TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2012

COLE + REED P.C.
CERTIFIED PUBLIC ACCOUNTANTS

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2012

AUDITED FINANCIAL STATEMENTS

REQUIRED SUPPLEMENTARY INFORMATION

OTHER FINANCIAL INFORMATION

REPORT REQUIRED BY *GOVERNMENT AUDITING STANDARDS*

COLE + REED P.C.
CERTIFIED PUBLIC ACCOUNTANTS

Independent Auditors' Report

Board of Trustees
Teachers' Retirement System
of Oklahoma

We have audited the accompanying statements of plan net assets of the Teachers' Retirement System of Oklahoma (the "System"), a part of the financial reporting entity of the state of Oklahoma, as of June 30, 2012 and 2011, and the related statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note M, the System's actuary has determined that the System's unfunded actuarial accrued liability (the "UAAL") is approximately $8,398,000,000. The funding of the actuarial accrued liabilities is predicated on a funding schedule mandated by Oklahoma Statutes. Under the present funding schedule, the UAAL will be fully amortized in 22 years.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net assets of the System at June 30, 2012 and 2011, and the changes in its net assets for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

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In accordance with *Government Auditing Standards*, we have also issued a report dated December 11, 2012, on our consideration of the System's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, beginning on page 3, and the schedules of funding progress and employers' contributions on page 30, be presented to supplement the basic financial statements. Such information, although not a 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.

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The information included in pages 31 through 33 is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the 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 financial statements as a whole.

Cole & Reed P.C.

Oklahoma City, Oklahoma
December 11, 2012

Teachers' Retirement System of Oklahoma

Management's Discussion and Analysis

Management is pleased to present this discussion and analysis of the financial activities of the Oklahoma Teachers Retirement System ("OTRS" or the "System") for the years ended June 30, 2012 and 2011. The System is responsible for administering retirement benefits for a 401(a) defined benefit plan for all educational employees of the state of Oklahoma as well as a voluntary defined contribution plan, 403(b). The System was established on July 1, 1943 for the purpose of providing these retirement benefits and other specific benefits for qualified persons employed by public educational institutions. The main purpose of the System is to provide a primary source of lifetime retirement benefits relative to years of service at the time of retirement. It is the objective of the System to provide these benefits in a prudent, responsible, and cost-effective manner. Plan net assets are used to pay current and future benefits to retired clients.

This discussion and analysis is intended to serve as an introduction to the System's basic financial statements. OTRS's basic financial statements are comprised of three components: 1) *statement of plan net assets*, 2) *statement of changes in plan net assets*, and 3) *notes to the financial statements*. This report also contains *required supplementary information* in addition to the basic financial statements themselves.

The *statement of plan net assets* presents information on all of the System's assets and liabilities, with the difference between the two reported as *net assets held in trust for pension benefits and* a*nnuity benefits of electing members.* Over time, increases or decreases in net plan assets may serve as a useful indicator of whether the financial position of the System is improving or deteriorating. Information relating to the System's ability to meet the cost of future benefit payments, is not shown on the *statement of plan net assets,* but is located in both the *notes to the financial statements* and the required *supplementary information.*

The *statement of changes in plan net assets* presents information showing how the System's net assets changed during the most recent fiscal year. Changes in net assets are recognized using the accrual basis of accounting, in which expenses are recorded when the liability is incurred and revenues are recorded in the accounting period in which they are earned and become measurable.

The *notes to the financial statements* are critical to the reader's understanding of the financial status of the System. These notes include a description of the System, details on the cash and investments of the System, as well as contribution and benefit information.

The *required supplementary information* presents a Schedule of Funding Progress that provides historical trend information about the actuarially determined funded status of the System. The Schedule of Employers' Contributions provides historical trend information about the annual required contributions ("ARC") of the System and the contributions made to the System in relation to the ARC. Other supplementary information includes the Schedules of Administrative Expenses, the Schedules of Investment Expenses, and the Schedules of Professionals/Consultants Fees. These schedules provide additional analysis of the information provided in the financial statements.

CONDENSED FINANCIAL INFORMATION

Plan Net Assets as of June 30:

ASSETS	2012	2011	2010	2012 % Change	2011 % Change
Cash	$ 24,936,734	$ 14,348,481	$ 9,646,573	73.79%	48.74%
Receivables	276,870,038	270,340,945	172,564,773	2.42%	56.66%
Long and short-term investments, at fair value	10,414,998,956	10,349,078,808	8,519,177,169	0.64%	21.48%
Capital assets, net	1,543,239	874,921	187,847	76.39%	365.76%
TOTAL INVESTMENTS AND OTHER ASSETS	10,718,348,967	10,634,643,155	8,701,576,362	0.79%	22.22%
Securities lending institutional daily assets fund	1,764,088,842	2,023,648,275	2,247,747,871	-12.83%	-9.97%
TOTAL ASSETS	12,482,437,809	12,658,291,430	10,949,324,233	-1.39%	15.61%
LIABILITIES					
Investment settlements and other liabilities	313,564,107	254,834,471	134,652,920	23.05%	89.25%
Payable under securities lending agreement	1,764,088,842	2,023,648,275	2,247,747,871	-12.83%	-9.97%
TOTAL LIABILITIES	2,077,652,949	2,278,482,746	2,382,400,791	-8.81%	-4.36%
NET ASSETS					
Net assets held in trust for pension benefits	$10,404,784,860	$10,379,808,684	$ 8,566,923,442	0.24%	21.16%

Changes in Plan Net Assets for the year ended June 30:

