 | Gonzales I S D            | Hughes Springs I S D          | Lamesa I S D              |
| Ector Cty I S D             | Goodrich I S D            | Hull Daisetta I S D           | Lampasas I S D            |
| Edcouch Elsa I S D          | Goose Creek I S D         | Humble I S D                  | Lancaster I S D           |
| Eden C I S D                | Gordon I S D              | Hunt I S D                    | Laneville I S D           |
| Edgewood I S D, Edgewood    | Goree I S D               | Huntington I S D              | Laredo I S D              |
| Edgewood I S D, San Antonio | Gorman I S D              | Huntsville I S D              | Lasara I S D              |
| Edinburg C I S D            | Grady I S D               | Hurst Euless I S D            | Latexo I S D              |
|                             | Graford I S D             | Hutto I S D                   | Lazbuddie I S D           |

# Participating Employers

(continued)

|                           |                              |                                |                          |
|---------------------------|------------------------------|--------------------------------|--------------------------|
| Leakey I S D              | Medina I S D                 | O Donnell I S D                | Red Lick I S D           |
| Leander I S D             | Medina Valley I S D          | Oakwood I S D                  | Red Oak I S D            |
| Leary I S D               | Megargel I S D               | Odem Edroy I S D               | Redwater I S D           |
| Lefors I S D              | Melissa I S D                | Oglesby I S D                  | Refugio I S D            |
| Leggett I S D             | Memphis I S D                | Olfen I S D                    | Ricardo I S D            |
| Leon I S D                | Menard I S D                 | Olney I S D                    | Rice I S D               |
| Leonard I S D             | Mercedes I S D               | Olton I S D                    | Rice Cons I S D          |
| Levelland I S D           | Meridian I S D               | Onalaska I S D                 | Richards I S D           |
| Leveretts Chapel I S D    | Merkel I S D                 | Orange Grove I S D             | Richardson I S D         |
| Lewisville I S D          | Mesquite I S D               | Orangefield I S D              | Richland Springs I S D   |
| Lexington I S D           | Mexia I S D                  | Ore City I S D                 | Riesel I S D             |
| Liberty I S D             | Meyersville I S D            | Overton I S D                  | Rio Grande City C I S D  |
| Liberty Eylau I S D       | Miami I S D                  | Paducah I S D                  | Rio Hondo I S D          |
| Liberty Hill I S D        | Midland I S D                | Paint Creek I S D              | Rio Vista I S D          |
| Lindale I S D             | Midlothian I S D             | Paint Rock I S D               | Rising Star I S D        |
| Linden Kildare Cons I S D | Midway I S D, Henrietta      | Palacios I S D                 | River Road I S D         |
| Lindsay I S D             | Midway I S D, Waco           | Palestine I S D                | Rivercrest ISD           |
| Lingleville I S D         | Milano I S D                 | Palmer I S D                   | Riviera I S D            |
| Lipan I S D               | Mildred I S D                | Palo Pinto I S D               | Robert Lee I S D         |
| Little Elm I S D          | Miles I S D                  | Pampa I S D                    | Robinson I S D           |
| Littlefield I S D         | Millford I S D               | Panhandle I S D                | Robstown I S D           |
| Livingston I S D          | Miller Grove I S D           | Panther Creek Cons I S D       | Roby C I S D             |
| Llano I S D               | Millsap I S D                | Paradise I S D                 | Rochelle I S D           |
| Lockhart I S D            | Mineola I S D                | Paris I S D                    | Rochester I S D          |
| Lockney I S D             | Mineral Wells I S D          | Pasadena I S D                 | Rockdale I S D           |
| Lohn I S D                | Mirando City I S D           | Patton Springs I S D           | Rocksprings I S D        |
| Lometa I S D              | Mission Cons I S D           | Pawnee I S D                   | Rockwall I S D           |
| London I S D              | Monahans Wickett I S D       | Pearland I S D                 | Rogers I S D             |
| Lone Oak I S D            | Montague I S D               | Pearsall I S D                 | Roma I S D               |
| Longview I S D            | Monte Alto I S D             | Peaster I S D                  | Roosevelt I S D          |
| Loop I S D                | Montgomery I S D             | Pecos Barstow Toyah I S D      | Ropes I S D              |
| Lorraine I S D            | Moody I S D                  | Penelope I S D                 | Roscoe I S D             |
| Lorena I S D              | Moran I S D                  | Perrin Whitt Cons I S D        | Rosebud Lott Cons I S D  |
| Lorenzo Cons I S D        | Morgan I S D                 | Perryton I S D                 | Rotan I S D              |
| Los Fresnos Cons I S D    | Morgan Mill I S D            | Petersburg I S D               | Round Rock I S D         |
