# Duluth Teachers' Retirement Fund Association

## Duluth, Minnesota

DTRFA

# Annual Financial Report

## Fiscal Year Ended June 30, 2013

# DULUTH TEACHERS' RETIREMENT FUND ASSOCIATION

# ANNUAL FINANCIAL REPORT

# YEAR ENDED JUNE 30, 2013

**Report Prepared by:**
**J. Michael Stoffel**
**Ron Warner**

**Duluth Teachers' Retirement Fund Association**
**625 East Central Entrance**
**Duluth, Minnesota 55811**
**(218) 722-2894**

# Table of Contents

# Certificate of Achievement

Government Finance Officers Association

Certificate of Achievement for Excellence in Financial Reporting

Presented to

**Duluth Teachers' Retirement Fund Association Minnesota**

For its Comprehensive Annual Financial Report for the Fiscal Year Ended

**June 30, 2012**

Executive Director/CEO

# Letter of Transmittal

Duluth Teachers' Retirement Fund Association
DTRFA
625 East Central Entrance • Duluth, MN 55811
Phone: 218-722-2894 • Fax: 218-722-8208 • www.dtrfa.org
J. Michael Stoffel, Executive Director

December 27, 2013

Board of Trustees and Members of the Association
Duluth Teachers' Retirement Fund Association
625 East Central Entrance
Duluth, MN 55811

Dear Trustees and Members of the Association:

I am pleased to present this ***Annual Financial Report*** of the Duluth Teachers' Retirement Fund Association (DTRFA) for the fiscal year ended June 30, 2013. This report is intended to provide you with financial, investment, actuarial, and statistical information regarding the pension programs administered by the DTRFA. Responsibility for the accuracy and completeness of this report rests solely with the management and staff of the Association.

**History and Overview**

The DTRFA was established in 1910 to provide retirement coverage to eligible employees of the Duluth Public Schools. Eligible employees include the licensed, certified staff of Duluth Public Schools, certain staff at Lake Superior College hired prior to July 1, 1995 who elected to continue membership in the DTRFA, and DTRFA staff. Since 1964, the DTRFA also offers to Association members three tax deferred 403(b) investment funds through payroll deduction with the school district. The Association is governed by a nine-member Board of Trustees, which sets policy and oversees operations consistent with applicable laws. The Executive Director is the administrative officer for the Association.

There are several additional levels of oversight of the operations of the pension plan: the Office of the State Auditor conducts the annual financial and compliance audit and performs annual investment return analysis; WIPFLI, a local accounting firm, provides accounting consultation services and performs quarterly audit procedures; Jeffrey Slocum & Associates, the investment consultant for the Association, reports to the Board after each calendar quarter regarding investment performance and compliance with investment law and policy; The Segal Company prepares an actuarial valuation report each year to measure the actuarial soundness of the fund; the Legislative Commission on Pensions and Retirement conducts additional analysis and comparisons.

**Financial Information and Controls**

The financial statements have been prepared in conformity with Statement Number 25, Statement Number 40, Statement Number 50, and other generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board. The Office of the State Auditor has audited the financial statements. Their opinion is shown on page 8. An operating budget for administrative expenses is approved by the Board of Trustees each fiscal year. A system of internal controls is in place to provide reasonable assurance for the safekeeping of assets, the reliability of financial records, and to promote efficient operations. As in all internal control environments, there are inherent limitations. The Association's internal controls have been designed to reduce, though not eliminate, such limitations. The concept of reasonable assurance implies a high degree of assurance, constrained by the costs and benefits of establishing incremental control procedures. A summary of financial highlights, an overview of the financial statements, and an analysis of net assets and related additions and deductions is presented in the management's discussion and analysis beginning on page 10.

**Investment Activities**

For the Pension Fund, the time-weighted rate of return net of all fees was 16.7% for the 12 months ended June 30, 2013, and 12.8% for the three-year period then ended. Both of these rates of return were in the top decile of all public pension funds in the USA. For the tax deferred 403(b) plan, net investment returns for the year were 24.9% in the Equity Fund, 1.2% in the Bond Fund, and 0.8% in the Money Market Fund. The three-year return in the tax deferred funds were 18.9% in the Equity Fund, 5.2% in the Bond Fund, and 0.7% in the Money Market Fund.

The Board of Trustees of the Association continues to pay close attention to the overall risk profile of the investment portfolio. The overriding investment philosophy followed at DTRFA continues to center on long held principles of diversification and the search for long-term value. This broad diversification is meant to protect the investment portfolio and dampen the day to day vagaries of the global financial markets. It is management's view that our long-term time horizon, the diversification of our holdings, and present opportunities to acquire securities at discounts to intrinsic value, position the investment portfolio to continue in its recovery as the economy improves.

**Funding and Financing Status**

An important measure of the health of a pension fund is the funding ratio. This ratio is the measure of total actuarial value of assets compared to total actuarial accrued liability. The higher the funding ratio, the greater the level of investment income potential. Additionally, a higher ratio gives members a greater degree of assurance that their pensions are secure. According to the actuarial valuation report for the year ended June 30, 2013, the pension plan had a funding ratio of 54% compared to a ratio of 63% the previous year-end. More detailed information and analysis of the funding and financing of the retirement plan is included in the management's discussion and analysis and in the actuarial section of this report.

**Legislation**

Significant legislation was passed in May 2013 to work in conjunction with the idea that the DTRFA may soon need to pursue a consolidation of the pension plan with the State Teachers Retirement Association (TRA). There are two leading reasons for this conclusion: 1) The crisis in the investment markets during fiscal years 2008 and 2009 left the pension plan with a significant unfunded liability; 2) The demographics of the pension plan have deteriorated to the point where there are almost twice as many people receiving monthly benefits from the plan as there are active contributing members. In order to prepare the plan for a potential merger, legislative action was taken to infuse a significant amount of state aid into the pension fund and move the benefit structure and other features of the DTRFA plan closer to that of the TRA. The legislation passed in 2013 changed the DTRFA benefit accrual rates and the contribution rates so that they are the same as the TRA. Having the same structure in the DTRFA and the TRA removes some of the difficulties that would otherwise arise when discussions begin regarding a merger of the two plans.

**National Recognition**

Finally, I am proud to announce that in 2013, the DTRFA received recognition from a national organization. The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the DTRFA for its comprehensive annual financial report for the fiscal year ended June 30, 2012. This was the seventeenth consecutive year the DTRFA has achieved this prestigious award. In order to be awarded a Certificate of Achievement, we must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one year only.

**Acknowledgments**

Each year in this paragraph I express my gratitude to the staff of the DTRFA, our advisors and consultants, and the many people who have worked so diligently to assure the successful operation and financial soundness of the Association. Those sentiments are again important, but I also wish to express how grateful I am to have had the opportunity to serve as your executive director for the last 22 years. It has been my pleasure to work for the active and retired members of the DTRFA. My time here has been very challenging professionally, and very rewarding and fulfilling. I am glad I have had the opportunity to contribute something in appreciation for the public school educators in our community who have played such an important role in my own family. As I prepare to depart for my next endeavor, I will take with me and cherish many memories of so many good people – the staff, the trustees, and the members of the DTRFA.

Sincerely yours,

J. Michael Stoffel

J. Michael Stoffel
Executive Director

# Board of Trustees

# Administrative Organization

## Administrative Staff

J. Michael Stoffel
*Executive Director*

Kim Remington
*Administrative Staff*

Kay Norris
*Retirement Technician*

Ron Warner
*Accountant*

## Professional Services

Best & Flanagan, LLP
*Legal Services*
Minneapolis, Minnesota

WIPFLi, LLP
*Accounting Consulting*
Duluth, Minnesota

Johnson, Killen & Seiler, P.A.
*Legal Services*
Duluth, Minnesota

Office of the State Auditor
*Auditing Services*
Duluth, Minnesota

Segal Company
*Actuarial Services*
Chicago, Illinois

## Investment Consultant

Jeffrey Slocum & Associates
Minneapolis, Minnesota

## Investment Advisors

Disciplined Growth Investors
Minneapolis, Minnesota

Permal Capital Management, LLC
Boston, Massachusetts

HarbourVest Partners, LLC
Boston, Massachusetts

Tweedy, Browne Company, LLC
Stamford, Connecticut

Western Asset Management Company
Pasadena, California

North Sky Capital
Minneapolis, Minnesota

The Vanguard Group
Valley Forge, Pennsylvania

Wellington Management Company
Boston, Massachusetts

Wells Fargo Bank, N.A.
Minneapolis, Minnesota

Blackrock, Inc.
Seattle, Washington

Pacific Investment Management Company
Newport Beach, California

William Blair & Company
Chicago, Illinois

# Independent Auditor's Report


**STATE OF MINNESOTA**
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SAINT PAUL, MN 55103-2139

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## INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Duluth Teachers' Retirement Fund Association

**Report on the Financial Statements**

We have audited the accompanying financial statements of the Duluth Teachers' Retirement Fund Association as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Association's basic financial statements, as listed in the table of contents.

***Management's Responsibility for the Financial Statements***
Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

***Auditor's Responsibility***
Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Association's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

***Opinion***
In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net position of the Duluth Teachers' Retirement Fund Association as of June 30, 2013, and the changes in plan net position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

***Other Matters***
*Required Supplementary Information*
Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Required Supplementary Information as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

*Supplementary and Other Information*
Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Duluth Teachers' Retirement Fund Association's basic financial statements. The introductory section, the other supplementary information, the investment section, the actuarial section, and the statistical section as listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The other supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

The introductory section, investment section, actuarial section, and statistical section have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

REBECCA OTTO
STATE AUDITOR

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

December 23, 2013

# Management's Discussion & Analysis

The following overview is a discussion and analysis of the financial activities of the Duluth Teachers' Retirement Fund Association (DTRFA) for the fiscal year ended June 30, 2013. Its purpose is to provide explanations and insights into the information in the financial statements, notes to the financial statements, and required supplementary information.

### Financial Highlights

- Net assets in the defined benefit plan, which represent funds available to pay current and future pension benefits, increased by $11 million during the fiscal year to $205 million. This 5.5% increase in net assets was primarily due to strong investment performance. Net assets in the defined contribution plan grew by $4.9 million, an increase of 11.0%.
- Total additions in the defined benefit pension plan were $37 million which was $30 million higher than the amount in the previous fiscal year. The increase was primarily due to investment experience. In fiscal year 2013 net investment return was +16.7% compared to a return last year of -0.2%. Similarly, due primarily to investments, total additions in the defined contribution plan were $11.2 million, compared to $4.7 million last fiscal year, an increase of 139%.
- The defined benefit plan recorded a 16.7% rate of return for the year, net of fees. For longer periods of time, the DTRFA annualized returns over 20 and 25 years of +7.5% and +8.4% respectively provide some additional perspective about the returns of the plan. For the defined contribution plan, net returns for the last fiscal year were +1.2% in the Bond Fund, +24.9% in the Equity Fund, and +0.8% in the Money Market Fund.
- The actuarial funding ratio of the defined benefit plan, a comparison of actuarial value of assets to actuarial accrued liability, was 54% at June 30, 2013. The funding ratio decreased from the 63% level of the previous year due to the actuarial smoothing of investment losses in previous years – a portion of investment losses in fiscal years 2008, 2009 and 2012 were realized in fiscal year 2013; and because benefits in the pension plan were recently increased.