ADDITIONS:	2012	2011	2010	2012 % Change	2011 % Change
Member contributions	$ 291,385,506	$ 286,643,244	$ 290,247,028	1.65%	-1.24%
Employer contributions	376,635,234	364,025,589	366,282,238	3.46%	-0.62%
Matching contributions	23,188,952	23,128,795	26,448,892	0.26%	-12.55%
Dedicated tax revenue	281,806,711	251,322,410	227,926,247	12.13%	10.26%
Member tax shelter contributions	3,448,031	5,010,856	5,402,646	-31.19%	-7.25%
Net investment income gain	134,376,020	1,919,301,220	1,186,235,015	-93.00%	61.80%
Security lending net income	9,279,228	6,336,019	5,032,411	46.45%	25.90%
TOTAL ADDITIONS	1,120,119,682	2,855,768,133	2,107,574,477	-60.78%	35.50%
DEDUCTIONS:					
Benefit payments	1,036,132,586	979,245,846	912,912,714	5.81%	7.27%
Refund of member contributions and tax sheltered annuity	54,737,731	58,920,565	74,951,443	-7.10%	-21.39%
Administrative expenses	4,273,189	4,716,480	4,979,589	-9.40%	-5.28%
TOTAL DEDUCTIONS	1,095,143,506	1,042,882,891	992,843,746	5.01%	5.04%
NET INCREASE	24,976,176	1,812,885,242	1,114,730,731	-98.62%	62.63%
NET ASSETS, BEGINNING OF YEAR	10,379,808,684	8,566,923,442	7,452,192,711	21.16%	14.96%
NET ASSETS, END OF YEAR	$10,404,784,860	$10,379,808,684	$ 8,566,923,442	0.24%	21.16%

FINANCIAL HIGHLIGHTS AND ANALYSIS

Total fund returns for fiscal year 2012 were essentially flat with an increase of 0.2% from fiscal 2011. Domestic and international equity, which compose 58.0% of the investment portfolio asset allocation, both decreased by -0.70% and -12.2%, respectively. Investments in fixed income securities, which compose 29.0% of the investment portfolio, increased by 11.2%. The increase in net assets for fiscal year 2011 was primarily due to investment gains as a result of significant market improvement. The total investment returns for FY 2011 were 23.5%. Domestic and international equity, which composed 60.0% of the investment portfolio asset allocation, had the greatest increases at 34.0%.

	2012	2011	2010	2008	2003
Plan net assets	$ 10,404,784,860	$ 10,379,808,684	$ 8,566,923,442	$ 8,945,589,282	$ 5,696,883,206
Yearly % change	0.2%	21.2%	15.0%	-7.3%	2.9%

The total investment returns for the one, five, and ten year periods are below the actuarial assumed rate of investment return of 8.0%, while the returns for the 3 year period exceeded the actuarial assumed rate of investment return. More importantly, the total investment returns from November 1991 to current were 9.0% annualized, well in excess of the 8.0% actuarial assumed rate of return.

Total returns	1 year	3 year	5 year	10 year
2012	1.8%	13.6%	2.7%	7.6%
2011	23.5%	6.5%	5.9%	6.9%
2010	16.6%	-3.1%	3.4%	4.4%
2008	-7.2%	6.5%	10.0%	(1)
2003	5.2%	-0.8%	4.0%	(1)

(1) Historical returns were not available for this time period

Benefit payments increased 5.8% in 2012 compared to a 7.3% increase in 2011. The increase in 2012 is a result of a 3.7% increase in the number of benefit recipients and a 1.1% increase in the average monthly benefit. The increase in 2011 is a result of a 4.3% increase in the number of benefit recipients and a 1.7% increase in the average monthly benefit. Benefit payments in 2012 to retired members exceed contributions from contributing members and employers by $95 million or a ratio of 1.10 to 1. A ratio of less than one is desirable because it signifies that the System is receiving more contributions than it pays out in benefits. The table on the following page reflects the ongoing employer and member contributions.

FINANCIAL HIGHLIGHTS AND ANALYSIS (Continued)

	2012	2011	2010	2008	2003
Member contributions	$ 291,385,506	$ 291,654,100	$ 295,649,674	$ 286,738,943	$ 220,503,413
Employer contributions	376,635,234	364,025,589	366,282,238	308,804,479	218,841,977
Matching contributions	23,188,952	23,128,795	26,448,892	21,274,957	14,267,487
Dedicated tax revenue	281,806,711	251,322,410	227,926,247	266,761,597	128,879,976
Total contributions	973,016,403	930,130,894	916,307,051	883,579,976	582,492,853
Benefit payments	1,036,132,586	979,245,846	912,912,714	806,540,725	608,976,125
Refund of contributions	32,076,398	58,920,565	74,951,443	63,925,592	73,563,552
Total payments	$ 1,068,208,984	$1,038,166,411	$ 987,864,157	$ 870,466,317	$ 682,539,677
Ratio benefit payments/ contributions	1.10	1.12	1.08	0.99	1.17

Since 2003, the number of benefit recipients increased by 14,657 or 38.5%. The number of members retiring has remained relatively stable for the last five years.

	2012	2011	2010	2008	2003
Benefit recipients	52,716	50,829	48,756	45,238	38,059
Yearly % change	3.7%	4.3%	4.2%	4.0%	4.2%
Net increase	1,887	2,073	1,960	1,732	1,544

The following table reflects the average monthly benefit for service retirements. Over the ten-year period from 2003, the average benefit increased by $251, or 19.2%. The retirement benefit payments increased 56.5% or $385.7 million over this ten-year period. In FY 2012 and 2011, the average benefit increases are due to an increase in the average benefit received by the newer retirees.

	2012	2011	2010	2008	2003
Average benefit	$ 1,555	$ 1,537	$ 1,511	$ 1,437	$ 1,304
Yearly % change	1.1%	1.7%	1.9%	1.3%	4.7%

The ratio of active members to retired members of the System is 1.67 to 1 in 2012 compared to 2.34 to 1 in 2003. Over the past ten years, the number of members contributing into the System increased 5.6%. During the same period, the number of retired members increased by 38.5%.