| Louise I S D              | Morton I S D                 | Petrolia I S D                 | Round Top Carmine I S D  |
| Lovejoy I S D             | Motley County I S D          | Pettus I S D                   | Roxton I S D             |
| Lovelady I S D            | Moulton I S D                | Pewitt Cons I S D              | Royal I S D              |
| Ltle Cyprs Mrcvle C I S D | Mount Calm I S D             | Pflugerville I S D             | Royse City I S D         |
| Lubbock I S D             | Mount Enterprise I S D       | Pharr San Juan Alamo ISD       | Rule I S D               |
| Lubbock Cooper I S D      | Mount Pleasant I S D         | Pilot Point I S D              | Runge I S D              |
| Lueders Avoca I S D       | Mount Vernon I S D           | Pine Tree I S D                | Rusk ISD                 |
| Luffkin I S D             | Muenster I S D               | Pittsburg I S D                | S & S Cons I S D         |
| Luling I S D              | Muleshoe I S D               | Plains I S D                   | Sabinal I S D            |
| Lumberton I S D           | Mullin I S D                 | Plainview I S D                | Sabine I S D             |
| Lynford Cons I S D        | Mumford I S D                | Plano I S D                    | Sabine Pass I S D        |
| Lytile I S D              | Munday I S D                 | Pleasant Grove I S D           | Saint Jo I S D           |
| Mabank I S D              | Murchison I S D              | Pleasanton I S D               | Salado I S D             |
| Madisonville Cons I S D   | Nacogdoches I S D            | Plemons Stinnett Phillips CISD | Saltillo I S D           |
| Magnolia I S D            | Natalia I S D                | Point Isabel I S D             | Sam Rayburn Cons I S D   |
| Malakoff I S D            | Navarro I S D                | Ponder I S D                   | Samnorwood I S D         |
| Malone I S D              | Navasota I S D               | Poolville I S D                | San Angelo I S D         |
| Malta I S D               | Nazareth I S D               | Port Aransas I S D             | San Antonio I S D        |
| Manor I S D               | Neches I S D                 | Port Arthur I S D              | San Augustine I S D      |
| Mansfield I S D           | Nederland I S D              | Port Neches Groves I S D       | San Benito Cons I S D    |
| Marathon I S D            | Needville I S D              | Post I S D                     | San Diego I S D          |
| Marble Falls I S D        | New Boston I S D             | Poteet I S D                   | San Elizario I S D       |
| Marfa I S D               | New Braunfels I S D          | Poth Cons I S D                | San Felipe Del Rio I S D |
| Marietta I S D            | New Caney I S D              | Pottsboro I S D                | San Isidro I S D         |
| Marion I S D              | New Deal I S D               | Prairie Lea I S D              | San Marcos Cons I S D    |
| Marlin I S D              | New Diana I S D              | Prairie Valley I S D           | San Perlita I S D        |
| Marshall I S D            | New Home I S D               | Prairiland I S D               | San Saba I S D           |
| Mart I S D                | New Summerfield I S D        | Premont I S D                  | San Vicente I S D        |
| Martins Mill I S D        | New Waverly I S D            | Presidio I S D                 | Sands Cons I S D         |
| Martinsville I S D        | Newcastle I S D              | Priddy I S D                   | Sanford I S D            |
| Mason I S D               | Newton I S D                 | Princeton I S D                | Sanger I S D             |
| Masonic Home I S D        | Nixon Smiley C I S D         | Pringle Morse Cons I S D       | Santa Anna I S D         |
| Matagorda I S D           | Nocona I S D                 | Progreso I S D                 | Santa Fe I S D           |
| Mathis I S D              | Nordheim I S D               | Prosper I S D                  | Santa Gertrudis I S D    |
| Maud I S D                | Normangee I S D              | Quanah I S D                   | Santa Maria I S D        |
| May I S D                 | North East I S D             | Queen City I S D               | Santa Rosa I S D         |
| Maypearl I S D            | North Forest I S D           | Quinlan I S D                  | Santo I S D              |
| Mc Allen I S D            | North Hopkins I S D          | Quitman I S D                  | Savoy I S D              |
| Mc Camey I S D            | North Lamar I S D            | Rains I S D                    | Schertz Cibolo I S D     |
| Mc Dade I S D             | North Zulch I S D            | Ralls I S D                    | Schleicher Cty I S D     |
| Mc Gregor I S D           | Northside I S D, San Antonio | Ramirez Common S D             | Schulenburg I S D        |
| Mc Kinney I S D           | Northside I S D, Vernon      | Randolph Field I S D           | Scurry Rosser I S D      |
| Mc Lean I S D             | Northwest I S D              | Ranger I S D                   | Seagraves I S D          |
| Mc Leod I S D             | Novice I S D                 | Rankin I S D                   | Sealy I S D              |
| Mc Mullen County I S D    | Nueces Canyon Cons I S D     | Raymondville I S D             | Seguin I S D             |
| Meadow I S D              | Nursery I S D                | Reagan County I S D            | Seminole Public Schools  |