### Overview of the Financial Statements

The discussion and analysis below is intended to assist the reader in better understanding the purpose and meaning of each of the key components of the financial statements, which are comprised of the following:

1. The *Statement of Plan Net Position* presents information about assets and liabilities, with the difference between the two reported as *net position-restricted for pension benefits.* The net position reflects the resources available to pay benefits to members when due. Over time, increases and decreases in the net position measures whether the financial position of the DTRFA is improving or deteriorating.
2. The *Statement of Changes in Plan Net Position* presents the results of fund operations during the year and discloses the additions to and deductions from plan net position. It supports the net change that has occurred to the prior year's net position on the statement of plan net position.
3. The *Notes to the Financial Statements* provide additional information that is essential to gain a full understanding of the data provided in the basic financial statements. The notes provide important and detail information about the DTRFA, the various pension trust funds, and the statements themselves.
4. The *Required Supplementary Information* consists of data on the funded status of the plan, the status of contributions from the employers and the State of Minnesota, and information pertaining to actuarial methods and assumptions. Also included as *Other Supplementary Information* are schedules of investment and administrative expenses, and information about cash receipts and disbursements.

## Management's Discussion and Analysis - Continued

**Financial Analysis**

The following table shows condensed information from the Statement of Plan Net Position:

| Plan Net Position | 2013 | 2012 | Change | Percent |
|---|---|---|---|---|
| Cash & Investments | $255,187,695 | $244,986,338 | $10,201,357 | 4.2% |
| Receivables | 1,068,724 | 2,115,417 | (1,046,693) | -49.5% |
| Securities Lending Collateral | 5,792,500 | 5,534,113 | 258,387 | 4.7% |
| Capital Assets | 247,843 | 271,609 | (23,766) | -8.8% |
| Total Assets | 262,296,762 | 252,907,477 | 9,389,285 | 3.7% |
| Liabilities | (7,260,191) | (13,568,797) | 6,308,606 | -46.5% |
| **Plan Net Position** | **$255,036,571** | **$239,338,680** | **$15,697,891** | **6.6%** |

The plan net position increased by $15.7 million during fiscal year 2013. This was primarily a result of investment experience – during the twelve months ended June 30, 2013 all equity markets, except for the emerging markets, delivered double digit returns. As a result, additions to plan net position increased significantly.

The following two tables show condensed information from the Statement of Changes in Plan Net Position:

| Additions to Plan Net Position | 2013 | 2012 | Change | Percent |
|---|---|---|---|---|
| Member & Employer Contributions | $11,391,322 | $10,481,506 | $909,816 | 8.7% |
| Total Investment Income (Loss) | 36,784,015 | 819,532 | 35,964,483 | 4,388.4% |
| Other | 11,735 | 112,171 | (100,436) | (89.5)% |
| **Total Additions** | **$48,187,072** | **$11,413,209** | **$36,773,863** | **322.2%** |

Employee and employer contribution rates in the defined benefit plan each increased by ½% at the beginning of fiscal year 2013. Contribution rates will increase again by ½% each on July 1, 2013. Voluntary employee contributions in the tax deferred funds were also higher in fiscal year 2013 compared to the previous year. The investment rate of return for the defined benefit plan of 16.7% in fiscal year 2013 was higher than the 8.0% actuarially assumed return and higher than the return of -0.2% in fiscal year 2012.

| Deductions from Plan Net Position | 2013 | 2012 | Change | Percent |
|---|---|---|---|---|
| Benefit Payments | $25,430,230 | $24,806,357 | $623,873 | 2.5% |
| Withdrawals & Transfers | 6,181,949 | 5,507,292 | 674,657 | 12.3% |
| Contribution Refunds | 265,188 | 96,935 | 168,253 | 173.6% |
| Administrative Expense | 611,814 | 715,777 | (103,963) | (14.5)% |
| **Total Deductions** | **$32,489,181** | **$31,126,361** | **$1,362,820** | **4.4%** |
| **Increase (Decrease) in Plan Net Position** | **$15,697,891** | **$(19,713,152)** | **$35,411,043** | **179.6%** |

Total deductions during fiscal year 2013 were slightly higher compared to the previous year. There were higher benefit payments in the defined benefit plan due to a greater number of retirees and higher withdrawals in the defined contribution plan. Total administrative expenses decreased by 14.5% in fiscal year 2013 primarily due to lower personnel related costs and lower actuarial costs.

## Actuarial Funded Status, Financial Position, and Economic Factors

The funding objective of the DTRFA defined benefit plan is to meet long-term benefit promises through prudent investment of fund assets and contributions which remain approximately level as a percent of member payroll over decades of time. Historical information relating to progress in meeting this objective is presented on pages 21-22. The DTRFA continues to maintain a long-term investment approach consistent with the long-term nature of plan obligations.

As of June 30, 2013, the funded ratio of the defined benefit plan was 54%, a decrease from the 63% level a year earlier. The funded ratio is derived by comparing the "actuarial value" of plan assets to the actuarial accrued liabilities of the plan. State law requires that a five-year smoothing method be used to determine actuarial value of plan assets. Most public pension funds use a smoothing technique to value their assets for actuarial purposes. This is done to avoid significant swings in the value of assets from one year to the next. During fiscal year 2013, this smoothing technique resulted in the recognition of $22.7 million in deferred investment losses from fiscal years 2009 and 2012. The recognition of the deferred losses from those years was offset by the recognition of a $7.9 million of gains from fiscal years 2010 and 2011. In fiscal year 2013, the fund experienced an actual investment gain of $15.8 million, of which $3.2 million was allocated to the current year. That same amount will be allocated to each of the next four years. At June 30, 2013 deferred investment gains totaled $15.2 million, which will be recognized during the next four years.

During fiscal year 2013, the fund experienced a net actuarial gain of $2.9 million due to demographic and other economic factors. Of this amount, there was a $1.3 million gain due to retirements occurring at ages later than assumed by the actuaries, a $742,000 gain due to member salaries that increased at a lower rate than assumed by the plan, and a loss of $625,000 due to retirees living longer than assumed by the plan. The remaining $1.4 million actuarial gain was attributed to a combination of several other immaterial factors.

Significant legislation was enacted in 2010 and again in 2013 to address a declining funding ratio following the negative market returns in fiscal years 2008 and 2009. Major provisions of the legislation included an increase to employee and employer contribution rates, and an additional $6 million in State aid in fiscal years 2014 and 2015. In addition, in order to facilitate discussions of a potential merger of the DTRFA with the State Teachers Retirement Association (TRA), the benefit accrual rate was increased from 1.7% to 1.9% so that it is consistent with the TRA, and an automatic 1% cost of living adjustment was reinstated.

The actuarial valuation report for July 1, 2013 notes that contribution rates are not sufficient for the plan to achieve 100% funding by the year 2040, the date required in law for the plan to be fully funded. Based on contribution rates in effect on July 1, 2013, the total rate of 27.66% (7.0% employee, 7.29% employer, and 13.37% State payment) is 2.88% lower than the actuarially required rate of 30.54%.

## Requests for Information

This financial report is designed to provide the Board of Trustees, members, retirees, employers, and other users with a general overview of the financial activities of the DTRFA and to demonstrate the Association's accountability for the funds under its control. Questions concerning any information provided in this report, or requests for additional financial information should be addressed to the staff of the Association.

# Statement of Plan Net Position

## June 30, 2013

| | Pension Trust Funds | | | | |
|---|---|---|---|---|---|
| | Defined Benefit Plan | Defined Contribution Plan | | | |
| | Pension Fund | Bond Fund | Equity Fund | Money Mkt Fund | Total |
| **Assets** | | | | | |
| Cash | $87,784 | $54,876 | $120,645 | $62,282 | $325,587 |
| Short-term investments | 11,043,877 | | 89,373 | 7,415,057 | 18,548,307 |
| Total cash and equivalents | 11,131,661 | 54,876 | 210,018 | 7,477,339 | 18,873,894 |
| Receivables | | | | | |
| Member contributions | 500,214 | | | | 500,214 |
| Employer contributions | 522,549 | | | | 522,549 |
| Interest and dividends | 24,330 | | 9 | 3,170 | 27,509 |
| Stock and bond sales | 10,899 | | | | 10,899 |
| Other | 7,252 | | 300 | 1 | 7,553 |
| Total receivables | 1,065,244 | | 309 | 3,171 | 1,068,724 |
| Investments, at fair value | | | | | |
| Corporate and other bonds | 36,923,105 | 13,084,082 | | | 50,007,187 |
| Equities | 119,546,896 | | 29,079,877 | | 148,626,773 |
| Private equity and limited partnerships | 36,180,686 | | | | 36,180,686 |
| Real assets | 1,499,155 | | | | 1,499,155 |
| Total investments | 194,149,842 | 13,084,082 | 29,079,877 | | 236,313,801 |
| Invested securities lending collateral | 5,435,320 | | 357,180 | | 5,792,500 |
| Properties, at cost, net of accumulated depreciation of $441,516 | 247,843 | | | | 247,843 |
| Total assets | 212,029,910 | 13,138,958 | 29,647,384 | 7,480,510 | 262,296,762 |
| **Liabilities** | | | | | |
| Accounts payable | 151,650 | | 1 | 300 | 151,951 |
| Securities lending liabilities | 6,468,112 | | 425,038 | | 6,893,150 |
| Stock and bond purchases | 109,605 | | | | 109,605 |
| Deferred contributions | | 21,329 | 65,955 | 18,201 | 105,485 |
| Total liabilities | 6,729,367 | 21,329 | 490,994 | 18,501 | 7,260,191 |
| **Net position - restricted for pension benefits** | $205,300,543 | $13,117,629 | $29,156,390 | $7,462,009 | $255,036,571 |

The accompanying notes are an integral part of these financial statements.

