



April 15, 2011

Mr. Aristotle Hutras, Director
Ohio Retirement Study Council
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Dear Aris:

In accordance with Section 3307.041, Revised Code, STRS Ohio is submitting the proposed 2011-2012 fiscal year budgets. The attached information is composed of three parts in the uniform format adopted by the five Ohio public retirement systems.

RETIREMENT BOARD CHAIR
TIM MYERS

RETIREMENT BOARD VICE CHAIR
JAMES MCGREEVY

EXECUTIVE DIRECTOR
MICHAEL J. NEHF

- The first page is a statement of planned operating and capital expenditures, including comparisons to the 2010–2011 fiscal year budget.
- The second page is a separate schedule of Retirement Board-related budget items. These anticipated board expenses, which reflect a 10.45% decrease from this year, are included in the overall organization operating budget.
- The third page is a three-year historical summary of investment assets and related management costs.

The proposed operating budget for next year (July 1, 2011–June 30, 2012) reflects no increase over the current year's budget and no increase in personnel. Although total planned expenditures are reduced, the budget provides funds for several new initiatives, including an information technology controls audit and an asset/liability study of the investment funds. Areas of significant decrease include custodial banking fees, computer technology and communications. The proposed capital budget provides for additional technology upgrades and continued facilities maintenance.

These budgets were presented to the Retirement Board at its April 14 meeting. Overall, the proposed budgets continue to provide the resources we need to pay timely and accurate pension and health care benefits to members; successfully manage investment assets; and ensure we meet all fiduciary responsibilities and legal requirements. Additionally, the proposed budgets comply with all Retirement Board policies and demonstrate to members that STRS Ohio is managing operating expenses prudently.

We anticipate making a formal presentation to the ORSC in May. Please feel free to contact me if you need additional information.

Sincerely,

Michael J. Nehf
Executive Director

Enclosure

**Ohio Retirement System Budget Presentation to ORSC
STRS Ohio 2011–2012 Budget to 2010–2011 Budget
and Increase (Decrease)**

| Budget Periods | 7/01/2011- 6/30/2012 2012 Budget | 7/01/2010- 6/30/2011 2011 Budget | Increase (Decrease) | % Increase/ Decrease |
|--|--|--|------------------------|-------------------------|
| Personnel | \$ 66,866,000 | \$ 66,244,000 | \$ 622,000 | 0.94% |
| Salaries and Wages | 52,976,900 | 52,785,400 | 191,500 | 0.36% |
| OPERS Contributions | 6,987,600 | 7,039,000 | (51,400) | -0.73% |
| Health Insurance | 5,939,200 | 5,423,500 | 515,700 | 9.51% |
| Miscellaneous Expenses | 962,300 | 996,100 | (33,800) | -3.39% |
| Professional Services | 8,393,800 | 8,498,400 | (104,600) | -1.23% |
| Actuarial | 296,400 | 293,000 | 3,400 | 1.16% |
| Audit | 165,000 | 261,000 | (96,000) | -36.78% |
| Custodial Banking Fees | 2,075,000 | 2,500,000 | (425,000) | -17.00% |
| Investment Consulting | 3,400,000 | 3,280,000 | 120,000 | 3.66% |
| Other Consulting | 2,159,400 | 1,879,400 | 280,000 | 14.90% |
| Banking Expense | 298,000 | 285,000 | 13,000 | 4.56% |
| Communications Expense | 3,006,700 | 3,440,800 | (434,100) | -12.62% |
| Printing and Postage | 2,375,000 | 2,765,000 | (390,000) | -14.10% |
| Telephone | 410,500 | 443,000 | (32,500) | -7.34% |
| Member/Employer Education | 217,200 | 225,700 | (8,500) | -3.77% |
| Other Communications | 4,000 | 7,100 | (3,100) | -43.66% |
| Other Operating Expense | 9,178,400 | 9,258,600 | (80,200) | -0.87% |
| Conferences and Education | 300,500 | 293,600 | 6,900 | 2.35% |
| Travel | 620,300 | 628,900 | (8,600) | -1.37% |
| Computer Technology | 4,636,700 | 4,730,100 | (93,400) | -1.97% |
| Other Operating | 3,295,900 | 3,274,000 | 21,900 | 0.67% |
| Ohio Retirement Study Council | 260,000 | 260,000 | 0 | 0.00% |
| Treasury of State Warrant Clearing Charges | 5,000 | 12,000 | (7,000) | -58.33% |
| Attorney General Charges | 60,000 | 60,000 | 0 | 0.00% |
| Net Building Expense | \$ 2,612,900 | \$ 2,663,800 | \$ (50,900) | -1.91% |
| Total Operating Budget | \$ 90,057,800 | \$ 90,105,600 | \$ (47,800) | -0.05% |
| Total Capital Budget | \$ 2,277,100 | \$ 2,101,000 | \$ 176,100 | 8.38% |
| Building Improvements | 506,000 | 575,000 | | |
| Building Maintenance Equipment | 64,400 | 66,000 | | |
| Infrastructure and Upgrades | 1,706,700 | 1,320,000 | | |
| General Capital | 0 | 140,000 | | |