Seymour I S D  
 Shallowater I S D  
 Shamrock I S D  
 Sharyland I S D  
 Shelbyville I S D  
 Sheldon I S D  
 Shepherd I S D  
 Sherman I S D  
 Shiner I S D  
 Sidney I S D  
 Sierra Blanca I S D  
 Silsbee I S D  
 Silverton I S D  
 Simms I S D  
 Sinton I S D  
 Sivells Bend I S D  
 Skidmore Tynan I S D  
 Slaton I S D  
 Slidell I S D  
 Slocum I S D  
 Smithville I S D  
 Smyer I S D  
 Snook I S D  
 Snyder I S D  
 Socorro I S D  
 Somerset I S D  
 Somerville I S D  
 Sonora I S D  
 South San Antonio I S D  
 South Texas I S D  
 Southland I S D  
 Southside I S D  
 Southwest I S D  
 Spade I S D  
 Spearman I S D  
 Splendora I S D  
 Spring I S D  
 Spring Branch I S D  
 Spring Creek I S D  
 Spring Hill I S D  
 Springlake Earth I S D  
 Springtown I S D  
 Spur I S D  
 Spurger I S D  
 Stafford Muncpl Sch Dist  
 Stamford I S D  
 Stanton I S D  
 Star I S D  
 Stephenville I S D  
 Sterling City I S D  
 Stockdale I S D  
 Stratford I S D  
 Strawn I S D  
 Sudan I S D  
 Sulphur Bluff I S D  
 Sulphur Springs I S D  
 Sundown I S D  
 Sunnyvale I S D  
 Sunray I S D  
 Sweeny I S D  
 Sweet Home I S D  
 Sweetwater I S D  
 Taft I S D  
 Tahoka I S D  
 Tarkington I S D  
 Tatum I S D  
 Taylor I S D  
 Teague I S D  
 Temple I S D  
 Tenaha I S D  
 Terlingua C S D  
 Terrell I S D  
 Terrell County I S D  
 Texarkana I S D  
 Texas City I S D  
 Texhoma I S D  
 Texline I S D  
 Thorndale I S D  
 Thrall I S D  
 Three Rivers I S D  
 Three Way I S D, Maple

Three Way I S D, Stephenville  
 Throckmorton I S D  
 Tidehaven I S D  
 Timpson I S D  
 Tioga I S D  
 Tolar I S D  
 Tom Bean I S D  
 Tomball I S D  
 Tornillo I S D  
 Trent I S D  
 Trenton I S D  
 Trinidad I S D  
 Trinity I S D  
 Troup I S D  
 Troy I S D  
 Tulia I S D  
 Tuloso Midway I S D  
 Turkey Quitaque C I S D  
 Tyler I S D  
 Union Grove I S D  
 Union Hill I S D  
 United I S D  
 Utopia I S D  
 Uvalde Cons I S D  
 Valentine I S D  
 Valley Mills I S D  
 Valley View I S D, Pharr  
 Valley View I S D, Valley View  
 Van I S D  
 Van Alstyne I S D  
 Van Vleck I S D  
 Vega I S D  
 Venus I S D  
 Veribest I S D  
 Vernon Cons I S D  
 Victoria I S D  
 Vidor I S D  
 Vysehrad I S D  
 Waco I S D  
 Waelder I S D  
 Walcott I S D  
 Wall I S D  
 Waller I S D  
 Walnut Bend I S D  
 Walnut Springs I S D  
 Warren I S D  
 Waskom I S D  
 Water Valley I S D  
 Waxahachie I S D  
 Weatherford I S D  
 Webb C I S D  
 Weimar I S D  
 Wellington I S D  
 Wellman Union I S D  
 Wells I S D  
 Weslaco I S D  
 West I S D  
 West Hardin Cty C I S D  
 West Orange Cove C I S D  
 West Oso I S D  
 West Rusk Cty Cons I S D  
 West Sabine I S D  
 Westbrook I S D  
 Westhoff I S D  
 Westphalia I S D  
 Westwood I S D  
 Wharton I S D  
 Wheeler I S D  
 White Deer I S D  
 White Oak I S D  
 White Settlement I S D  
 Whiteface I S D  
 Whitehouse I S D  
 Whitesboro I S D  
 Whitewright I S D  
 Whitharral I S D  
 Whitney I S D  
 Wichita Falls I S D  
 Wildorado I S D  
 Willis I S D  
 Wills Point I S D