# Statement of Changes in Plan Net Position

## For the Year Ended June 30, 2013

| | Pension Trust Funds | | | | |
|---|---|---|---|---|---|
| | Defined Benefit Plan | Defined Contribution Plan | | | |
| | Pension Fund | Bond Fund | Equity Fund | Money Mkt Fund | Total |
| **Additions** | | | | | |
| Contributions | | | | | |
| Employer | $3,013,717 | | | | $3,013,717 |
| Plan members' deposits & transfers | 3,050,990 | $1,628,891 | $1,620,913 | $1,730,811 | 8,031,605 |
| State funding | 346,000 | | | | 346,000 |
| Total contributions | 6,410,707 | 1,628,891 | 1,620,913 | 1,730,811 | 11,391,322 |
| Investment activities income | | | | | |
| Net appreciation in fair value of investments | 29,775,722 | (209,006) | 5,622,330 | | 35,189,046 |
| Interest | 587,219 | 21 | 336 | 80,124 | 667,700 |
| Dividends | 1,418,122 | 403,741 | 452,206 | | 2,274,069 |
| Rental income (net) | 79,729 | | | | 79,729 |
| Total investment activities income | 31,860,792 | 194,756 | 6,074,872 | 80,124 | 38,210,544 |
| Less investment expense | (1,311,857) | (10,913) | (105,094) | (8,160) | (1,436,024) |
| Net investment activities income | 30,548,935 | 183,843 | 5,969,778 | 71,964 | 36,774,520 |
| Securities lending | | | | | |
| Securities lending income | 12,370 | | 1,182 | | 13,552 |
| Less securities lending expense | (3,704) | | (353) | | (4,057) |
| Net income from securities lending | 8,666 | | 829 | | 9,495 |
| Total net investment income | 30,557,601 | 183,843 | 5,970,607 | 71,964 | 36,784,015 |
| Other income | 11,735 | | | | 11,735 |
| Total Additions | 36,980,043 | 1,812,734 | 7,591,520 | 1,802,775 | 48,187,072 |
| **Deductions** | | | | | |
| Benefits to participants | | | | | |
| Retirement | 23,474,340 | | | | 23,474,340 |
| Disability | 121,959 | | | | 121,959 |
| Survivor | 1,833,931 | | | | 1,833,931 |
| Contribution refunds | 265,188 | | | | 265,188 |
| Plan members' withdrawals & transfers | | 1,599,433 | 2,956,490 | 1,626,026 | 6,181,949 |
| Total benefits, refunds & withdrawals | 25,695,418 | 1,599,433 | 2,956,490 | 1,626,026 | 31,877,367 |
| Administrative expenses | 537,013 | 23,419 | 36,982 | 14,400 | 611,814 |
| Total Deductions | 26,232,431 | 1,622,852 | 2,993,472 | 1,640,426 | 32,489,181 |
| **Net increase (decrease)** | 10,747,612 | 189,882 | 4,598,048 | 162,349 | 15,697,891 |
| **Net position - restricted for pension benefits** | | | | | |
| **- Beginning of year** | 194,552,931 | 12,927,747 | 24,558,342 | 7,299,660 | 239,338,680 |
| **- End of year** | $205,300,543 | $13,117,629 | $29,156,390 | $7,462,009 | $255,036,571 |

The accompanying notes are an integral part of these financial statements.

# Notes to the Financial Statements

## NOTE 1. SUMMARY OF ACCOUNTING POLICIES

**Organization**
The Duluth Teachers' Retirement Fund Association (Association) was created in 1910 to provide retirement and other specified benefits for its members pursuant to Minnesota Statutes Chapters 354A and 356. Association membership consists of eligible employees of Independent School District 709, eligible staff of Lake Superior College and the employees of the Association. The Association is governed by a nine-member board of trustees.

**Financial Reporting Entity**
The Association's financial statements include the Pension Fund, a defined benefit plan, and three funds in the defined contribution plan - the Bond Fund, Equity Fund, and Money Market Fund. These plans are presented as pension trust funds in the financial statements. The Association's financial statements include all plans for which it is financially accountable. The Association is not included as a component unit of another reporting entity.

**Basis of Accounting**
The Association's financial statements are prepared using the accrual basis of accounting. Additions are recorded in the accounting period when they are earned and become measurable and deductions are recorded when the liability is incurred. Member and employer contributions are recorded as revenues when due, pursuant to formal commitments, as well as statutory or contractual requirements. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

**Deposits and Investments**
Deposits
Minnesota Statutes, Section 356A.06, Subd. 8a authorizes the Association to deposit its cash and to invest in money market accounts and certificates of deposit in financial institutions designated by the Association's Board of Trustees. Minnesota statutes require that all of the Association's deposits be covered by insurance, surety bond, or collateral.

Investments
Minnesota Statutes, Sections 354A.08, 356A.06, Subd. 7 and the Association's Articles of Incorporation and Bylaws designate authorized investment types and limitations. Minnesota Statutes, Section 356A.04, Subd. 2 specifies that investments are governed by the "prudent person standard." The prudent person standard pertains to all fiduciaries, and includes anyone who has authority with respect to the Association.

Investments are reported at fair value. Short-term investments are reported at cost, which approximates fair value. Securities traded on an exchange are valued at the last reported sales price at current exchange rates. Investments that do not have an established market are reported at estimated fair value. Net appreciation (depreciation) in fair value of investments includes net unrealized and realized gains and losses. Purchases and sales of securities are recorded on a trade-date basis. Dividends are recorded on the ex-dividend date.

There are no investments in, loans to, or leases with parties related to the Association.

**Receivables**
Receivables are recognized in the period in which amounts are due pursuant to formal commitments as well as contractual requirements. At June 30, 2013, receivables consisted of contributions owed by members and employers, interest and dividends from investments, and amounts due from the sales of investments where the trade was initiated prior to June 30, 2013, but settled at a later date.

**Liabilities**
Liabilities for benefits and refunds are recognized when due and payable in accordance with the terms of the plan. At June 30, 2013, liabilities consisted principally of investment management fees, obligations to return securities lending collateral, member deposits in the defined contribution plan which will be credited to the members' accounts after the computation of the monthly unit value, and obligations for the purchase of investments where the trade was initiated prior to June 30, 2013, but settled at a later date.

**Risk Management**
The Association is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; injuries to employees; and natural disasters. To cover its potential liabilities, the Association purchases commercial insurance. There were no significant reductions in insurance coverage from coverage in the prior year, and there were no insurance claims or settlements in the past three fiscal years.

**Properties**
Land, land improvements, building, and furniture and fixtures are stated at cost. Depreciation is computed over the estimated useful lives of the properties using the straight-line method.

## 1. Summary of Accounting Policies (cont.)

A summary of properties at June 30, 2013, is as follows:

| Class | Useful Life-Yrs. | Carrying Value | Accumulated Depreciation | Net |
|---|---|---|---|---|
| Land | N/A | $35,540 | N/A | $35,540 |
| Land Improvement | 7-15 | 68,414 | $54,063 | 14,351 |
| Building | 15-30 | 397,388 | 212,671 | 184,717 |
| Furniture, fixtures | 5-7 | 188,017 | 174,782 | 13,235 |
| Totals | | $689,359 | $441,516 | $247,843 |

## NOTE 2. DEPOSIT & INVESTMENT RISK DISCLOSURES

### Deposits

Custodial credit risk for deposits is the risk that in the event of a bank failure, the Association's deposits may not be returned. The deposits are held in one institution with interest-bearing account balances up to $250,000 insured by the Federal Deposit Insurance Corporation (FDIC) and non-interest bearing accounts fully insured by the FDIC. As required by Minnesota statutes, the Association's deposits in excess of the FDIC limit are covered by collateral. At year end the Association had cash deposits totaling $335,107 all of which were covered by insurance.

### Investments

The following table shows the investments of the Association by type at June 30, 2013:

| | |
|---|---|
| **Short-term investments** | |
| Commingled investment funds | $14,548,307 |
| Certificates of deposit | 4,000,000 |
| **Investments held by the Association or its agent** | |
| Commingled international equity fund | 10,576,588 |
| International equity mutual funds | 45,600,114 |
| Commingled domestic equity funds | 30,683,072 |
| Domestic equity mutual funds | 11,639,208 |
| Domestic equities | 43,454,914 |
| Asset backed securities | 368,752 |
| Corporate bonds | 261,597 |
| Mortgage backed securities | 2,720,816 |
| Commingled bond funds | 46,656,022 |
| Real estate | 1,499,155 |
| Limited partnership investments | 12,786,394 |
| Private equity investments | 23,394,292 |
| **Invested collateral on securities loaned** | |
| Money market funds | 4,567,755 |
| Mortgage backed securities | 340,610 |
| Asset backed securities | 261,029 |
| Corporate bonds | 623,106 |
| **Investments held by broker-dealers under securities lending program** | |
| Domestic equities | 6,672,877 |
| Total investments | $260,654,608 |

| | |
|---|---|
| Amounts from Statement of Plan Net Assets: | |
| Short-term investments | $18,548,307 |
| Investments | 236,313,801 |
| Invested securities lending collateral | 5,792,500 |
| Total investments | $260,654,608 |

### Credit Risk – Debt Securities

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to the Association. The Association limits credit risk by requiring investment managers to meet the following requirements:

- Total portfolio quality must be maintained at a minimum overall rating of "A".
- Securities that have a rating of "BBB" or lower may not exceed 15% of an investment manager's portfolio.
- The average quality rating of commercial paper and money market securities in the portfolio will be at least "A1/P1".

As shown below, the value of below investment grade debt securities is $2,683,174 or 5.4% of the debt portfolio.

| Quality Rating | |
|---|---|
| AAA | $7,292 |
| AA+ | 89,861 |
| AA | 3,023 |
| A+ | 29,844,761 |
| A | 16,948,431 |
| BBB+ | 83,444 |
| BBB | 113,575 |
| BBB- | 346,411 |
| B | 103,665 |
| CCC | 1,833,203 |
| D | 202,876 |
| Not rated | 430,645 |
| Total credit risk debt securities | $50,007,187 |

**2. Deposit & Investment Risk Disclosures (cont.)**

Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty, the Association will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. At June 30, 2013 the Association had no custodial credit risk because all investment securities were registered in the name of the Association and were held in the possession of the Association's custodial bank.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Association limits this risk by including the following guidelines in the Statement of Investment Objectives and Policies (SIOP):

- The market value weighted average expected maturity of the bond portfolio shall not exceed 15 years.
- The volatility of returns for the fixed income component should be controlled so that the annualized standard deviation of quarterly returns does not exceed 130% of the same measure for the Barclays Capital U.S. Aggregate Index.
- The average effective modified duration of each bond portfolio must be between 75% and 125% of the effective duration of the Barclays Capital U.S. Aggregate Index.
- Asset-backed or collateralized mortgage obligations will be classified as having a "high risk" if they have an average life greater than 10 years and duration greater than 5.6 years. Asset-backed or collateralized mortgage backed securities meeting the definition of high risk will be limited to no more than 10%, at market value, of the manager's portfolio.

Duration is a measure of a debt investment's exposure to fair value changes arising from changes in interest rates. Effective duration uses the present value of cash flows, weighted for those cash flows as a percentage of the investment's full price.

At June 30, 2013 the index range required by the Association for bond managers is 4.1 years to 6.9 years based on a Barclays Capital U.S. Aggregate Index of 5.5 years at June 30, 2013.

The Association's bond portfolios were within the required range. The Pension Fund bond portfolio had a duration of 4.1 and the Bond Fund portfolio had a duration of 5.8 at June 30, 2013. The overall effective weighted duration for all fixed income investments is shown below.

| Investment | Fair Value | Duration (Years) |
|---|---|---|
| Asset backed securities | $368,752 | .00 |
| Corporate bonds | 261,597 | (.60) |
| Mortgage backed securities | 2,720,816 | 1.06 |
| Commingled bond funds | 46,656,022 | 4.78 |
| Total debt securities | $50,007,187 | 4.51 |

Concentration of Credit Risk

Concentration of credit risk is the risk of loss that may be attributed to the magnitude of investments in a single holding. The Association limits this risk by maintaining diversified portfolios. The following guidelines are from the Statement of Investment Objectives & Policies (SIOP):

- No more than 6% of any portfolio may be invested in any one corporate issuer.
- No purchase of non-agency mortgage obligations or non-agency mortgage backed pass-throughs will be permitted unless exposure falls below 15%.
- No purchases of real estate related asset backed securities are permitted.
- Rule 144a securities are limited to 20% of a portfolio.
- Foreign bonds are limited to 20% of the portfolio.
- No equity investment may exceed 5% of the total outstanding shares of any company.

At June 30, 2013 there were no single issuer investments that exceeded the above guidelines.

Foreign Currency Risk

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

State law limits certain investments to a total portfolio limit of no more than 20% of the market value of the portfolio. Emerging market equities and international bonds are included in this category.