	2012	2011	2010	2008	2003
Members contributing	87,778	88,085	89,896	88,678	83,127
Yearly % change	-0.3%	-2.0%	0.6%	0.6%	-2.6%
Benefit recipients	52,716	50,829	48,756	45,238	38,059
Yearly % change	3.7%	4.3%	4.2%	4.0%	4.2%
Ratio contributing/retired	1.67	1.73	1.84	1.96	2.18

The measure of the progress in accumulating sufficient assets to meet the long-term benefit obligations is the funded status or the funded ratio of the System. The funded ratio is the actuarial value of assets expressed as a percentage of the actuarial accrued liability. The funding policy is the method to provide benefits, specified in the System, through the amounts and timing of contributions from the employers and the contributing clients. The excess of the actuarial accrued liability over the actuarial value of assets is the unfunded actuarial accrued liability ("UAAL"). The actuarial value of assets differs from the year-end fair value of the System's plan net assets by smoothing the effects of market fluctuations. In the calculation of the actuarial value of assets, 20% of the difference between the actual and assumed investment returns is included in the actuarial value of assets. During extended periods of market declines, the market value of the System's plan net assets usually will be less than the actuarial value of assets.

The unfunded actuarial accrued liability (UAAL) as of June 30, 2011 was $7.6 billion, and increased to $8.398 billion in 2012. As a result, the System's funded ratio-actuarial value of assets divided by the actuarial accrued liability-decreased from 56.7% to 54.8% as of June 30, 2012. These decreases were primarily due to a loss on assets with returns of only 1.3%on a market value basis and 3.3% on the actuarial value of assets compared to the assumed rate of 8.0%. Based upon the current statutory contribution schedule, the funding period is 22 years. This is the same as in the previous actuarial valuation despite the experienced losses.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the System's finances for all those with an interest in the System. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Executive Director of the Teachers' Retirement System of Oklahoma, P.O. Box 53524, Oklahoma City, Oklahoma 73152 or (405) 521-2387.

STATEMENTS OF PLAN NET ASSETS

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

As of June 30, 2012 (with Comparative Totals as of June 30, 2011)

			Comparative Totals June 30	
	401(a) Plan	403(b) Plan	2012	2011
ASSETS				
Cash	$ 24,936,734	$ -	$ 24,936,734	$ 14,348,481
Short-term investments	275,456,138	-	275,456,138	361,798,249
Accrued interest and dividends receivable	43,659,356	-	43,659,356	45,636,139
Member contributions receivable	23,754,560	-	23,754,560	22,103,498
Employer contributions receivable	33,991,038	-	33,991,038	34,484,109
Receivable from the State of Oklahoma	29,333,333	-	29,333,333	27,322,221
Due from brokers for securities sold	146,131,751	-	146,131,751	140,794,978
Security lending institutional daily assets fund	1,764,088,842	-	1,764,088,842	2,023,648,275
Long-term investments:				
Mutual funds	-	210,049,295	210,049,295	223,451,514
U.S. government securities	1,086,437,639	-	1,086,437,639	1,128,778,574
U.S. corporate bonds	1,714,515,243	-	1,714,515,243	1,806,875,024
International corporate bonds and government securities	76,226,837	-	76,226,837	70,083,523
Equity securities	6,296,233,773	-	6,296,233,773	6,549,478,652
Alternative investments	283,762,403	-	283,762,403	171,396,984
Real estate	472,317,628	-	472,317,628	37,216,288
Total long-term investments	9,929,493,523	210,049,295	10,139,542,818	9,987,280,559
Capital assets, net	1,543,239	-	1,543,239	874,921
TOTAL ASSETS	$ 12,272,388,514	$ 210,049,295	$ 12,482,437,809	$ 12,658,291,430
LIABILITIES				
Benefits in process of payment	$ 3,906,006	$ -	$ 3,906,006	$ 80,477,110
Due to brokers for securities purchased	300,652,220	-	300,652,220	164,155,126
Payable under security lending agreement	1,764,088,842	-	1,764,088,842	2,023,648,275
Other liabilities	9,005,881	-	9,005,881	10,202,235
TOTAL LIABILITIES	$ 2,077,652,949	$ -	$ 2,077,652,949	$ 2,278,482,746
NET ASSETS				
Net assets held in trust for pension benefits and annuity benefits of electing members	$ 10,194,735,565	$ 210,049,295	$ 10,404,784,860	$ 10,379,808,684

See accompanying notes to financial statements.

STATEMENTS OF CHANGES IN PLAN NET ASSETS

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

For the Year ended June 30, 2012
(with Comparative Totals for the year ended June 30, 2011)

	401(a) Plan	403(b) Plan	Comparative Totals Year Ended June 30 2012	2011
Additions:				
Members	$ 291,385,506	$ -	$ 291,385,506	$ 286,643,244
Members tax shelter	-	3,448,031	3,448,031	5,010,856
Employer statutory requirement from local school districts	376,635,234	-	376,635,234	364,025,589
Matching funds	23,188,952	-	23,188,952	23,128,795
Dedicated tax	281,806,711	-	281,806,711	251,322,410
Total contributions	973,016,403	3,448,031	976,464,434	930,130,894
Investment income:				
Interest & dividends	308,064,104	11,501,601	319,565,705	286,510,332
Net appreciation in fair value of investments	(144,717,179)	(5,690,518)	(150,407,697)	1,668,724,492
Investment expenses	(34,781,988)	-	(34,781,988)	(35,933,604)
Gain from investing activities	128,564,937	5,811,083	134,376,020	1,919,301,220
Income from securities lending activities:				
Securities lending income	10,916,738	-	10,916,738	7,454,140
Securities lending expenses:				
Management fees	(1,637,510)	-	(1,637,510)	(1,118,121)
Net income from securities lending activities	9,279,228	-	9,279,228	6,336,019
Net investment gain	137,844,165	5,811,083	143,655,248	1,925,637,239
Total additions	1,110,860,568	9,259,114	1,120,119,682	2,855,768,133
Deductions:				
Retirement, death, survivor, and health benefits	1,036,132,586	-	1,036,132,586	979,245,846
Refund of member contributions and annuity payments	32,076,398	22,661,333	54,737,731	58,920,565
Administrative expenses	4,273,189	-	4,273,189	4,716,480
Total deductions	1,072,482,173	22,661,333	1,095,143,506	1,042,882,891
NET INCREASE	38,378,395	(13,402,219)	24,976,176	1,812,885,242
NET ASSETS, BEGINNING OF YEAR	10,156,357,170	223,451,514	10,379,808,684	8,566,923,442
NET ASSETS, END OF YEAR	$ 10,194,735,565	$ 210,049,295	$ 10,404,784,860	$ 10,379,808,684

See accompanying notes to financial statements.

