State of Illinois
State Universities Retirement System

Auditor's Report on Allocation of Pension Amounts

For the Year Ended June 30, 2017
Performed as Special Assistant Auditors for
the Auditor General, State of Illinois

BKD LLP
CPAs & Advisors

State of Illinois
State Universities Retirement System
Auditor's Report of Allocation of Pension Amounts
For the Year Ended June 30, 2017

Table of Contents

State of Illinois
State Universities Retirement System
Auditor’s Report of Allocation of Pension Amounts
For the Year Ended June 30, 2017

System Officials

Executive Director	Mr. W. Bryan Lewis (7/1/16 – 7/5/16) Mr. Martin Noven (11/2/16 – present)
Interim Executive Director	Mr. William Mabe (7/1/16 – 11/14/16)
Chief Financial Officer	Ms. Phyllis Walker
Chief Investment Officer	Mr. Daniel Allen (7/1/16 – 7/29/16)
Interim Chief Investment Officer	Mr. Doug Wesley (6/10/16 – 3/16/17)
Chief Investment Officer	Mr. Doug Wesley (3/17/17 – present)
General Counsel	Ms. Bianca Green
Director of Internal Audit	Mr. Steven Hayward
Chairperson	Mr. Tom Cross
Vice Chairman	Mr. Dorinda Miller
Treasurer	Mr. John Engstrom
Board of Trustees	Mr. Aaron Ammons Mr. Dennis Cullen Mr. Fred Giertz Mr. Paul Johnson, Jr. (7/1/16 – 5/22/17) Mr. Francis Idehen, Jr. Mr. Steven Rock Mr. Antonio Vasquez Mr. Mark Cozzi (6/2/17 – present)

Office Location

1901 Fox Drive
Champaign, Illinois 61820

State of Illinois
State Universities Retirement System
Auditor's Report of Allocation of Pension Amounts
For the Year Ended June 30, 2017

Summary

The audit of the accompanying Schedule of Allocation and Schedule of Pension Amounts (Schedules) of the State of Illinois, State Universities Retirement System (System) was performed by **BKD, LLP**.

Based on their audit, the auditors expressed an unmodified opinion on the System's Schedules.

BKD LLP
CPAs & Advisors
225 N. Water Street, Suite 400 // Decatur, IL 62523-2326
217.429.2411 // fax 217.429.6109 // bkd.com

Independent Auditor's Report

Honorable Frank J. Mautino
Auditor General, State of Illinois
Springfield, Illinois
and
Board of Trustees
State Universities Retirement System
Champaign, Illinois

Report on the Pension Schedules

As Special Assistant Auditors for the Auditor General, we have audited the accompanying Schedule of Allocation of the State Universities Retirement System, as of and for the year ended June 30, 2017, and the related notes. We have also audited the total for all entities of the columns titled beginning net pension liability, ending net pension liability, total deferred outflows of resources, total deferred inflows of resources, and total pension expense subject to allocation (specified column totals) included in the accompanying Schedule of Pension Amounts (Schedules) of the System as of and for the year ended June 30, 2017 and the related notes.

Management's Responsibility for the Schedules

Management is responsible for the preparation and fair presentation of these schedules 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 the schedules that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on the Schedule of Allocation and the specified column totals included in the Schedule of Pension Amounts 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 Schedule of Allocation and specified column totals included in the Schedule of Pension Amounts are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Schedule of Allocation and specified column totals included in the Schedule of Pension Amounts. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the Schedule of Allocation and specified column totals in the Schedule of Pension Amounts, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the System's preparation and fair presentation of the Schedule of Allocation and specified column totals included in the Schedule of Pension Amounts 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 System'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 Schedule of Allocation and specified column totals included in the Schedule of Pension Amounts.

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 Schedules referred to above, present fairly, in all material respects, the employer allocations as of and for the year ended June 30, 2017, and total beginning net pension liability, total ending net pension liability, total deferred outflows of resources, total deferred inflows of resources, and total pension expense for the total of all participating entities for the System as of and for the year ended June 30, 2017, in accordance with accounting principles generally accepted in the United States of America.

Other Matter

We have audited, in accordance with auditing standards generally accepted in the United States of America, the financial statements of the System as of and for the year ended June 30, 2017, and our report thereon, dated December 12, 2017, expressed an unmodified opinion on those financial statements.

We have previously audited the System's 2016 financial statements, and we expressed an unmodified audit opinion in our report dated December 12, 2016. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2016, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Restriction on Use

Our report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, the Comptroller, System management, the Board of Trustees, and System Employers and their auditors and is not intended to be and should not be used by anyone other than these specified parties.