The Association's investment policies require non-U.S. equity managers to invest at least 80% of the portfolio in large capitalization stocks and no more than 20% in small capitalization stocks. The policies also require bond managers to invest no more than 20% of the portfolio in issues of the foreign bond sector (defined as securities whose payments are based on foreign interest rates).

# Notes - Continued

**2. Deposit and Investment Risk Disclosure (cont.)**

The Association's investments with exposure to foreign currency risk are as follows (in U.S. Dollars):

| Investment | Currency | Fair Value of Investment |
|---|---|---|
| Private equity investments | European Euro | $5,733,347 |
| Commingled international equity fund | Various | 10,576,588 |
| International equity mutual funds | Various | 45,600,114 |

**Securities Lending**

Minnesota Statutes and the investment policies of the Association permit securities lending transactions - loans of securities to broker-dealers and other approved entities for collateral with a simultaneous agreement to return the collateral for the same securities in the future. Securities on loan include U.S. Government securities, corporate and other bonds, and common stocks. The Association's investment custodian acts as its agent in lending securities for cash collateral at 102% of the value of the securities loaned plus accrued income. The contract with the custodian requires them to indemnify the Association if the borrowers fail to return the securities. Securities on loan are recorded as investments on the Statement of Plan Net Position and the corresponding liability is recorded for the market value of the collateral received. At year-end, the Association had no credit risk exposure to borrowers because the collateral amounts received were greater than amounts out on loan.

All securities loans can be terminated on demand by either the Association or the borrower. Loan terms are open-ended and are negotiated on a daily basis. Collateral received is invested in various types of short-term securities, asset backed securities, and corporate bonds.

The securities on loan at year-end had a market value of $6,672,877. The Association had received collateral of $6,893,150 on these loans and the market value of the invested collateral received for the securities on loan was $5,792,500. If all the loans were terminated at June 30, 2013, the Association would have needed to make up the $1.1 million difference between the market value of the invested collateral and the collateral liability.

**Commitments and Contingencies**

At June 30, 2013 the Pension Fund had commitments for future purchases of private equity investments amounting to approximately $9,200,000.

## NOTE 3. DEFINED BENEFIT PLAN

The following brief description of the Pension Fund plan is provided for general information purposes only. The plan is not subject to the provisions of the Employee Retirement Income Security Act of 1974.

**General**

The Association administers a cost-sharing multiple employer defined benefit pension plan covering licensed educators of Independent School District 709, staff of Lake Superior College hired prior to July 1, 1995 who elected coverage by the Association, and the employees of the Association. At June 30, 2013 membership consisted of:

| | |
|---|---|
| • Retirees and beneficiaries receiving benefits | 1,445 |
| • Terminated plan members entitled to, but not yet receiving benefits | 1,025 |
| • Active plan members | 873 |
| Total | 3,343 |

**Pension Benefits**

Association members may be eligible for benefits under three different plans depending on year of hire. Members in all three plans are covered by Social Security.

Old Plan – Covers members hired prior to July 1, 1981. Normal retirement benefits are earned at age 60, or if age plus service totals 90. Benefits vest after 10 years or at age 60. The annual normal retirement benefit is equal to 1.45% of a member's high five-year average salary multiplied by the total years of credited service. Early benefits are available as early as age 55 with 10 or more years of credited service with a .25% per month early retirement deduction under age 60. Old Plan members receive a benefit under Tier I or Tier II if that benefit is greater.

Tier I Plan – Covers members hired before July 1, 1989. Normal retirement benefits are earned at age 65 or with 30 plus years of service over age 62, or if age plus service totals 90. Retirement benefits vest after 3 years of service or at age 65. The annual retirement benefit is equal to 1.2% for each of the first ten years of service credit and 1.7% for each subsequent year of service credit multiplied by the high five years average salary. (On July 1, 2013, these formula accrual rates will change to 1.4% and 1.9% respectfully for all prospective service credit.) Early benefits are available as early as age 55 with three or more years of credited service or at any age with 30 or more years of credited service with a .25% per month early retirement deduction under the normal retirement age. Tier I Plan members receive a benefit under the Tier II Plan if that benefit is greater.

# Notes - Continued

**3. Defined Benefit Plan (cont.)**

Tier II Plan – Covers Association members hired after June 30, 1989. Normal retirement benefits are tied to the Social Security normal retirement age but cannot exceed age 66. Retirement benefits vest after 3 years for members hired prior to July 1, 2010 and after 5 years for members hired after June 30, 2010 or age 65. The annual normal retirement benefit is equal to 1.70% for all years of credited service multiplied by the high five successive years average salary. (On July 1, 2013, the formula accrual rate will change to 1.9% for all prospective service credit.) Benefits are available as early as age 55 with three or more years of credited service with an actuarial equivalence early retirement reduction under full retirement age.

Under all plans, members may elect to receive their pension benefits in the form of a single-life annuity, a joint and survivor annuity, or a life and term certain annuity, and have the option of electing Social Security actuarial income leveling. Terminating members may receive a refund of their contributions with interest computed at 4% or may elect an augmented deferred retirement benefit if retirement benefits have vested.

**Death and Disability Benefits**

If active members die prior to the receipt of their first retirement allowance payment, death benefits are payable under each of the three plans. Active members who have not reached normal retirement age and have at least three years of credited service may receive a disability benefit upon becoming permanently disabled.

**Cost of Living Adjustment**

For the fiscal year ended June 30, 2013 there was no cost of living adjustment (COLA). The laws that were in effect during the year required that the plan be at least 80% funded before a COLA could be paid. The funding ratio of the plan was less than 80%, therefore there was no COLA.

Effective July 1, 2013 a COLA will be paid to eligible benefit recipients on January 1 of each year. The COLA, first payable on January 1, 2014, is equal to one percent. The COLA mechanism will permanently change once the funding ratio of the plan exceeds 90% using actuarial value of assets. When that threshold is achieved, the COLA will match the consumer price index, up to 5%.

**Funding**

Benefit and contribution provisions are established by state law and may be amended only by the Minnesota Legislature. Minnesota Statutes, Section 354A.12 set the rates for employee and employer contributions that, expressed as a percentage of annual covered payroll, are sufficient to cover administrative expense and to fully fund the pension plan by the year 2040. The requirement to reach full funding by the year 2040 is set in Minnesota Statutes, Section 356.215, Subd. 11. That statute also requires that assets in excess of the actuarial accrued liability be amortized as a level percentage of covered payroll over a rolling 30-year period.

As part of the annual actuarial valuation, the actuary determines the sufficiency of the statutory contribution rates toward meeting the required full funding deadline. The actuary compares the actual contribution rate to a "required" contribution rate. The required contribution rate consists of: (a) normal costs based on entry age normal cost methods, (b) a supplemental contribution for amortizing any unfunded actuarial accrued liability (UAAL) by the required date for full funding, and (c) an allowance for administrative expenses. Administrative expenses are financed by employee and employer contributions.

For the fiscal year ended June 30, 2013, members were required to contribute 6.5% of their salaries to the Association. Employer contributions were 6.79% of the members' salaries. Legislation passed in 2013 makes the following changes to the contributions to the pension fund:

- Beginning July 1, 2013 members will be required to contribute 7.0% of their salaries and employers will be required to contribute 7.29% of members' salaries.
- Beginning July 1, 2014 members will be required to contribute 7.5% of their salaries and employers will be required to contribute 7.5% of members' salaries.
- In fiscal year 2014 and in fiscal year 2015, the State of Minnesota will make a state aid payment of $6,000,000 to the Association. This payment will be in addition to the $346,000 in state aid committed to the plan, and an additional amount of state amortization aid that is variable each year.

# Notes - Continued

**3. Defined Benefit Plan (cont.)**

**<u>Funded Status and Funding Progress</u>**

The funded status as of July 1, 2013, the most recent actuarial date is as follows:

| | |
|---|---|
| Actuarial value of assets | $190,116,720 |
| Actuarial accrual liability (AAL) | 352,143,396 |
| Unfunded AAL (UAAL) | 162,026,676 |
| Funded ratio | 54.0% |
| Annual actual covered payroll | $44,384,639 |
| UAAL as a percentage of payroll | 365.1% |

The funded ratio decreased 9.4% from the previous year. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents similar information but uses a multi-year format to show trend information. These trends indicate whether the actuarial value of plan assets are increasing or decreasing over time relative to the actuarial accrued liability for benefits. The trend information was obtained from the annual valuation report of the independent actuary retained by the DTRFA.

Additional information as of the latest valuation follows:

- Valuation date.............. July 1, 2013
- Actuarial cost method...... Entry age normal
- Amortization method...... Level percent of payroll
- Amortization period......... Closed, to June 30, 2040
- Inflation rate.................. 3.5%
- Asset valuation method: Actuarial value of assets is determined using the market value of assets adjusted by spreading over a five-year period the difference between the actual return on investments and the assumed rate of return.
- Investment return: 8.0% per annum for the period July 1, 2013 through June 30, 2017, and 8.5% thereafter.
- A one percent annual post-retirement adjustment.
- Projected salary increase: Total reported pay for the current fiscal year is increased annually for each future year according to an ultimate rate table which includes a 8-year select period.

## NOTE 4. DEFINED CONTRIBUTION PLAN

The Bond Fund, Equity Fund, and Money Market Fund were established to account for a voluntary tax deferred program which meets the requirements of section 403(b) of the Internal Revenue Code. Each fund has different investment objectives. Voluntary contributions may be made by eligible employees of Independent School District 709, subject to plan and Internal Revenue Code limitations. There are no employer contributions to these funds. Income tax on employee contributions and on associated earnings are deferred until amounts are withdrawn. Benefits are paid as lump-sum, or as periodic benefit payments, at the option of the participant based on the value of participant's account balance at the time of withdrawal. At June 30, 2013, there were 383 participants in the Bond Fund, 509 participants in the Equity Fund, and 275 participants in the Money Market Fund.

A summary of the unit values in the tax deferred program at June 30, 2013, is as follows:

| | Bond Fund | Equity Fund | Money Mkt. Fund |
|---|---|---|---|
| Net posiiton | $13,117,629 | $29,156,390 | $7,462,009 |
| Number of units | 893,068 | 2,366,235 | 2,721,349 |
| Net asset value per unit | $14.6883 | $12.3218 | $2.7420 |

# Required Supplementary Information

## Schedule of Funding Progress

(Dollars in Thousands)

| Actuarial Valuation Date | Actuarial Value of Assets (a) | Actuarial Accrued Liability (AAL) Entry Age (b) | Unfunded AAL (UAAL) (b-a) | Funded Ratio (a/b) | Covered Payroll (c) | UAAL as a Percentage of Covered Payroll ((b-a)/c) |
|---|---|---|---|---|---|---|
| 7/1/08 | $298,067 | $363,044 | $64,977 | 82.1% | $51,711 | 125.7% |
| 7/1/09 | 279,256 | 364,811 | 85,555 | 76.6 | 51,019 | 167.7 |
| 7/1/10 | 255,309 | 312,650 | 57,341 | 81.7 | 49,502 | 115.8 |
| 7/1/11 | 235,072 | 321,065 | 85,993 | 73.2 | 48,325 | 177.9 |
| 7/1/12 | 206,833 | 326,244 | 119,410 | 63.4 | 45,764 | 260.9 |
| 7/1/13 | 190,117 | 352,143 | 162,026 | 54.0 | 44,385 | 365.1 |

*(unaudited)*

## Schedule of Contributions From Employers and the State of Minnesota

(Dollars in Thousands)

| Year Ended June 30 | Annual Required Employer Contributions | Actual Employer Contributions | Employer Percentage Contributed | Additional State Contributions | State Percentage Contributed |
|---|---|---|---|---|---|
| 2008 | $ 4,560 | $ 2,994 | 65.7% | - | - |
| 2009 | 5,170 | 2,954 | 57.1 | $346 | 6.7% |
| 2010 | 5,922 | 2,866 | 48.4 | 760 | 12.8 |
| 2011 | 3,609 | 2,798 | 77.5 | 659 | 18.3 |
| 2012 | 4,997 | 2,879 | 57.6 | 554 | 11.1 |
| 2013 | 7,162 | 3,014 | 42.1 | 346 | 4.8 |

Note: Annual required contribution is actuarially determined based on projected payroll.
The employer is required by statute to contribute 6.79% of payroll to the Pension Fund. Beginning in 2009, the State of Minnesota began making additional payments directly to the Pension Fund.
The employer and the State made all the contributions required by statute.