NOTE A--DESCRIPTION OF THE SYSTEM

The following brief description of the Teachers' Retirement System of Oklahoma (the "System") is provided for general information purposes only. Participants should refer to Title 70 of the Oklahoma Statutes, 1991, sections 17-101 through 121, as amended.

The System was established as of July 1, 1943, for the purpose of providing retirement allowances and other specified benefits for qualified persons employed by state-supported educational institutions. The System is a part of the state of Oklahoma financial reporting entity, which is combined with other similar funds to comprise the fiduciary-pension trust funds of the state of Oklahoma (the "State"). The supervisory authority for the management and operation of the System is a 13-member board of trustees, which acts as a fiduciary for investment of the funds and the application of plan interpretations. The System administers a cost-sharing multiple-employer pension plan which is a defined benefit pension plan ("DB Plan") as well as a tax-deferred defined contribution plan ("DC Plan").

DB Plan

Oklahoma teachers and other certified employees of common schools, faculty and administrators in public colleges and universities, and administrative personnel of state educational boards and agencies who are employed at least half-time, must join the System's DB Plan. Membership is optional for all other regular employees of public educational institutions who work at least 20 hours per week. The DB Plan's membership consisted of the following as of June 30:

	2012	2011
Retirees and beneficiaries currently receiving benefits	$ 52,716	$ 50,829
Terminated vested clients	8,687	7,725
Active clients	87,778	88,085
	$ 149,181	$ 146,639

There are 614 contributing employers in the System. In addition, there were 8,564 and 7,498 of non-vested inactive members at June 30, 2012 and 2011, respectively, which are entitled to a refund of their accumulated contributions.

DC Plan

Members are also offered a tax-deferred defined contribution plan qualified under the Internal Revenue Code ("IRC") Section 403(b). The DC Plan is also referred to by the System as the Tax-Sheltered Annuity Plan. Membership in the DC Plan is voluntary and investments primarily consist of mutual funds and are participant directed. ING is responsible for administrative services, including custody and record keeping services.

NOTE A--DESCRIPTION OF THE SYSTEM--Continued

<u>DC Plan--Continued</u>
The DC Plan had approximately 4,190 and 4,408 participants as of June 30, 2012 and 2011, respectively. Contributions are voluntary and require a minimum of $200 per year. The maximum deferral amount is the lesser of 100% of the participant's compensation or the maximum amount allowed by the IRC, currently $17,000.

NOTE B--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

<u>Basis of Accounting</u>: The System has prepared its financial statements in accordance with accounting principles generally accepted in the United States of America and using the economic resources measurement focus. The financial statements are prepared using the accrual basis of accounting, under which expenses are recorded when the liability is incurred, revenues are recorded in the accounting period they are earned and become measurable, and investment purchases and sales are recorded as of their trade dates. Member and employer contributions are established by Oklahoma Statutes as a percentage of salaries and are recognized 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 Oklahoma Statutes. Administrative expenses are funded through investment earnings.

<u>Budgetary Control</u>: The System prepares and submits an annual budget of operating expenses on the cash basis for monitoring and reporting to the Oklahoma Office of State Finance. The System's budget process follows the budget cycle for State operations as outlined by the Oklahoma Office of State Finance.

The Executive Director may approve changes within the budget, but a change to the total budget must be handled according to the provision of Title 62 O.S. Sec. 41.12 of the Oklahoma Statutes.

<u>Investments</u>: The System is authorized to invest in eligible investments as approved by the board of trustees as set forth in the System's investment policy.

NOTE B--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES--Continued

Investments--Continued: System investments are reported at fair value. The short-term investment fund is comprised of an investment in units of commingled trust funds of the System's custodial agent, which is reported at cost, which approximates fair value. Debt and equity securities are reported at fair value, as determined by the System's custodial agent, using pricing services or prices quoted by independent brokers based on the latest reported sales prices at current exchange rates for securities traded on national or international exchanges. The Security Lending Institutional Daily Assets Fund represents investment in JP Morgan's Institutional Daily Assets Fund and is carried at amortized cost, which approximates fair value.

The System also invests as a limited partner in alternative investments. These investments employ specific strategies such as leverage buyouts, venture capital, growth capital, distressed investments and mezzanine capital. The strategies of all such funds are long term and illiquid in nature. As a result, investors are subject to redemption restrictions which generally limit distributions and restrict the ability of limited partners to exit a partnership investment prior to its dissolution. Alternative investment partnerships are valued using their respective net asset value (NAV), and are audited annually. The most significant input into the NAV of such an entity is the fair value of its investment holdings. These holdings are valued by the general partners on a quarterly or semi-annual basis, in conjunction with management and investment advisors, and consultation with valuation specialists. The management assumptions are based upon the nature of the investment and the underlying business. The valuation techniques vary based upon investment type and involve a certain degree of expert judgment.

The System's real estate investments are primarily through limited partnerships. Properties owned by the partnership are subject to independent third-party appraisals performed in accordance with the Uniform Standards of Professional Appraisal Practice once every year. The System's real estate investments are long term and illiquid in nature. As a result, investors are subject to redemption restrictions which generally limit distributions and restrict the ability of limited partners to exit a partnership investment prior to its dissolution. Limited partner interests are valued by the System using the NAV of the partnership. The most significant input into the NAV of such an entity is the value of its investment holdings. These holdings are valued by the general partners on a continuous basis, audited annually and may be periodically appraised by an independent third party. The valuation assumptions are based upon both market and property specific inputs which are not observable and involve a certain degree of expert judgment.