**Ohio Retirement System Budget Presentation to ORSC
STRS Ohio Board Budget**

| | <u>2012 Budget</u> | <u>2011 Budget</u> | <u>Increase (Decrease)</u> | <u>% Increase Decrease</u> |
|---------------------------------|------------------------|------------------------|--------------------------------|--------------------------------|
| Board Expenses | | | | |
| Board Education and Travel | \$ 25,000 | \$ 26,000 | \$ (1,000) | -3.85% |
| Travel to Attend Board Meetings | 25,000 | 27,000 | (2,000) | -7.41% |
| Other Board Expense | <u>10,000</u> | <u>14,000</u> | <u>(4,000)</u> | -28.57% |
| Total Board Expense | <u>\$ 60,000</u> | <u>\$ 67,000</u> | <u>\$ (7,000)</u> | -10.45% |



Ohio Retirement System Budget Presentation to ORSC
STRS Ohio Historical Investment Expenses

| | <u>Fiscal 2010</u> Actuals | <u>Fiscal 2009</u> Actuals | <u>Fiscal 2008</u> Actuals |
|---|---------------------------------|---------------------------------|---------------------------------|
| Investment Assets | | | |
| Total Internally Managed Assets | \$ 44,322,557,000 | \$ 39,794,093,000 | \$ 53,072,696,000 |
| Total Externally Managed Assets | <u>12,517,776,000</u> | <u>12,796,110,000</u> | <u>17,354,859,000</u> |
| Total Investment Assets * | <u>\$ 56,840,333,000</u> | <u>\$ 52,590,203,000</u> | <u>\$ 70,427,555,000</u> |
| Investment Expenses | | | |
| Total Internal Investment Expenses | \$ 27,201,004 | \$ 31,095,248 | \$ 32,150,725 |
| Total External Investment Expenses | 129,794,675 | 126,050,499 | 127,228,140 |
| Investment Consulting | 745,800 | 674,702 | 679,791 |
| Brokerage/Commissions | 17,726,451 | 19,398,838 | 23,152,262 |
| Custodian Fees | <u>3,287,624</u> | <u>3,154,044</u> | <u>4,917,680</u> |
| Total Investment Expenses | <u>\$ 178,755,554</u> | <u>\$ 180,373,331</u> | <u>\$ 188,128,598</u> |
| Total Investment Expenses as a | | | |
| Percent of Total Investment Assets | 0.31% | 0.34% | 0.27% |

* Real estate debt is removed from investment assets.



State Teachers Retirement System of Ohio (STRS Ohio) Operating Budget for Fiscal 2012

Overview

The proposed operating **budget for fiscal 2012 reflects a slight decrease** from the current year's budgeted amount. As noted in the budget sent to the ORSC, the proposed budget, which goes into effect on July 1, 2011, totals \$90,057,800 compared to \$90,105,600 for this year. This budget supports the business needs of STRS Ohio and enables us to properly manage and operate the retirement benefit and health care programs we're charged by statute to perform. The budget:

- Does not increase current associate head count.
- Reflects significant decreases in expenditures for custodial banking fees, computer technology and communications.
- Provides for an information technology controls audit.
- Supports an asset/liability study of the investment funds.
- Recognizes that STRS Ohio associates do not receive step increases or cost-of-living adjustments, and that most associates have not received any type of increase to their salary in three years, since July 1, 2008. Thus, the budget includes a 3% merit increase for eligible associates. (Please note: Merit increases are not awarded "across the board," but are based on a written evaluation of each associate's performance by his/her supervisor.)