*(unaudited)*

# Other Required Supplementary Information

## Actuarial Methods and Assumptions

The actuarial accrued liability is determined as part of an annual actuarial valuation. Significant methods and assumptions are:

- The most recent actuarial valuation date is July 1, 2013.
- Actuarial cost is determined using the Entry Age Normal Actuarial Cost Method.
- The amortization method assumes a level percentage of an increasing payroll using a payroll growth assumption of 3.5%.
- The amortization period is closed. The date to amortize an unfunded actuarial accrued liability is June 30, 2040. Assets in excess of the actuarial accrued liability reduces contribution requirements as a level percent of pay over a rolling 30-year period.
- The investment rate of return is 8.0% per annum for the period July 1, 2012 through June 30, 2017, and 8.5% thereafter.
- A one percent post-retirement adjustment is payable on January 1 each year.
- Actuarial value of assets is determined using the market value of assets adjusted by spreading over a five-year period the difference between the actual return on investments and the assumed rate of return.
- A rate of inflation of 3.5%.
- Salary increases are based on a select and ultimate table, with an eight-year select period. For service from hire through 7 completed years, a 7.75% salary increase is assumed.
- Mortality rates using the RP-2000 Mortality Table for males and females, set back 3 years, and projected with generational improvement from 2012.

## Significant Changes to Plan Provisions and Actuarial Methods & Assumptions - Last 6 Years

2008 - Actuarial Assumption Changes:

- Payroll growth assumption changed from 5.0% to 4.5%.
- Salary assumptions, based on a select and ultimate table, were changed after age 50. Ultimate rates at age 55 changed from 5.0% to 4.5%; at age 60 changed from 5.0% to 4.0%; at age 65 changed from 5.0% to 3.5%.
- Mortality table changed to 1994 Group Annuity Mortality (GAM) table, set back 2 years.
- Disabled lives mortality changed to the Disabled Eligible for Social Security Disability-ERISA Sec. 4044 for 2006 for ages 54 and younger, graded between ages 55 and 64, and the GAM table set back two years for ages 65 and older.
- Retirement rates changed: from 10% at age 55 to age 60, to 15%; from 20% at age 65 to 45%; from graded rates at age 70 to age 80, to 100%.
- Withdrawal select period rates changed: first year 60% (was 40%); second year 20% (was 10%); third year 15% (was 6%).
- Form of annuity selected, male: 30% elect 50% joint & survivor option; 40% elect 100% joint & survivor option.
- Form of annuity selected, female: 15% elect 50% joint & survivor option; 15% elect 100% joint & survivor option.

2010 - Changes to Plan Provisions:

- Employee contribution rate increased from 5.5% to 6.0% on July 1, 2011, then to 6.5% on July 1, 2012.
- Employer contribution rate increased from 5.79% to 6.29% on July 1, 2011, then to 6.79% July 1, 2012.
- Automatic cost of living adjustment replaced with one based on the funding ratio of the plan, effective July 1, 2010.
- Vesting increased from 3 years to five years for employees hired after June 30, 2010.
- Interest paid on refunds reduced from 6.0% to 4.0%, effective July 1, 2010.
- The rate of augmentation for all deferred accounts lowered to 2.0%, effective July 1, 2012.

2012 - Actuarial Assumption Changes:

- Interest rate changed from 8.5% to 8.0% for the period July 1, 2012 through June 30, 2017, then 8.5% thereafter.
- Payroll growth assumption changed from 4.5% to 3.5%.
- Salary scale, mortality, turnover and retirement assumptions updated to reflect recent experience and future expectations.

2013 - Changes to Plan Provisions:

- Employee contribution rate increases from 6.5% to 7.0% on July 1, 2013, then to 7.5% on July 1, 2014.
- Employer contribution rate increases from 6.79% to 7.29% on July 1, 2013, then to 7.5% July 1, 2014.
- An additional State aid payment of $6 million will be paid October 2013 and 2014.
- One percent automatic cost of living adjustment restored, effective July 1, 2014
- Benefit multipliers increased in Tier I and Tier II for prospective service credit; from 1.2% to 1.4%, and 1.7% to 1.9%.
- Early retirement reduction factors revised in the Tier II plan

*(Unaudited)*

# Schedule of Investment & Administrative Expenses

## For the Year Ended June 30, 2013

| | Pension Trust Funds | | | | |
|---|---|---|---|---|---|
| | Defined Benefit Plan | Defined Contribution Plan | | | |
| | Pension Fund | Bond Fund | Equity Fund | Money Mkt Fund | Total |
| **Investment Expenses** | | | | | |
| Salaries | $28,585 | | | | $28,585 |
| Payroll taxes | 2,154 | | | | 2,154 |
| Group insurance | 6,689 | | | | 6,689 |
| Legal and professional | 55,611 | | | | 55,611 |
| Investment management | 1,075,175 | | $81,596 | | 1,156,771 |
| Investment advisor | 89,129 | $5,913 | 11,798 | $3,160 | 110,000 |
| Custodial bank fees | 54,514 | 5,000 | 11,700 | 5,000 | 76,214 |
| **Total investment expenses** | **$1,311,857** | **$10,913** | **$105,094** | **$8,160** | **$1,436,024** |
| **Administrative Expenses** | | | | | |
| Personnel | | | | | |
| Salaries | $192,661 | $13,797 | $21,557 | $7,759 | $235,774 |
| Payroll taxes | 14,863 | 1,066 | 1,666 | 600 | 18,195 |
| Group insurance | 35,204 | 3,209 | 5,013 | 1,805 | 45,231 |
| Total personnel expenses | 242,728 | 18,072 | 28,236 | 10,164 | 299,200 |
| General expenses | | | | | |
| Bank charges | 12,094 | | | 15 | 12,109 |
| Data processing | 4,756 | 625 | 977 | 352 | 6,710 |
| Depreciation | 22,191 | 504 | 787 | 283 | 23,765 |
| Dues and periodicals | 3,465 | | | | 3,465 |
| Insurance | 3,313 | | | | 3,313 |
| Meetings, conventions & travel | 31,711 | | | | 31,711 |
| Printing, postage & office supplies | 13,658 | 360 | 472 | 264 | 14,754 |
| Real estate taxes | 17,913 | | | | 17,913 |
| Repairs and service contracts | 10,982 | | | | 10,982 |
| Supplies - building | 16,788 | | | | 16,788 |
| Utilities and telephone | 9,994 | | | | 9,994 |
| Other | 454 | | | | 454 |
| Total general expense | 147,319 | 1,489 | 2,236 | 914 | 151,958 |
| Professional fees | | | | | |
| Actuarial | 51,995 | | | | 51,995 |
| Auditing and accounting | 52,118 | 3,858 | 6,510 | 3,322 | 65,808 |
| Legal and consulting | 42,853 | | | | 42,853 |
| Total professional fees | 146,966 | 3,858 | 6,510 | 3,322 | 160,656 |
| **Total administrative expenses** | **$537,013** | **$23,419** | **$36,982** | **$14,400** | **$611,814** |

# Summary Schedules

## For the Year Ended June 30, 2013

## Summary Schedule of Cash Receipts and Disbursements

### Pension Fund

| | |
|---|---|
| **Cash and Equivalents at Beginning of Year - July 1, 2012** | **$16,102,004** |
| **Add Receipts:** | |
| Member Contributions | 3,037,025 |
| Employer Contributions | 3,001,087 |
| State Funding | 346,000 |
| Investment Income | 2,299,132 |
| Investments Redeemed/Sold | 135,177,708 |
| Other | 11,735 |
| **Total Cash Receipts** | 143,872,687 |
| **Less Disbursements:** | |
| Benefit Payments | 25,426,806 |
| Refunds | 265,188 |
| Administrative Expense | 499,724 |
| Investment Expense | 1,322,624 |
| Investments Purchased | 121,328,688 |
| **Total Cash Disbursements** | 148,843,030 |
| **Cash and Equivalents at End of Year - June 30, 2013** | **$11,131,661** |

## Schedule of Payments to Consultants

### Pension Fund

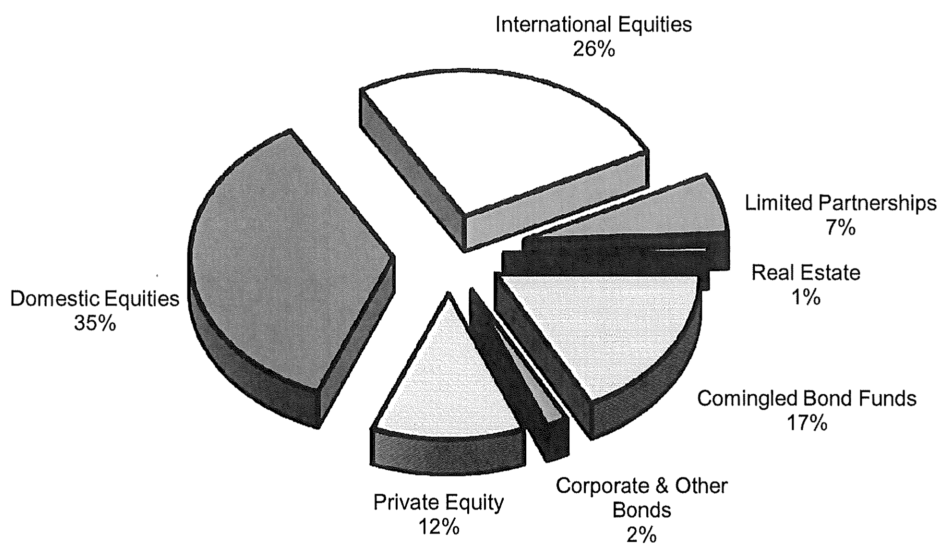
| Individual or Firm Name | Nature of Services | Fee Paid |
|---|---|---|
| Eikill & Schilling Ltd. | Accounting/Consulting | $24,256 |
| Wipfli LLP | Accounting/Consulting | $10,012 |
| Office of the State Auditor | Auditing Services | 17,851 |
| The Segal Company | Actuarial Services | 51,995 |
| Best & Flanagan LLP | Legal Services | 49,388 |
| Johnson, Killen, & Seiler, P.A. | Legal Services | 864 |
| Total | | **$154,366** |