Net investment income includes net appreciation (depreciation) in the fair value of investments, interest income, dividend income, investment income from foreign currency translation gains and losses, securities lending income and expenses, and investment expenses, which includes investment management and custodial fees and all other significant investment related costs.

NOTE B--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES--Continued

Investments--Continued: International investment managers use forward foreign exchange contracts to enhance returns or to control volatility. Currency risks arise due to foreign exchange rate fluctuations. Forward foreign exchange contracts are negotiated between two counter-parties. The System could incur a loss if its counter-parties failed to perform pursuant to the terms of their contractual obligations. At June 30, 2012, the System had forward currency contracts with fair values of $62.7 million in receivables and had forward currency contracts with fair values of $61.4 million in payables. The gains and losses on these contracts are included in the income in the period in which the exchange rates change. See Note C for additional information regarding investment derivatives as of June 30, 2012.

The System's investment policy provides for investment diversification of stocks, bonds, fixed income securities, real estate, alternative investments and other investment securities along with investment in commingled or mutual funds. Investment securities and investment securities underlying commingled or mutual fund investments are exposed to various risks, such as interest rate, market, and credit risks. Due to the risks associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities may occur in the near term and those changes could materially affect the amounts reported in the statements of plan net assets.

Capital Assets: Capital assets are stated at cost when acquired, net of accumulated depreciation. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets, which range from five to ten years.

Risks and Uncertainties: Contributions to the System and the actuarial information included in the required supplementary information are reported based on certain assumptions pertaining to interest rates, inflation rates, employee compensation, and demographics. Due to the changing nature of these assumptions, it is at least reasonably possible that changes in these assumptions may occur in the near term and, due to the uncertainties inherent in setting assumptions, that the effect of such changes could be material to the financial statements.

Income Taxes: The System is exempt from federal and state income taxes and has received a favorable determination from the Internal Revenue Service (the "IRS") under Internal Revenue Code (the "IRC") Section 401(a). The System's 403(b) Plan is also tax exempt and has received a private letter ruling from the IRS.

NOTE B--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES--Continued

Compensated Absences: It is the State's policy to permit employees to accumulate earned but unused vacation and sick leave. Employees earn annual vacation leave based upon their start date and years of service. All accrued vacation leave is payable upon termination, resignation, retirement, or death. Sick leave does not vest to the employee and therefore is not recorded as a liability. Amounts due to the employees for compensated absences were approximately $282,000 and $267,000 at June 30, 2012 and 2011, respectively.

Plan Termination: In the event the System terminates, the board of trustees will distribute the net assets of the System to provide the following benefits in the order indicated:

Accumulated contributions will be allocated to each respective member, former member, retired member, joint annuitant, or beneficiary then receiving payments.

The balance of such assets, if any, will be allocated to each member then having an interest in the System based upon the excess of their retirement income under the System less the retirement income, which is equal to the actuarial equivalent of the amount allocated to them in accordance with the preceding paragraph in the following order:

- Those retired members, joint annuitants, or beneficiaries receiving payments,
- Those members eligible to retire,
- Those members eligible for early retirement,
- Former members electing to receive a vested benefit, and
- All other members.

Use of Estimates: The preparation of the System's financial statements in conformity with accounting principles generally accepted in the United States of America requires the System's management to make significant estimates and assumptions that affect the reported amounts of net assets held in trust for pension benefits at the date of the financial statements and the actuarial information included in the required supplementary information as of the benefit information date, the changes in System net assets during the reporting period and, when applicable, disclosures of contingent assets and liabilities at the date of the financial statements. Actual results could differ from those estimates.

NOTE C--CASH AND INVESTMENTS

Custodial Credit Risk: Custodial credit risk is the risk that in the event of the failure of a counterparty, the System will not be able to recover the value of its bank deposits or investments. Bank deposits are exposed to custodial credit risk if they are uninsured and uncollateralized. In relation to its bank deposits, the System is not considered to be exposed to custodial credit risk. Although the System does not have a formal bank deposit policy for custodial credit risk, the State Treasurer holds all of the System's bank deposits. As required by Oklahoma Statutes, all bank deposits held by the State Treasurer are insured by Federal Deposit Insurance Corporation, collateralized by securities held by the cognizant Federal Reserve Bank, or invested in U.S. government obligations.

At June 30, 2012 and 2011, the carrying amount of the System's bank deposits was approximately $24,937,000 and $14,348,000, respectively. The bank balance of the System's bank deposits at June 30, 2012 and 2011 was approximately $(34,881,000) and $11,459,000, respectively.

Investment securities are exposed to custodial credit risk if they are uninsured, are not registered in the name of the System, and are held by a counterparty or the counterparty's trust department but not in the name of the System. While the System's investment policy does not specifically address custodial credit risk it does limit the amount of cash equivalents and short-term investments to no more than 5% of each manager's portfolio. At June 30, 2012 and 2011, the System had uninsured and uncollateralized cash and cash equivalents of approximately $275,456,000 and $361,798,000, respectively, with its custodial agent. The System's custodial agent for the years ended June 30, 2012 and 2011 was JP Morgan.