SIGNED ORIGINAL ON FILE

Decatur, Illinois
January 2, 2018

State Universities Retirement System

Schedule of Allocation

As of and for the Years Ended June 30, 2017 and 2016

Entity	FY 2017 Actual Contribution	Allocation Percentage	FY 2016 Actual Contribution	Allocation Percentage
State of Illinois	$ 1,612,164,501	100%	$ 1,542,946,474	100%
Total	$ 1,612,164,501	100%	$ 1,542,946,474	100%

State Universities Retirement System

Schedule of Pension Amounts

As of and for the Year Ended June 30, 2017

and Beginning Net Pension Liability as of July 1, 2016

			Deferred Outflows of Resources				
Entity	**Beginning Net Pension Liability**	**Ending Net Pension Liability**	**Differences Between Expected and Actual Experience**	**Net Differences Between Projected and Actual Investment Earnings**	**Changes of Assumptions**	**Changes in Proportion and Differences Between Contributions and Proportionate Share of Contributions**	**Total Deferred Outflows of Resources**
State of Illinois	$25,965,271,744	$25,481,105,955	$ 139,193,227	$ 1,036,195,939	$ 205,004,315	$ —	$ 1,380,393,481
Total	$25,965,271,744	$25,481,105,955	$ 139,193,227	$ 1,036,195,939	$ 205,004,315	$ —	$ 1,380,393,481

Deferred Inflows of Resources					Pension Expense		
Differences Between Expected and Actual Experience	Net Differences Between Projected and Actual Investment Earnings	Changes of Assumptions	Changes in Proportion and Differences Between Contributions and Proportionate Share of Contributions	Total Deferred Inflows of Resources	Proportionate Share of Allocable Plan Pension Expense	Net Amortization of Deferred Amounts from Changes in Proportion and Differences Between Contributions and Proportionate Share of Contributions	Total Pension Expense Subject to Allocation
$ 1,170,771	$ 941,575,112	$ 259,657,577	$ —	$ 1,202,403,460	$ 2,412,918,129	$ —	$ 2,412,918,129
$ 1,170,771	$ 941,575,112	$ 259,657,577	$ —	$ 1,202,403,460	$ 2,412,918,129	$ —	$ 2,412,918,129

State Universities Retirement System

Notes to the Schedules of Allocation and Pension Amounts

Year Ended June 30, 2017

The State Universities Retirement System (SURS or the System) is the administrator of a cost-sharing, multiple-employer defined benefit plan. SURS was established on July 21, 1941, to provide retirement annuities and other benefits for staff members and employees of the state universities, certain affiliated organizations and certain other state educational and scientific agencies and for survivors, dependents, and other beneficiaries of such employees.

GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, defines special funding situations as circumstances in which a nonemployer entity is legally responsible for making contributions directly to a pension plan that is used to provide pensions to the employees of another entity or entities and either (1) the amount of the contributions for which the nonemployer entity is legally responsible is not dependent upon one or more events unrelated to pensions or (2) the nonemployer is the only entity with a legal obligation to make contributions directly to a pension plan. The State of Illinois is considered a nonemployer contributing entity. The Schedule of Allocations and Schedule of Pension Amounts include amounts for the State of Illinois. Within these schedules, the term "employer" encompasses both the employers and the State (nonemployer contributing entity).

Defined Benefit Plan

SURS is included in the State of Illinois' financial reports as a component unit. SURS is governed by Chapter 40, Act 5, Article 15, of the Illinois Compiled Statutes. These statutes assign the authority to establish and amend the benefit provisions of the plan to the State Legislature. Operation of the System and the direction of its policies are the responsibility of the Board of Trustees of the System. It is also these statutes that define the scope of SURS' reporting entity. There are no statutory provisions for termination of the System. The Illinois Constitution provides that the pension obligation of the state shall be an enforceable contractual relationship, the benefits of which shall not be diminished or impaired.

Benefit Provisions

The traditional defined benefit plan was established in 1941. An alternative defined benefit program known as the portable benefit package and a defined contribution plan was established effective January 1, 1998 due to the enactment of Public Act 90-0448. A summary of the benefit provisions can be found in the System's comprehensive annual financial report (CAFR) Notes to the Financial Statements. The System's CAFR can be accessed on their website at www.SURS.org.