# Investment Summary

## Schedule of Investments - June 30, 2013

| Pension Fund | Percent of Market Value | Market Value | Cost | Market Value Over (Under) Cost |
|---|---|---|---|---|
| Commingled bond funds | 17.3% | $33,571,940 | $33,961,503 | ($389,563) |
| Corporate & other bonds | 1.7% | 3,351,165 | 5,643,025 | (2,291,860) |
| Domestic equities | 35.5% | 68,910,261 | 39,309,376 | 29,600,885 |
| International equities | 26.1% | 50,636,635 | 46,109,830 | 4,526,805 |
| Limited partnerships | 6.6% | 12,786,394 | 10,870,782 | 1,915,612 |
| Private equity | 12.0% | 23,394,292 | 19,918,424 | 3,475,868 |
| Real estate | 0.8% | 1,499,155 | 1,499,155 | - |
| Total Pension Fund | 100.0% | 194,149,842 | 157,312,095 | 36,837,747 |
| **Tax Shelter Bond Fund** | | | | |
| Commingled Bond Fund | 100.0% | 13,084,082 | 11,941,801 | 1,142,281 |
| **Tax Shelter Equity Fund** | | | | |
| Domestic equity funds | 60.3% | 17,551,819 | 11,187,819 | 6,364,000 |
| Domestic equities | 20.6% | 5,987,991 | 2,874,682 | 3,113,309 |
| International equity fund | 19.1% | 5,540,067 | 4,505,039 | 1,035,028 |
| Total Equity Fund | 100.0% | 29,079,877 | 18,567,540 | 10,512,337 |
| **Total All Funds** | | **$236,313,801** | **$187,821,436** | **$48,492,365** |

### Asset Allocation - Pension Fund

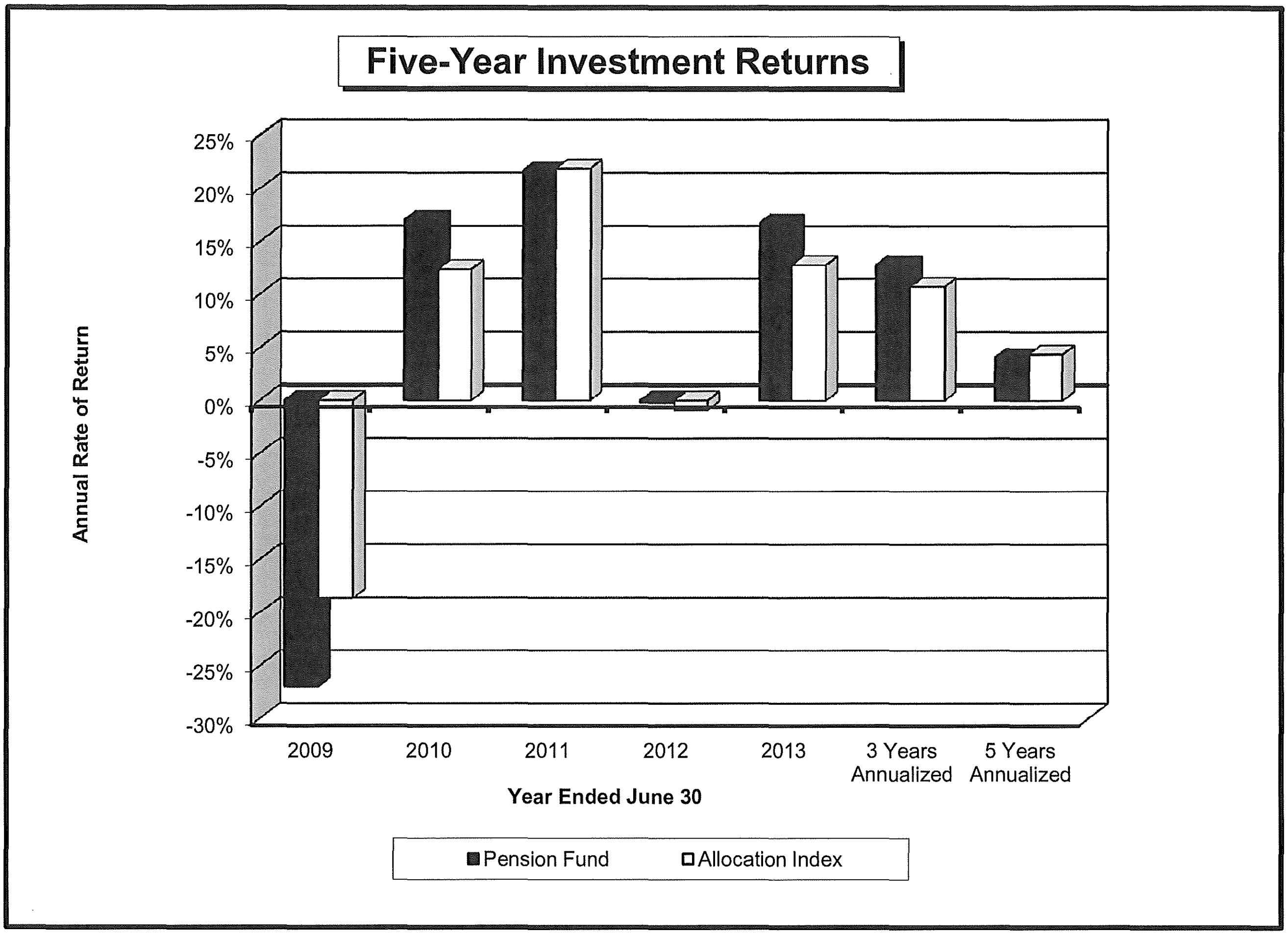


# Investment Returns
## (Last Five Years)

A time-weighted performance measure includes the effect of income earned as well as realized and unrealized market value changes. In addition, the time-weighted total rate of return nets out the influence of contributions made to and distributions taken from the manager or fund. The time-weighted rates of return below are based on market rate returns, net of investment fees, calculated in accordance with the standards set forth by the CFA Institute (formerly AIMR).

| | Annualized Returns for Periods Ended June 30, 2013 - Pension Fund; Net of Fees | | |
|---|---|---|---|
| **Pension Fund Investments** | **1-year** | **3-year** | **5-year** |
| **Total Pension Fund Portfolio** | **16.7%** | **12.8%** | **4.1%** |
| Allocation index* | 12.8% | 10.7% | 4.4% |
| **U.S. Equities** | **26.7%** | **18.8%** | **6.6%** |
| S&P 500 | 20.6% | 18.5% | 7.0% |
| Russell 2000 Growth | 23.7% | 20.0% | 8.9% |
| Russell 2500 Value | 26.9% | 18.9% | 9.4% |
| **International Equities** | **17.1%** | **11.1%** | **-1.6%** |
| MSCI ACWI ex-U.S. | 13.6% | 8.0% | -0.8% |
| **Fixed Income** | **4.9%** | **6.3%** | **7.6%** |
| Barclays Capital Aggregate Index | -0.7% | 3.5% | 5.2% |
| **Real Assets** | **9.8%** | **11.8%** | **-1.5%** |
| Custom Real Asset Index | 10.7% | 13.1% | -3.2% |
| **Cash Equivalents** | **0.0%** | **0.0%** | **0.2%** |
| 91-Day Treasury Bills | 0.1% | 0.1% | 0.2% |

**The allocation index is comprised of the S&P 500 Index, the Russell 2000 Growth Index, the Russell 2500 Value Index, the MSCI ACWI Index, the Barclays Capital Aggregate Index, the Custom Real Asset Index, Treasury Bills + 10% annually, and 91-day Treasury Bills in proportion to the weights of the respective asset class in the Pension Fund.*




# Schedule of Investment Fees

## Year Ended June 30, 2013

| Investment Managers - Pension Fund | Assets Under Management | Fees Paid |
|---|---|---|
| Western Asset Management Company | $36,974,159 | $108,329 |
| Disciplined Growth Investors | 28,325,460 | 205,222 |
| Wellington Management Company | 27,191,381 | 232,569 |
| HarbourVest Partners, LLC | 18,418,078 | 297,438 |
| North Sky Capital | 2,202,996 | 58,976 |
| Permal Capital Management, LLC | 2,773,218 | 73,403 |
| PIMCO Bravo | 6,966,869 | 99,238 |

| Other Investment Service Fees - Pension Fund | Nature of Services | Fees Paid |
|---|---|---|
| Jeffrey Slocum & Associates | Consulting | $89,129 |
| Best & Flanagan | Legal | 6,399 |
| Wells Fargo | Custodian | 54,514 |

# Brokerage Commissions Paid

## Year Ended June 30, 2013

| Brokerage Firm | Dollar Volume | Number of Shares Traded | Total Commissions | Commissions Per Share |
|---|---|---|---|---|
| Bank of America | $3,343,295 | 109,000 | $1,253 | $0.01 |
| Goldman Sachs & Company | 2,220,283 | 87,317 | 1,940 | 0.02 |
| Morgan Stanley | 1,440,328 | 49,683 | 1,167 | 0.02 |
| Credit Suisse Securities | 1,281,771 | 43,400 | 1,352 | 0.03 |
| UBS Securities | 1,253,228 | 44,892 | 851 | 0.02 |
| * Lynch Jones & Ryan | 1,077,749 | 36,400 | 1,820 | 0.05 |
| * Knight Equity Markets | 1,021,931 | 44,230 | 1,756 | 0.04 |
| JP Morgan Chase | 970,124 | 36,200 | 1,026 | 0.03 |
| Jefferies LLC | 904,625 | 29,700 | 566 | 0.02 |
| Citigroup Global Markets, Inc. | 840,431 | 32,600 | 1,202 | 0.04 |
| ISI Group | 833,232 | 28,470 | 588 | 0.02 |
| Barclays Capital | 755,406 | 28,200 | 610 | 0.02 |
| Roth Capital | 707,533 | 17,800 | 890 | 0.05 |
| Deutsche Bank Securities | 602,846 | 27,300 | 750 | 0.03 |
| Investment Technology Group | 556,612 | 14,900 | 222 | 0.01 |
| Craig Hallum | 515,372 | 12,700 | 635 | 0.05 |
| Merlin Securities | 461,745 | 40,935 | 1,671 | 0.04 |
| Wells Fargo Securities | 432,628 | 17,300 | 697 | 0.04 |
| Benchmark Company | 390,733 | 15,925 | 788 | 0.05 |
| Raymond James & Associates | 386,465 | 8,220 | 316 | 0.04 |
| RBC Capital Markets | 355,274 | 12,300 | 449 | 0.04 |
| BNY Brokerage | 354,534 | 13,050 | 598 | 0.05 |
| R W Baird | 249,858 | 9,900 | 273 | 0.03 |
| Stifel Nicolaus & Company | 240,024 | 8,710 | 364 | 0.04 |
| Feltl & Company | 229,211 | 11,600 | 580 | 0.05 |
| Dougherty | 219,717 | 6,100 | 305 | 0.05 |
| Sanford C Bernstein & Company | 199,702 | 6,400 | 113 | 0.02 |
| Freidman, Billings, Ramsey | 195,713 | 8,200 | 328 | 0.04 |
| Macquarie | 189,201 | 6,800 | 272 | 0.04 |
| CIBC World Markets, Inc. | 181,902 | 30,300 | 877 | 0.03 |
| BTIG | 175,197 | 3,700 | 142 | 0.04 |
| Keefe Bruyette & Woods | 171,157 | 11,200 | 420 | 0.04 |
| Northland Securities | 161,040 | 5,750 | 214 | 0.04 |
| Janney Montgomery Scott | 158,719 | 4,600 | 172 | 0.04 |
| Needham & Company | 145,457 | 8,300 | 357 | 0.04 |
| Mizuho Securities | 142,147 | 3,600 | 125 | 0.03 |
| William Blair & Company | 140,635 | 3,275 | 164 | 0.05 |
| Cowen & Company | 139,487 | 6,900 | 262 | 0.04 |
| Dowling & Partners, Inc. | 131,583 | 3,090 | 123 | 0.04 |
| Others (includes 51 brokerage firms) | 2,234,030 | 90,300 | 3,360 | 0.04 |
| Totals | $26,010,925 | 979,247 | $29,598 | $0.03 |

* Commission recapture broker. A portion of the total commissions paid are rebated to the Association.