Credit Risk: Fixed-income securities are subject to credit risk. Credit quality rating is one method of assessing the ability of the issuer to meet its obligation. The System's investment policy requires that at the time of purchase all corporate bonds or debentures be at the highest rating of the four rating services recognized by the Comptroller of the Currency of the United States of America.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2012

NOTE C--CASH AND INVESTMENTS--Continued

Credit Risk--Continued:

Investment Type	S&P Ratings (Unless Noted)	Fair Value	Fair Value as a Percent of Total Fixed Income Fair Value
		(Amounts in Thousands)	
U.S. corporate bonds	AAA	$ 102,499	3.56%
	AA+	24,687	0.86%
	AA	7,502	0.26%
	AA-	15,144	0.53%
	A+	30,218	1.05%
	A	67,067	2.33%
	A-	106,429	3.70%
	BBB+	77,157	2.68%
	BBB	182,270	6.34%
	BBB-	238,800	8.30%
	BB+	143,316	4.98%
	BB	137,680	4.79%
	BB-	110,412	3.84%
	B+	101,840	3.54%
	B	109,050	3.79%
	B-	85,450	2.97%
	CCC+	41,458	1.44%
	CCC	17,917	0.62%
	CCC-	4,775	0.17%
	CC	1,529	0.05%
	D	3,999	0.14%
	NR	105,316	3.70%
Total U.S. corporate bonds		$ 1,714,515	59.64%
International corporate bonds	AA-	$ 2,842	0.10%
	A-	2,419	0.08%
	BBB-	1,624	0.06%
	BB+	1,333	0.05%
	BB-	1,163	0.04%
	B	333	0.01%
	CCC	901	0.03%
	NR	265	0.01%
Total international corporate bonds		$ 10,880	0.38%

NOTE C--CASH AND INVESTMENTS--Continued

Credit Risk--Continued:

Investment Type	S&P Ratings (Unless Noted)	Fair Value	Fair Value as a Percent of Total Fixed Income Fair Value
		(Amounts in Thousands)	
International government securities	AAA	$ 4,233	0.15%
	AA+	941	0.03%
	AA	3,059	0.11%
	AA-	1,313	0.05%
	A	394	0.01%
	A-	14,879	0.52%
	BBB+	9,283	0.32%
	BBB	10,171	0.35%
	BBB-	4,026	0.14%
	BB+	1,281	0.04%
	BB	5,593	0.19%
	B+	1,691	0.06%
	B	1,189	0.04%
	NR	7,294	0.25%
Total international government securities		$ 65,347	2.26%
Municipal bonds	AA+	$ 284	0.01%
	AA	608	0.02%
	AA-	869	0.03%
	A	1,183	0.04%
	A-	381	0.01%
	BBB+	777	0.03%
Total municipal bonds		$ 4,102	0.14%
U.S. government securities	AGY (1)	$ 293,989	10.22%
	AA+	80,032	2.78%
	A	4,886	0.17%
	A-	278	0.01%
	BBB	1,196	0.04%
Total U.S. government securities		$ 380,381	13.22%
		$ 2,175,225	75.50%

(1) U.S. Agency securities - implicity guaranteed by the U.S. Government.

NOTE C--CASH AND INVESTMENTS--Continued

Interest Rate Risk: Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. While all investments are subject to market changes, securities invested in index funds are more sensitive to market risk. Although the System's investment policy does not specifically address the duration of fixed–income securities, the System's management does monitor interest rate risk by monitoring the performance of each investment manager. As of June 30, 2012, the System had the following investments with maturities:

	Investment Maturities at Fair Value (in Years) *(Amounts in Thousands)*				
Investment Type	Less than One	One to Five	Five to Ten	More than Ten	Total Fair Value
U.S. corporate securities					
Asset-backed securities	$ 28,061	$ 57,640	$ 5,108	$ 14,137	$ 104,946
CMO/REMIC/CMBS	72,856	-	1,144	50,242	124,242
Corporate bonds	66,433	437,186	800,088	181,620	1,485,327
	167,350	494,826	806,340	245,999	1,714,515
International corporate bonds	3,495	3,319	3,751	315	10,880
International government securities	21,219	5,288	20,235	18,605	65,347
Municipal bonds	-	-	-	4,102	4,102
U.S. government securities	41,928	210,157	180,100	650,151	1,082,336
	$ 233,992	$ 713,590	$ 1,010,426	$ 919,172	$ 2,877,180

NOTE C--CASH AND INVESTMENTS--Continued

Foreign Currency Risk: Foreign currency risk is the potential risk for loss due to changes in exchange rates. The System's investment policy provides that international investment managers invest no more than 30% of their portfolio's total assets in one or more issuers in a single country, provided that in the U.K. such limit shall be 35%. Investment in cash and cash equivalents, foreign equities, and fixed-income securities as of June 30, 2012 is shown in the following table by monetary unit to indicate possible foreign currency risk.

(Amounts in Thousands)

Currency	Equities	Corporate Bonds	Government Bonds	Foreign Exchange Contracts	Cash and Cash Equivalents	Grand Total
Australian Dollar	$ 18,689	$ 2,712	$ 757	$ -	$ 72	$ 22,230
Brazilian Real	24,632	-	4,094	-	50	28,776
Canadian Dollar	23,558	1,761	-	(5)	67	25,382
Chilean Peso	378	-	-	-	-	378
Danish Krone	14,607	-	-	-	26	14,633
Euro	369,048	6,264	14,344	1,332	971	391,960
Hong Kong Dollar	78,023	-	-	-	148	78,171
Indonesian Rupiah	5,498	-	-	-	-	5,498
Japanese Yen	247,915	-	-	-	1,956	249,871
Malaysian Ringgit	3,725	-	-	-	-	3,725
Mexican Peso	7,530	-	24,696	-	-	32,227
New Taiwan Dollar	9,911	-	-	-	3,195	13,106
New Turkish Lira	7,485	-	-	-	-	7,485
Norwegian Krone	8,053	-	-	-	134	8,187
Phillipine Peso	5,554	-	4,994	-	11	10,559
Polish Zloty	1,358	-	-	-	-	1,358
Pound Sterling	258,745	-	-	3	472	259,221
Singapore Dollar	12,885	-	-	-	36	12,922
South African Rand	13,676	-	-	(1)	16	13,691
South Korean Won	28,520	-	-	-	17	28,536
Swedish Krona	23,740	-	-	-	51	23,791
Swiss Franc	84,560	143	-	3	144	84,850
Thai Baht	6,912	-	-	-	-	6,912
Total	1,255,002	10,880	48,885	1,334	7,366	1,323,467
Not subject to foreign currency risk	-	-	16,462	-	-	-
Total	$ 1,255,002	$ 10,880	$ 65,347	$ 1,334	$ 7,366	$ 1,323,467