Wilmer Hutchins I S D  
 Wilson I S D  
 Wimberley I S D  
 Windham School District  
 Windthorst I S D  
 Winfield I S D  
 Wink Loving Cons I S D  
 Winnsboro I S D  
 Winona I S D  
 Winters I S D  
 Woden I S D  
 Wolfe City I S D  
 Woodsboro I S D  
 Woodson I S D  
 Woodville I S D  
 Wortham I S D  
 Wylie I S D, Abilene  
 Wylie I S D, Wylie  
 Yantis I S D  
 Yoakum I S D  
 Yorktown I S D  
 Ysleta I S D  
 Zapata I S D  
 Zavalla I S D  
 Zephyr I S D

Cedar Crest Charter Sch  
 Cedar Ridge Charter Sch  
 Cedars International Acad  
 Children First Ac Houston  
 Children First Ele Acad  
 Coastal Bend Youth C C S  
 Com Quest Academy  
 Cross Roads Charter  
 Dallas Can Academy  
 Dallas Comm Charter Sch  
 Dr. Garza-Gonzalez Ch Sch  
 Eagle Advantage School  
 Eagle Charter Abilene  
 Eagle Charter Beaumont  
 Eagle Charter Brownsville  
 Eagle Charter Bryan  
 Eagle Charter Dallas  
 Eagle Charter Del Rio  
 Eagle Charter Fort Worth  
 Eagle Charter Laredo  
 Eagle Charter Lubbock  
 Eagle Charter McAllen  
 Eagle Charter Midland  
 Eagle Charter San Antonio  
 Eagle Charter Texarkana  
 Eagle Charter Tyler  
 Eagle Charter Waco  
 East Texas Charter School  
 Eden Park Academy  
 Education Center Int Acad  
 El Paso Academy East  
 El Paso School Excellence  
 Erath Excels! Academy  
 Faith Family Acad Oak Cl  
 Faith Fam Acad Waxahachie  
 Focus Learning Academy  
 Fruit of Excellence Sch  
 Ft Worth Acad Fine Arts  
 Gabriel Tafolla Charter  
 Gateway Academy  
 Gateway Charter Academy  
 George Gervin Academy  
 George I Sanchez Charter  
 Girls & Boys Prep Acad  
 Guardian Angel Academy  
 Gulf Coast Trades Center  
 Gulf Shores Academy  
 Harmony Science Academy  
 Heights Academy  
 Higgs Carter King Academy  
 Honors Academy  
 Houston Alt Prep Charter  
 Houston Hgts Learning Ac  
 I Am That I Am Academy  
 Idea Academy  
 Impact Charter School  
 Inspired Vision Academy  
 Jamie's House Charter Sch  
 Jean Massieu Academy  
 Jesse Jackson Academy  
 John H.Wood Charter Sch  
 Jubilee Academics Center  
 Katherine Anne Porter Sch  
 Kenny Dorham School  
 K I P P Academy  
 La Amistad Academy  
 La Escuela Delas Americas  
 Life Charter School  
 Mainland Prep Academy  
 Medical Center Charter  
 Metro Charter Academy  
 Mid Valley Academy  
 N Houston H S Business  
 Nancy Ney Charter School  
 Nova Charter Southeast  
 Nova School  
 Northwest Prep Academy  
 NW Math Sci Lang Academy  
 N Y O S Charter School  
 Odyssey Academy  
 One Stop Multiservice