# Summary of Actuarial Assumption & Methods

Investment Rate of Return*................ 8.0% per annum for the period July 1, 2012 through June 30, 2017, and 8.5% thereafter.

Asset Valuation*............................. The market value of assets adjusted by spreading over a five-year period the difference between the actual return on investments and the assumed rate of return.

Pre- and Post-retirement Mortality**.... RP-2000 Mortality Table, set back three years, projected with generational improvement from 2012. Adopted 2012.

Retirement Age**........................... Graded rates. See table below for sample rates. Adopted 2012.

Rate of Withdrawal**...................... Select and ultimate rates. Select rates are: 1st year 45%; 2nd year 20%; 3rd year 12%. See table below for sample ultimate rates. Adopted 2012.

Pay Increase and Inflation*................ Select and ultimate table with an eight-year select period. For service from hire through 7 completed years, a 7.75% salary increase is assumed. Adopted 2012.

Actuarial Cost Method*.................... Entry age normal. Actuarial gains reduce, and actuarial losses increase the unfunded actuarial accrued liability.

Post-retirement Benefit Increase.......... A one percent post-retirement benefit increase is assumed to be paid on January 1 each year, as provided in Minnesota Statutes, Section 354A.27. Adopted 2013.

Payment on Unfunded Liability*......... A level percentage of payroll each year to the statutory amortization date assuming payroll increases of 3.5% per annum. If the Actuarial Value of Assets exceeds the Actuarial Accrued Liability, the surplus amount shall be amortized over 30 years as a level percentage of payroll. Adopted 2012.

Combined Service Annuity**............. A 10% load on liabilities for active and former members. Adopted 2002.

Date of Last Experience Study............ June 2012, covering fiscal years 2007-2011. Assumptions used in the July 1, 2012 actuarial valuation are those recommended in the 2012 experience study.

*specified by state law, Minnesota Statutes, Section 356.215
**approved by the Legislative Commission on Pensions and Retirement

**Sample Annual Rates per 100 Employees:**

| Age | Retirement Rate Old/Tier I | Retirement Rate Tier II | Withdrawal Rate All Employees | Pay Increases |
|---|---|---|---|---|
| 20 | 0% | 0% | 3.50% | 6.00% |
| 25 | 0% | 0% | 3.25% | 6.00% |
| 30 | 0% | 0% | 3.00% | 6.00% |
| 35 | 0% | 0% | 2.75% | 6.00% |
| 40 | 0% | 0% | 2.50% | 5.31% |
| 45 | 0% | 0% | 2.00% | 4.63% |
| 50 | 0% | 0% | 1.50% | 3.94% |
| 55 | 7.5% | 7.5% | 0.75% | 3.25% |
| 60 | 25% | 15% | 0.00% | 3.25% |
| 65 | 35% | 30% | 0.00% | 3.25% |

# Analysis of Financial Experience

Actual financial experience will not coincide exactly with assumed financial experience because the future cannot be predicted with certainty. The annual actuarial valuations reveal the differences between actual and assumed experience in the various risk areas. Differences between actual and assumed experience result in changes in liabilities, which are called actuarial gains (if the experience was financially favorable) and actuarial losses (if the experience was financially unfavorable). In the actuarial valuations, such gains and losses reduce and increase the unfunded actuarial accrued liability.

Below are the gains and losses in accrued liabilities during the last four fiscal years resulting from differences between assumed experience and actual experience:

| | Amount of Gain (or Loss) for the Year | | | |
|---|---|---|---|---|
| **Types of Activity** | **2010** | **2011** | **2012** | **2013** |
| **Pay Increases**<br>Smaller pay increases than assumed result in an actuarial gain. Greater pay increases than assumed result in an actuarial loss. | $2,152,999 | $2,515,586 | $2,660,739 | $742,316 |
| **Investment Income**<br>Greater investment income than assumed result in an actuarial gain. Less investment income than assumed results in an actuarial loss. | ($29,239,035) | ($22,610,790) | ($28,191,456) | ($12,648,785) |
| **Mortality After Retirement**<br>Retirants living longer than assumed results in an actuarial loss. Retirants living not as long as assumed results in an actuarial gain. | (840,350) | (1,060,690) | 851,593 | (625,015) |
| **Other Items** | (29,206) | (5,259,290) | 446,734 | 2,742,917 |
| **Gain (or Loss) During Year From Financial Experience** | (27,955,592) | (26,415,184) | (24,232,390) | (9,788,567) |
| **(Increase)/Decrease in Actuarial Accrued Liability Due to Plan Amendments** | 61,646,473 | 257,363 | 0 | (25,733,739) |
| **(Increase)/Decrease in Actuarial Accrued Liability Due to Changes In Actuarial Assumptions** | 0 | 0 | (4,361,273) | 0 |
| **Composite Gain (or Loss) During Year** | $33,690,881 | ($26,157,821) | ($28,593,663) | ($35,522,306) |

# Summary of Benefit Plans

## Features Common to All Plans - Old Plan & New Plan, Tier I & Tier II

**Contributions**: Employees contribute 6.5% of covered salary. Employer contributes 6.79% of salary. (Both contribution rates increase ½% on July 1, 2013.)

**Refunds:** Equal to employee contributions plus 6% interest to June 30, 2010 and 4% interest after June 30, 2010. Payable 30 days after ceasing to render teaching service.

**Deferred Benefits:** A vested, terminated member may leave contributions in the fund until eligible for retirement. The annuity formula at time of termination is used. The benefit is increased at a stated rate of interest each year from employment termination date until the effective date of the benefit.

**Post-retirement Increase:** Eligible benefit recipients receive a post-retirement benefit increase on January 1 each year. Once the funding ratio using actuarial value of the assets equals or exceeds 90%, the increase will be equal to CPI-U, up to 5%. Until that 90% threshold is met, the post-retirement benefit increase will be 1.0% each year.

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## Old Plan – Members Hired Before July 1, 1981

**Eligibility for Retirement Benefits:**

- Full Retirement Benefits: Eligible at age 60, or if age plus years of service totals at least 90.
- Early Retirement Benefits: Eligible at age 55 with ten or more years of credited service. An early retirement reduction is applied equal to ¼% per month under full retirement age.

**Note:** Old Plan members receive a retirement benefit from the Old Plan, or from New Plan Tier I, or from New Plan Tier II, whichever is highest.

**Annual Benefit Formula:** 1.45% times high-five average salary, times years of credited service.

**Vesting:** Retirement benefits vest after 10 years of service, or at age 60.

**Disability Benefits:** Eligible after 5 years of service. Must be totally and permanently disabled from teaching. Full benefits are paid regardless of age. Termination of employment is required.

**Survivor Benefits:**

- Death Before Retirement - Refund of two times member contributions, plus interest, to surviving beneficiaries. If member had at least ten years of service at time of death, a surviving spouse may instead, elect an annuity equal to 120% of the refund amount.
- Death While Eligible to Retire - If member had at least 10 years of service and was over age 55 at death, a surviving spouse may elect to receive a 100% joint and survivor annuity of equivalent actuarial value.
- Death After Retirement - The optional annuity elected at retirement is payable. Options include a 50% joint and survivor annuity, a 100% joint and survivor annuity, or a life and term certain annuity for 5, 10, 15 or 20 years.

# Summary of Benefit Plans

## Features Common to New Plan Tier I and New Plan Tier II

**Vesting:** Retirement benefits vest after 3 years of service, or at age 65. For employees hired after June 30, 2010 retirement benefits vest after five years, or at age 65.

**Disability Benefits:** Eligible after 3 years of service. Must be totally and permanently disabled from any substantial, gainful employment. Full benefits paid regardless of age. Termination of employment with the school district is not required.

**Survivor Benefits:**

- Death Before Retirement: Refund of member contributions, plus interest, to beneficiary. If member had at least 3 years of service, a surviving spouse may elect to receive a 100% joint and survivor annuity or term certain annuity of equivalent actuarial value. A reduction is applied to the benefit amount based on the years of service and age of the member at time of death. Term certain benefits are payable to dependent children if there is no spouse.
- Death After Retirement: The optional annuity elected at retirement is payable. Options include a 50% joint and survivor annuity, a 100% joint and survivor annuity, or a life and term certain annuity for 5, 10, 15 or 20 years.

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## New Plan Tier I – Members Hired July 1, 1981 to June 30, 1989

**Eligibility for Retirement Benefits:**

- Full Retirement Benefits - Eligible at age 65, or if age plus years of service totals at least 90.
- Early Retirement Benefits - Eligible at age 55 with 3 or more years of credited service. An early retirement reduction is applied equal to ¼% per month between retirement age and age 65. Also eligible at any age with at least 30 years of credited service. In this case, an early retirement reduction is applied equal to ¼% per month between retirement age and age 62.

**Note:** New Plan Tier I members receive a retirement benefit from New Plan Tier I, or from New Plan Tier II, whichever is highest.

**Annual Benefit Formula:** Service credit before July 1, 2013 is earned at 1.2% for each of the first ten years of credited service, and 1.7% for each year over ten, times high-five average salary. Service credit after June 30, 2013 is earned at 1.4% for each of the first ten years of credited service, 1.9% for each year over ten, times high-five average salary.

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## New Plan Tier II –Members Hired After June 30, 1989

**Eligibility for Retirement Benefits**

- Full Retirement Benefits: Age at which full Social Security retirement benefits are payable, but no higher than age 66. (There is no Rule-of-90 in Tier II.)
- Early Retirement Benefits: Eligible at age 55 with 3 or more years of credited service. There is an actuarial reduction of 5-6% per year for each year between retirement age and full retirement age.

**Annual Benefit Formula:** Service credit before July 1, 2013 is earned at 1.7% per year, times high-five average salary. Service credit after June 30, 2013 is earned at 1.9% per year, times high-five average salary.