NOTE C--CASH AND INVESTMENTS--Continued

Derivative Instruments: The System's investment derivatives include forward currency contracts. These investments are not speculative in nature and do not increase investment risk beyond allowable limits specified in the System's investment policy. The fair value balances and notional amounts of derivative instruments outstanding at June 30, 2012, classified by type, and the changes in fair value of such derivative instruments for the year then ended as reported in the 2012 financial statements are as follows:

(Amounts in Thousands)

Investment Derivatives	Change in fair value Classification	Change in fair value Amount	Fair Value at June 30, 2012 Classification	Fair Value at June 30, 2012 Amount	Notional
Foreign Currency Forward	Investment income	$ 1,799	Investments	$ 1,334	$ 235,763

A foreign currency forward contract is an agreement that obligates the parties to exchange given quantities of currencies at a pre-specified exchange rate on a certain future date. The fair values of the forward contracts are estimated based on the present value of their estimated future cash flows.

The foreign currency forward contracts subject the System to foreign currency risk because the investments are denominated in international currencies. The risks are described in foreign currency risk schedule where the fair value of the foreign currency contracts in U.S. dollars is presented.

NOTE D--COMMITMENTS

Commitments: At June 30, 2012, the System has total capital commitments of $1,187,500,000. Of this amount, $465,658,227 remained unfunded. The following table depicts the total commitments and unfunded commitments, respectively, by asset class.

(Amounts in Thousands)

	Total Commitments	Unfunded Commitments
Real Estate	$ 450,000	$ -
Alternative Investments	737,500	465,658
	$ 1,187,500	$ 465,658

NOTE E--SECURITIES LENDING ACTIVITY

The System's investment policy and State statutes provide for its participation in a securities lending program. The program is administered by the System's master custodian and there are no restrictions on the amount of loans that can be made. Certain securities of the System are loaned to participating brokers, who must provide collateral in the form of cash, U. S. Treasury or government agency securities, or letters of credit issued by approved banks. Under the terms of the agreement, collateralization of the fair value of the loaned securities must be provided in the amount of 102% when the security to be loaned and the collateral are in the same currency and 105% when the loan and collateral currencies are dissimilar.

The fair value of securities on loan at June 30, 2012 was approximately $1,818,359,000. The underlying collateral for these securities had a fair value of approximately $1,845,884,000 at June 30, 2012. Collateral of securities and letters of credit represented approximately $81,795,000 of total collateral at June 30, 2012. Because the System cannot pledge or sell collateral securities and letters of credit received unless the borrower defaults, the collateral and related liability are not presented in the accompanying statements of plan net assets. The following table describes the types of securities lent and collateral as of June 30, 2012.

(Amounts in Thousands)

Type of securities on loan	Market Value of Securities on Loan	Collateral Value
Government loans compared to cash collateral	$ 575,009	$ 593,769
Government loans compared to non-cash collateral	68,814	70,195
Equity loans compared to cash collateral	45,203	45,771
Equity loans compared to non-cash collateral	281	284
Corporate loans compared to cash collateral	1,117,649	1,124,549
Corporate loans compared to non-cash collateral	11,403	11,316
	$ 1,818,359	$ 1,845,884

At June 30, 2012, the System had no credit risk exposure since the amounts the System owed to borrowers exceeded the amounts borrowers owed the System. The contract with the System's lending agent requires it to indemnify the System if the borrowers fail to return the lent securities. In the event of a collateral shortfall due to a loss in value of investments made with cash collateral, such loss would be the responsibility of the System.

NOTE E--SECURITIES LENDING ACTIVITY--Continued

All securities loans can be terminated on demand by either the System or the borrower. Cash collateral is invested in a separate account for the System in accordance with investment guidelines approved by the System. At June 30, 2012 and 2011, the weighted average maturity of the cash collateral investments was 32 days and 24 days, respectively. The cash collateral investments are structured and maintained by the lending agent's investment desk utilizing an asset and liability methodology designed to manage to an appropriate extent any mismatch between the investment maturities and the System's loans.

NOTE F--CAPITAL ASSETS

Capital assets consist of the following at June 30:

	(Amounts in Thousands)	
	2012	2011
Furniture and fixtures	$ 2,602	$ 1,908
Accumulated depreciation	(1,059)	(1,033)
Capital assets, net	$ 1,543	$ 875

The System has commitments to lease building space as well as leases on certain equipment. The future minimum commitment for operating leases as of June 30, 2012 was approximately $176,000. The System's leases are one-year renewable contracts. Rental expense for all operating leases amounted to approximately $205,000 and $213,000 for the years ended June 30, 2012 and 2011, respectively.

NOTE G--RESERVE AND DESIGNATED FUNDS

The amount included in the Teachers' Deposit Fund, the Expense Fund, and the Capital Assets Fund is not available to pay regular retirement benefits. A brief description of the major funds is as follows:

NOTE G--RESERVE AND DESIGNATED FUNDS--Continued

The Teachers' Deposit Fund represents funds in the DC Plan. During FY 2010, the System hired ING as the service provider for the DC Plan. This process was undertaken to steadfastly provide a supplemental retirement program that will enhance the System's clients' retirement future. ING provides a comprehensive educational strategy, an array of investment options, clients have 24 hours a day access to their accounts on line, and dedicated customer service representatives available each weekday from 7:00 am to 7:00 pm.

- The Expense Fund represents funds accumulated to pay for the expense of administering and maintaining the System budgeted for the next fiscal year plus any accrued administrative costs as of the current fiscal year-end.
- The Capital Assets Fund represents the net book value of furniture and fixtures for the System.