### Regional Service Centers

Region 01 Ed Serv Center  
 Region 02 Ed Serv Center  
 Region 03 Ed Serv Center  
 Region 04 Ed Serv Center  
 Region 05 Ed Serv Center  
 Region 06 Ed Serv Center  
 Region 07 Ed Serv Center  
 Region 08 Ed Serv Center  
 Region 09 Ed Serv Center  
 Region 10 Ed Serv Center  
 Region 11 Ed Serv Center  
 Region 12 Ed Serv Center  
 Region 13 Ed Serv Center  
 Region 14 Ed Serv Center  
 Region 15 Ed Serv Center  
 Region 16 Ed Serv Center  
 Region 17 Ed Serv Center  
 Region 18 Ed Serv Center  
 Region 19 Ed Serv Center  
 Region 20 Ed Serv Center

### Charter Schools

A+ Academy  
 Academy of Accelerated  
 Academy of Beaumont  
 Academy of Careers and Tech  
 Academy of Dallas  
 Academy of Houston  
 Accelerated Int Academy  
 Alief Montessori School  
 ALPHA Charter School  
 Alphonso Crutch's Charter  
 Am Acad of Excellence Hou  
 American Inst of Learning  
 Amigos Por Vida Charter  
 Arlington Classics Acad  
 A W Brown Flwshp Chtr Sch  
 Azleway Charter School  
 Bay Area Charter School  
 Beatrice Mayes Institute  
 Benji's Special Educ Acad  
 Bexar County Academy  
 Big Springs Charter Sch  
 Brazos River Charter Sch  
 Brazos School for Inquiry  
 Bright Ideas Charter Sch  
 Burnham Wood Charter Sch  
 Calvin Nelms Charter  
 Career Plus Learning Acad

## Participating Employers

(continued)

Panola Charter School  
 Paradigm Accelerated Sch  
 Paso Del Norte Academy  
 Pegasus Charter School  
 Phoenix Charter School  
 Pineywoods Academy  
 Por Vida Inc  
 Prepared Table  
 Radiance Acad of Learning  
 Ranch Academy  
 Rapoport Academy  
 Raul Yzaguirre School  
 Richard Milburn Acad C C  
 Richard Milburn - Amarillo  
 Richard Milburn - Beaumont  
 Richard Milburn - Killeen  
 Richard Milburn - Lubbock  
 Richard Milburn - Midland  
 Rise Academy  
 Rylie Faith Family Acad  
 S T A R Charter School  
 San Antonio Sch Inquiry  
 San Antonio Tech Academy  
 San Marcos Prep Academy  
 School of Excellence  
 Seashore Learning Ctr  
 Sentry Technology Prep  
 Ser-Ninos  
 Shekinah Radiance Academy  
 South Plains Academy  
 Southwest High School  
 Southwest Preparatory Sch  
 St. Mary's Charter School  
 Technology Education Chtr  
 T E K O A Academy  
 Texas Empowerment Academy  
 Texas Language Charter  
 Texas Serenity Academy  
 The Education Center  
 The Ehrhart School  
 The Encino School  
 The North Hills School  
 Theresa B Lee Academy  
 T O V A S  
 Transformative Charter  
 Treetops International  
 Twenty-first Century Academy  
 Two Dimensions Prep Acad  
 Tx Academy of Excellence  
 Tx Serenity Acad Bayshore  
 U of H Charter Sch Tech  
 Universal Academy  
 Valley High Charter Sch  
 Vanguard Academy  
 Varnett Charter School  
 Wa-Set Preparatory Acdmy  
 Waco Charter School  
 West Houston Charter  
 Winfree Academy  
 Yes College Prep  
 Zoe Learning Academy

## Other Entities

Teacher Retirement System  
 Texas Food & Fibers Comm

## Other Educational Districts

Anderson Cty Spc Ed Co Op  
 Austin Cty Ed Co Op  
 Bowie County Sch Dist  
 Co Op for Special Svcs  
 Dallas County School Dist  
 Harris Cty Dept Education  
 Houston Trinity Cty Co Op  
 Johnson Cty Spc Ed Co Op  
 Palacios Fd Mnpwr Pgm  
 Parker County Co Op  
 Small Schools Coop



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