Budget/Operational Transparency

STRS Ohio's budget-to-actual expenditures status per 73 separate line items is reviewed at monthly Retirement Board meetings, and also posted on STRS Ohio's Web site for members and others to review. Information is also included in STRS Ohio newsletters, including the monthly *Board News* (most recently, the April 2011 issue), and communicated via the STRS Ohio e-mail news service, which currently has almost 140,000 subscribers.

Budget Components

Like any service organization, the majority of STRS Ohio's operating expenditures are in salaries and benefits. Day in and day out, STRS Ohio staff makes a concerted effort to control operating costs while providing the resources necessary to (1) pay timely and accurate pension and health care benefits; (2) successfully manage investment assets; and (3) ensure we meet all fiduciary responsibilities and legal requirements. **Staff size has decreased more than 17% since the peak staffing levels in fiscal 2004** (reflecting a reduction of more than 115 full- and part-time associates). However, improved efficiencies have enabled this smaller staff to compile a list of significant accomplishments that demonstrate our commitment to our mission of partnering with STRS Ohio members in providing financial performance and member service that assures financial security for current and future retirees.

During the past several years, these accomplishments include:

- Proposing a detailed and reasonable plan to return the pension fund to a 30-year funding period without additional contributions from employers.
- Achieving a total investment fund return of 13.54% for fiscal year 2010 and out-performing the benchmark return by 0.26%, while realizing a savings of approximately \$100 million in outside money management fees due to significant management of investment assets in-house. This year's return, as of April 30, is 23.5%.
- Meeting with members about their benefits, including 20,000 attendees at member education programs, 18,000 benefit counseling sessions and more than 300,000 calls to STRS Ohio's Member Services Center.
- Participating in a Medicare Advantage Plan, programs that support the use of generic drugs and a Medicare Part D prescription drug plan — all of which helped stretch participants' health care dollars and extend the solvency of the separate health care fund to 2024.

(continued)

- Working with constituent groups and educating members, legislators and the media about the necessity for changes to pension plan design, including meeting with more than 7,500 members around the state.
- Developing a strategic plan for the organization.
- Replacing STRS Ohio’s obsolete pension management computer system.
- Maintaining the trust and confidence of a majority of STRS Ohio members and their positive overall impressions of the system — in spite of the uncertainty about future pension plan design.
- Creating an Employer Self-Service Web site to facilitate information reporting to STRS Ohio by more than 1,100 employers.
- Increasing the use of the STRS Ohio Web site as a vehicle for educating members about their pension plan and health care coverage through online calculators, Web-based presentations and webinars, and secure access to personal account information; and providing online registration for member education programs.
- Reducing print communication costs by using the Web site and e-mail news service to provide timely information to STRS Ohio members.
- Preparing annual financial reports that continually receive the Government Finance Officers Association Certificate of Achievement for Excellence in Financial Reporting in recognition of achieving the highest standards in government accounting and financial reporting. STRS Ohio has also received the “Making Your Tax Dollars Count” award from the Auditor of State’s Office for three consecutive years for the quality of its financial reporting and absence of audit issues.

Associate Salaries

Mirroring the difficult economic times being experienced by all of Ohio’s citizens, the vast majority of STRS Ohio associates have not seen any increase in their salaries since July 1, 2008, when the average merit increase awarded was 3.6% based on a budgeted amount of 3.9%. There was a 0% merit increase for fiscal 2010, as well as for fiscal 2011, which ends on June 30, 2011. Going forward, any legislation that is passed involving public pension plan design will affect STRS Ohio associates.

The chart below details how merit increases were distributed on July 1, 2008, to the associates employed at STRS Ohio at that time, based on their performance during the preceding 12 months.

| 2008 Annual Performance Increase Frequency (July 1, 2008) | | |
|---|-------|------------|
| % Increase | Count | % of Total |
| 0% | 7 | 1% |
| 1 - 1.99% | 5 | 1% |
| 2 - 2.99% | 28 | 5% |
| 3 - 3.99% | 380 | 66% |
| 4 - 4.99% | 124 | 21% |
| 5%+ | 32 | 6% |

As can be seen, merit increases are not applied uniformly across the work force, but must be earned. Associates who perform at lower levels and do not meet expectations receive less than the budgeted amount; those associates who are exceptional performers receive higher amounts. Written performance appraisals for each STRS Ohio associate are completed by the respective supervisor; any accompanying recommendation for a merit increase goes through a multilevel review process requiring sign-off by the supervisor’s manager, department director and, ultimately, the executive director.