Summary of Significant Accounting Policies

Nature of Schedules

Employers participating in a cost-sharing pension plan, and any nonemployer contributing entities that meet the definition of a special funding situation, are required to recognize their proportionate share of the collective pension amounts for pension benefits provided to members through the SURS plan. GASB Statement No. 68, paragraph 92, states that in determining the employer's proportion of the collective net pension liability (NPL), the basis should be consistent with the manner in which contributions to the pension plan, excluding those to separately finance specific liabilities of the individual employer to the Plan, as determined, which is consistent with paragraphs 48-51. GASB 68, paragraph 92 further states that in determining the nonemployer's proportion of the collective net pension liability (NPL) and corresponding pension amounts the Plan should follow the Plan terms to determine the specific relationship of the contribution requirements of the nonemployer contributing entity to those of the employer and other contributing entities.

The State's contributions to the State Universities Retirement System are determined through actuarial valuations on an annual basis. Under the Illinois Compiled Statutes (40 ILCS 5/15-155), the actuarially determined contribution (Statutory Contribution) from the State of Illinois is calculated by an actuary in accordance with the Statutory Funding Plan. If an employee is paid from trust, grant or federal funds, the employer must make pension contributions from those funds sufficient to cover the normal costs of the employee's pension benefits in accordance with the Illinois Compiled Statutes (40 ILCS 5/15-155(b)). Certain participating employers (alumni associations, foundations, and other affiliated organizations) are not financed by the statutory contribution from the State and pay an employer contribution equal to the normal cost of the employee's pension benefits. These employer contributions are based on a percentage of earnings relating to normal cost, as determined through an annual actuarial valuation process. The employer normal cost for fiscal year 2017 was 12.53 percent of employee creditable covered payroll. The normal cost is equal to the value of current year's pension benefit and does not include any allocation for the past unfunded liability or interest on the unfunded liability. In accordance with Section 15-155(b), SURS participating employers that pay the full normal cost have met their requirement towards the pension liability.

The Schedule of Allocation presents the actual fiscal year 2017 contributions used within the proportionate share calculation for the nonemployer contributing entity (State of Illinois) and respective allocation percentage. For purposes of allocating the beginning net pension liability, the System utilized contributions reported during fiscal year 2016.

The Schedule of Pension Amounts presents the proportionate share of the total beginning and ending net pension liability, total deferred outflows of resources, total deferred inflows of resources, and corresponding pension expense to be allocated to the State of Illinois. The pension expense includes the amortization of any reported differences between expected and actual economic and demographic experience, differences between projected and actual investment earnings (net) on Plan investments, and the impact of changes of assumptions about future economic or demographic factors or other inputs. The total pension expense subject to allocation is adjusted for contributions made to the System by individual employers to liquidate specific liabilities the employers owe to the plan. The types of employer specific liabilities are those under Section 15.139.5(e) relating to contributions payable due to member earning increases exceeding 6 percent during the final rate of earnings period, contributions payable due to the employment of "affected annuitants" or return to work annuitants, and contributions payable for trust, grant or federal fund positions.

Measurement Focus and Basis of Accounting

The financial transactions are recorded using the economic resources measurement focus and the accrual basis of accounting. Employer and nonemployer contributing entity contributions are recognized as revenue when due pursuant to statutory or contractual requirements.

Use of Estimates in the Preparation of the Schedules

The preparation of the SURS Schedules in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts, and changes therein, and disclosures. Actual results could differ from those estimates and differences could be material. The System uses an actuary to determine the total pension liability for the defined benefit plan and to calculate the actuarially determined contributions of the State and employers.

Basis of Allocation

In determining the proportionate share of the net pension liability and corresponding employer pension amounts for a cost-sharing plan, the basis should be consistent with the manner in which contributions to the Plan, excluding those to separately finance specific liabilities of an individual employer are determined. The System has determined that the actual contributions made to the Plan during fiscal year 2017 are appropriate as the basis because they are representative of future contributions. GASB Statement No. 68, states that special funding situations are defined as circumstances in which a nonemployer entity (State of Illinois) is legally responsible for making contributions directly to a pension plan (SURS) that is used to provide pensions to the employees of another entity or entities (participating SURS employers) and the amount of contributions is not dependent upon one or more events unrelated to pensions. Chapter 40, Act 5, Article 15-156 of the Illinois Compiled Statutes states the obligation of the state as following:

a) The payment of (1) the required State contributions, (2) all benefits granted under this system and (3) all expenses in connection with the administration and operation thereof are obligations of the State of Illinois to the extent specified in this Article.

b) Beginning July 1, 2014, the State shall be obligated to contribute to the System in each State fiscal year an amount not less than the sum of (i) the State's normal cost for the year and (ii) the portion of the unfunded accrued liability assigned to that year by law.