# Additions by Source

## (Pension Fund - Last Six Years)

This table shows total additions in the pension fund for the most recent six years.
All information is taken from the financial statements.

| Fiscal Year | Member Contributions and Payments | Employer Contributions | State Funding | Net Investment Income | Other | Total |
|---|---|---|---|---|---|---|
| 2008 | $2,954,062 | $2,994,086 | | ($31,209,398) | $31,173 | ($25,230,077) |
| 2009 | 2,927,260 | 2,954,026 | $346,000 | (74,430,980) | 19,769 | (68,183,925) |
| 2010 | 2,899,071 | 2,866,150 | 760,364 | 30,110,108 | 51,643 | 36,687,336 |
| 2011 | 2,779,703 | 2,798,027 | 658,535 | 39,492,523 | 12,404 | 45,741,192 |
| 2012 | 2,888,242 | 2,878,549 | 553,710 | 284,479 | 112,171 | 6,717,151 |
| 2013 | 3,050,990 | 3,013,717 | 346,000 | 30,557,601 | 11,735 | 36,980,043 |

# Deductions by Type

## (Pension Fund - Last Six Years)

This table shows total deductions in the pension fund for the most recent six years.
All information is taken from the financial statements.

| Fiscal Year | Retirement | Survivor | Disability | Refunds | Administrative | Total |
|---|---|---|---|---|---|---|
| 2008 | $19,934,499 | $1,426,239 | $218,783 | $59,144 | $487,944 | $22,126,609 |
| 2009 | 20,943,537 | 1,543,301 | 217,325 | 290,392 | 505,164 | 23,499,719 |
| 2010 | 21,744,534 | 1,689,957 | 161,700 | 116,127 | 505,672 | 24,217,990 |
| 2011 | 22,185,946 | 1,719,781 | 162,188 | 210,819 | 497,009 | 24,775,743 |
| 2012 | 22,845,086 | 1,805,076 | 156,195 | 96,935 | 628,923 | 25,532,215 |
| 2013 | 23,474,340 | 1,833,931 | 121,959 | 265,188 | 537,013 | 26,232,431 |

# Chronology of Significant Events

1909 - Legislature authorizes formation of Teachers' Retirement Fund Associations
1910 - Duluth Teachers' Retirement Fund Association incorporated
1911 - First investments in municipal bonds
1921 - Fund put on actuarial reserve basis. Formula is 1/70 x years of service x high 10 year average salary. Age 55 normal.
1921 - First home mortgage was made
1943 - First equity investment made
1948 - Normal retirement age raised to age 60 over next 5 years
1957 - Social Security was adopted for all Duluth educators
- Formula is 1/140 x high 10 years average salary x years of service. Additional contributions allowed.

1964 - Tax Shelter 403(b) program started and qualified by the IRS. Bond account is only option.
1965 - Last direct home mortgage issued by the Association
1971 - Formula is 1.15% x high 5 average salary x years of service. Full retirement: age 60
1973 - Tax shelter equity account created
1978 - Part-time and hourly educators gained Social Security and pension coverage
1981 - Formula is 1.25% x high 5 average salary x years of service. Employee contribution rate 4.5%.
- Tier I formula instituted for members hired after 6/30/81
- Tax shelter money market account created

1983 - Contributions to the fund are treated as tax deferred for Federal income tax
1985 - Contributions to the fund are treated as tax deferred for State income tax
- Lump-sum cost of living adjustment (COLA) established. Unit value $34

1989 - Tier II formula instituted for members hired after 6/30/89
1992 - Minimum investment earnings removed for COLA. Waiting period for COLA reduced from 3 to 1 year.
1995 - Lump-sum COLA discontinued. Final unit value: $55
- Benefit formulas increased by 0.13%; Lump-sum COLA replaced with 2% COLA plus excess earnings.
- Employee contribution rate increased from 4.5% to 5.5%
- Membership closed to Lake Superior College staff hired after June 30

1997 - Benefit formulas increased by 0.07%. Annual State aid payments of $486,000 initiated.
- DTRFA moves to new office building on Central Entrance.

2001 - Last state aid payment received October 2001
2002 - Charter school teachers in Duluth no longer eligible for membership.
2008 - Direct State aid payment of $346,000 restored.
2010 - Legislation passed to raise contribution rates, suspend COLA, increase vesting period, reduce interest paid on refunds.
2013 - Legislation passed to raise contribution rates, restore a 1% COLA, increase benefit formula, revise early retirement reduction factors in the Tier II plan, increase state aid by $6 million in fiscal year 2014 and 2015.

# Historical Information - Pension Fund

| Fiscal Year | Actuarial Value of Assets | Actuarial Accrued Liabilities | Percent Funded | Rate of Return | Membership Active | Membership Retired | Annual Benefits |
|---|---|---|---|---|---|---|---|
| 2013 | $190,117,000 | $352,143,000 | 54.0 % | 16.7 % | 873 | 1,445 | $25,430,230 |
| 2012 | 206,833,000 | 326,244,000 | 63.4 | -0.2 | 919 | 1,386 | 24,806,357 |
| 2011 | 235,072,000 | 321,065,000 | 73.2 | 21.7 | 1,006 | 1,344 | 24,067,915 |
| 2010 | 255,309,000 | 312,650,000 | 81.7 | 17.0 | 1,054 | 1,295 | 23,596,191 |
| 2009 | 279,256,000 | 364,811,000 | 76.6 | -26.9 | 1,016 | 1,264 | 22,704,163 |
| 2008 | 298,067,000 | 363,044,000 | 82.1 | -10.6 | 1,140 | 1,243 | 21,579,521 |
| 2007 | 288,265,000 | 332,217,000 | 86.8 | 19.2 | 1,150 | 1,227 | 20,266,573 |
| 2006 | 270,926,000 | 322,229,000 | 84.1 | 11.0 | 1,174 | 1,190 | 19,319,594 |
| 2005 | 268,481,000 | 310,924,000 | 86.4 | 8.7 | 1,164 | 1,153 | 18,368,390 |
| 2004 | 276,949,000 | 301,704,000 | 91.8 | 17.9 | 1,178 | 1,137 | 17,406,336 |
| 2003 | 278,467,000 | 291,109,000 | 95.7 | 3.7 | 1,373 | 1,107 | 17,008,619 |
| 2002 | 280,515,000 | 279,428,000 | 100.4 | -8.3 | 1,276 | 1,085 | 16,074,805 |
| 2001 | 273,618,000 | 254,255,000 | 107.6 | -8.2 | 1,420 | 1,058 | 14,514,206 |
| 2000 | 251,007,000 | 241,899,000 | 103.8 | 26.5 | 1,441 | 996 | 12,449,327 |
| 1999 | 218,698,000 | 220,540,000 | 99.2 | 12.0 | 1,509 | 939 | 11,112,146 |
| 1998 | 187,482,000 | 197,078,000 | 95.0 | 16.5 | 1,437 | 910 | 9,869,169 |
| 1997 | 170,059,000 | 197,820,000 | 86.0 | 17.7 | 1,416 | 879 | 8,800,674 |
| 1996 | 157,007,000 | 189,518,000 | 82.8 | 14.9 | 1,415 | 860 | 8,825,142 |
| 1995 | 142,852,000 | 173,965,000 | 82.1 | 20.0 | 1,512 | 841 | 7,868,705 |
| 1994 | 133,632,000 | 137,042,000 | 97.5 | 2.0 | 1,484 | 832 | 8,133,891 |
| 1993 | 130,856,000 | 132,700,000 | 98.6 | 13.5 | 1,453 | 822 | 6,044,302 |
| 1992 | 116,492,000 | 124,140,000 | 93.8 | 12.4 | 1,558 | 728 | 5,552,167 |
| 1991 | 105,087,000 | 117,582,000 | 89.4 | 10.0 | 1,615 | 694 | 5,284,465 |
| 1990 | 97,187,000 | 103,824,000 | 93.6 | 10.5 | 1,553 | 676 | 5,014,008 |
| 1989 | 86,539,000 | 99,899,000 | 86.6 | 13.7 | 1,620 | 668 | 3,780,247 |
| 1988 | 76,279,000 | 90,759,000 | 84.0 | -6.3 | 1,578 | 665 | 4,644,406 |
| 1987 | 75,130,000 | 85,504,000 | 87.9 | 20.9 | 1,605 | 665 | 3,994,779 |
| 1986 | 64,673,000 | 78,011,000 | 82.9 | 33.4 | 1,251 | 608 | 3,575,077 |
| 1985 | 53,839,000 | 71,154,000 | 75.7 | 29.3 | 1,183 | 593 | 3,014,161 |
| 1984 | 47,859,000 | 73,174,000 | 65.4 | -4.0 | 1,137 | 562 | 2,323,413 |
| 1983 | 42,901,000 | 63,631,000 | 67.4 | 35.0 | 1,119 | 557 | 2,215,013 |
| 1982 | 39,004,000 | 58,568,000 | 66.6 | 5.8 | 1,173 | 531 | 2,163,562 |
| 1981 | 35,984,924 | 46,786,496 | 76.9 | 12.5 | 1,221 | 508 | 1,827,912 |
| 1980 | 32,102,869 | 42,014,869 | 77.3 | 11.0 | 1,268 | 501 | 1,765,742 |
| 1979 | 29,421,634 | 37,529,680 | 78.4 | 10.0 | 1,272 | 494 | 1,731,360 |
| 1978 | 27,999,592 | 35,738,048 | 78.3 | | 1,182 | 494 | 1,630,382 |
| 1977 | 26,703,470 | 34,484,488 | 79.7 | | 1,207 | 483 | 1,513,682 |
| 1975 | 23,537,352 | 29,438,620 | 80.0 | | 1,173 | 487 | 1,426,309 |
| 1973 | 22,635,801 | 24,463,370 | 92.5 | | 1,136 | 432 | 1,203,739 |
| 1971 | 19,782,599 | 25,644,571 | 77.1 | | 1,158 | 378 | 977,952 |
| 1969 | 18,893,566 | 16,995,875 | 111.2 | | 1,159 | 331 | 778,023 |
| 1967 | 15,989,940 | 15,193,619 | 105.2 | | 939 | 315 | 633,374 |
| 1965 | 13,383,460 | 13,297,963 | 100.6 | | 874 | 285 | 489,480 |
| 1962 | 10,793,087 | 11,530,817 | 93.6 | | 775 | 286 | 467,317 |
| 1959 | 9,149,200 | 10,396,897 | 88.0 | | 716 | 242 | 344,378 |
| 1954 | 6,542,424 | 8,202,803 | 79.8 | | 632 | 198 | 234,172 |
| 1952 | 5,603,225 | 7,035,678 | 79.6 | | 575 | 172 | 176,255 |
| 1949 | 4,511,251 | 5,710,673 | 79.0 | | 565 | 167 | 160,999 |
| 1946 | 3,894,364 | 5,632,563 | 69.1 | | 581 | 125 | 112,672 |
| 1943 | 3,530,411 | 4,736,725 | 74.5 | | 615 | 111 | 97,786 |
| 1940 | 3,184,300 | 4,161,948 | 76.5 | | 678 | 86 | 77,302 |
| 1937 | 2,790,459 | 3,718,979 | 75.0 | | 690 | 67 | 50,421 |
| 1934 | 2,385,690 | 3,360,525 | 71.0 | | 713 | 53 | 38,386 |
| 1931 | 1,787,097 | 2,762,428 | 64.7 | | 736 | 46 | 27,258 |
| 1928 | 1,202,626 | 2,168,376 | 55.5 | | 724 | 42 | 21,009 |
| 1925 | 714,317 | 1,700,474 | 42.0 | | 679 | 39 | 17,533 |
| 1922 | 313,523 | 1,287,310 | 24.4 | | 587 | 30 | 12,844 |
| 1919 | 95,879 | 836,550 | 11.5 | | | | |
| 1911 | 7,725 | | | | | | |