The net pension liability (NPL) is the portion of the actuarial present value of projected benefit payments related to past periods. The NPL to the nonemployer contributing entity (the State) is based on the allocation percentage from the Schedule of Allocation (100 percent).

The fiscal year 2017 actual contribution total used as the denominator for the allocation calculation in the Schedule of Allocation can be reconciled to the System's fiscal year 2017 CAFR as follows:

Defined Benefit Plan Employer Contributions – CAFR total	$ 1,650,550,708
Funding for excess benefit arrangements	6,409,288
Employer specific liability payments	(3,311,917)
SURS employer contributions for SURS employees	(996,974)
Employer contributions for federal/trust/grants which only pay normal cost	(40,439,991)
Miscellaneous revenue from nonemployer sources	(46,613)
Total contributions – Schedule of Allocation	$ 1,612,164,501

The employers will be required to recognize revenue (on-behalf contributions) and expense resulting from the special funding situation. Revenue should be an amount equal to the nonemployer contributing entities total proportionate share of collective pension expense that is associated with the employer. This information is not included within this report but unaudited information will continue to be provided to each employer on an annual basis by the System.

Pension Expense and Amortization of Pension Expense

Pension expense, as well as deferred outflows of resources and deferred inflows of resources related to pensions, should be recognized for the employers' (and nonemployer contributing entity's) proportionate shares of collective pension expense and collective deferred outflows of resources and deferred inflows of resources related to pensions.

Deferred outflows of resources are the consumption of net position that is applicable to future reporting periods. Deferred outflows of resources have a positive effect on net position. Deferred inflows of resources are the acquisition of net position that is applicable to future reporting periods. Deferred inflows of resources have a negative effect on net position. Other than differences between projected and actual investment earnings, deferred inflows and outflows of resources are recognized in pension expense beginning in the current period, using a straight line method over a closed period equal to the average of the expected remaining service lives of all employees that are provided with pensions through the System (active and inactive), determined as of the beginning of the measurement period. Net deferred inflows (or outflows) of resources pertaining to differences between projected and actual investment earnings are similarly recognized over a closed five year period.

State Universities Retirement System

Notes to the Schedules of Allocation and Pension Amounts

Year Ended June 30, 2017

The pension amounts allocated to the State of Illinois are based on total contributions to the System except for contributions from employers for employees paid through trusts, grants or federal funds and any other specific liabilities of the individual employers to the plan. The employer contributions related to trusts, grants or federal funds are made in accordance with State statute (Chapter 40, Act 5, Article 15-155(b)) which provides that these contributions are made based on the normal cost rate and meet the definition of funding current period cost and are not available to pay past service cost. The types of employer specific liabilities are those under Section 15.139.5(e) relating to contributions payable due to earning increases exceeding 6 percent during the final rate of earnings period and contributions payable due to the employment of “affected annuitants” or return to work annuitants.

The components of pension expense are:

Service cost	$ 658,715,745
Interest on the Total Pension Liability	2,951,246,535
Employee contributions	(278,642,830)
Projected earnings on plan investments	(1,214,561,768)
Pension plan administrative expenses	14,847,009
Recognition of outflow (inflow) of resources due to liabilities	398,540,422
Recognition of outflow (inflow) of resources due to assets	(78,840,777)
Total pension expenses	2,451,304,336
Reconciling items:	
Funding for excess benefit arrangements	6,409,288
Employer specific liability payments	(3,311,917)
SURS employer contributions for SURS employees	(996,974)
Employer contributions for federal/trust/grants	(40,439,991)
Miscellaneous revenue from nonemployer sources	(46,613)
Total pension expenses subject to allocation – Schedule of Pension Amounts	$ 2,412,918,129

The average of the expected remaining service lives of all members for FY 2017 is 2.9031 years.

State Universities Retirement System

Notes to the Schedules of Allocation and Pension Amounts

Year Ended June 30, 2017

Net Pension Liability

The net pension liability for SURS for fiscal year 2017 is calculated as set forth in the following table:

Net pension liability (beginning) – July 1, 2016	$ 25,965,271,744
Total pension expense	2,451,304,336
Change in deferred outflows of resources	(720,367,465)
Change in deferred inflows of resources	(564,551,910)
Defined Benefit Plan Employer Contributions – CAFR total	(1,650,550,710)
Net pension liability (ending) – June 30, 2017	$ 25,481,105,995

Requests for Information

SURS is considered a component unit of the State of Illinois' financial reporting entity and is included in the state's financial reports as a pension trust fund. SURS is governed by Section 5/15, Chapter 40 of the *Illinois Compiled Statutes*. SURS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by accessing the website at www.SURS.org.