The Funds had the following approximate balances at June 30:

	(Amounts in Thousands) 2012	2011
Teacher's deposit fund (DC Plan)	$ 210,049	$ 223,452
Expense fund	60,615	61,830
Capital assets fund	1,543	875
	$ 272,207	$ 286,157

NOTE H--CONTRIBUTIONS

All contribution rates are defined or amended by the Oklahoma Legislature. All active members contribute to the System; however, the employer may elect to make all or part of the contribution for its employees. There are special provisions for members of higher education who joined the System before July 1, 1995. The annual employer contributions reported for the years ended June 30, 2012 and 2011 were $376,635,234 and $364,025,589 respectively. Employers satisfied 100% of their contribution requirements for 2012 and 2011.

All members must contribute 7% of regular annual compensation, not to exceed the member's maximum compensation level, which for the years ended June 30, 2012 and 2011, was the full amount of regular annual compensation.

NOTE H--CONTRIBUTIONS--Continued

The employers are required to contribute a fixed percentage of annual compensation on behalf of active clients. The employer contribution rate was 7.85% from July 1, 2007 to December 31, 2007; 8.35% from January 1, 2008 to June 30, 2008; 8.5% on July 1, 2008; 9% from January 1, 2009 to December 31, 2009; and 9.5% beginning on January 1, 2011 for all remitting entities other than comprehensive and four year regional universities. The employer contribution rate was 7.05% from July 1, 2007 to December 31, 2007; 7.55% starting on January 1, 2008; 8.05% starting on January 1, 2009; and 8.55% starting on January 1, 2011 for comprehensive and four year universities. The rates for fiscal years 2012 and 2011 are applied on the full amount of the Client's regular annual compensation up to certain limits prescribed by the Internal Revenue Code.

NOTE I--BENEFITS

The System provides defined retirement benefits based on members' final compensation, age, and term of service. In addition, the retirement program provides for benefits upon disability and to survivors upon the death of eligible members. Title 70 O. S. Sec. 17-105 defines all retirement benefits. The authority to establish and amend benefit provisions rests with the State Legislature.

Benefit provisions include:

- Members become 100% vested in retirement benefits earned to date after five years of credited Oklahoma service. Members, who joined the System on June 30, 1992, or prior, are eligible to retire at maximum benefits when age and years of creditable service total 80. Members joining the System after June 30, 1992 are eligible for maximum benefits when their age and years of creditable service total 90. Members whose age and service do not equal the eligible limit may receive reduced benefits as early as age 55, and at age 62 receive unreduced benefits based on their years of service. The maximum retirement benefit is equal to 2% of final compensation for each year of credited service.
- Final compensation for members who joined the System prior to July 1, 1992 is defined as the average salary for the three highest years of compensation. Final compensation for members joining the System after June 30, 1992 is defined as the average of the highest five consecutive years of annual compensation in which contributions have been made. The final average compensation is limited for service credit accumulated prior to July 1, 1995 to $40,000 or $25,000, depending on the member's election. Monthly benefits are 1/12 of this amount. Service credits accumulated after June 30, 1995 is calculated based on each member's final average compensation, except for certain employees of the two comprehensive universities.

NOTE I--BENEFITS--Continued

- Upon the death of a member who has not yet retired, the designated beneficiary shall receive the member's total contributions plus 100% of interest earned through the end of the fiscal year, with interest rates varying based on time of service. A surviving spouse of a qualified member may elect to receive, in lieu of the aforementioned benefits, the retirement benefit the member was entitled to at the time of death as provided under the Joint Survivor Benefit Option.
- Upon the death of a retired member, the System will pay $5,000 to the designated beneficiary, in addition to the benefits provided for the retirement option selected by the member.
- A member is eligible for disability benefits after ten years of credited Oklahoma service. The disability benefit is equal to 2% of final average compensation for the applicable years of credited service.
- Upon separation from the System, members' contributions are refundable with interest based on certain restrictions provided in the plan, or by the IRC.
- Members may elect to make additional contributions to a tax-sheltered annuity program up to the exclusion allowance provided under the IRC under Code Section 403(b).

At the election of each eligible member initiating receipt of retirement benefits, the System remits between $100 and $105 per month per eligible retiree to the Oklahoma State and Education Employees Group Insurance Board ("OSEEGIB"), depending on the members' years of service during 2012 and 2011. Such amounts were approximately $29,597,000 and $29,405,000 in 2012 and 2011, respectively, and are included in retirement and other benefits expense. Amounts due to OSEEGIB at June 30, 2012 and 2011, respectively are approximately $2,435,000 and $2,424,000 and are included in benefits in process of payment. The System performs no administrative functions related to the benefits provided by OSEEGIB and the payments have a minimal and declining impact on the operation of the System.

NOTE J--DEDICATED TAX

The System receives 5.0% of the State's sales, use, and corporate and individual income taxes collected as dedicated tax. The System receives 1% of the cigarette taxes collected by the State and receives 5% of net lottery proceeds collected by the State. The System received approximately $281,807,000 and $251,322,000 from the State in 2012 and 2011, respectively. Amounts due from the State were approximately $29,333,000 and $27,322,000 at June 30, 2012 and 2011, respectively.

NOTE K--PENSION PLAN FOR EMPLOYEES OF THE SYSTEM

The System also makes employer contributions for its employees who are also members of the System. The System's contributions are under the same terms as other participating employers, as discussed in Note H. In addition to the employer contributions, the System also pays the employees' contributions as a fringe benefit. Benefits paid to members that worked for the System are the same as those described in Note I. The total employee contributions paid by the System for its employees were approximately $161,000, $188,000, and $204,000 for the years ended June 30, 2012, 2011, and 2010, respectively. Total employer contributions paid by the System were approximately $219,000 $256,000, and $251,000 for the years ended June 30, 2012, 2011, and 2010 respectively. The employer contributions for FY 2012, 2011, and 2010 were 115.9%, 77.6%, and 83.6%, respectively, of the actuarial determined annual required contribution amounts and 100% of the contribution rate amounts determined by the legislature.

NOTE L--PLAN AMENDMENTS

The 2012 legislative session resulted in no bills with an actuarial impact on the system.

NOTE M--DB PLAN FUNDING STATUS AND ACTUARIAL INFORMATION

The System's actuary conducts an annual valuation to determine the adequacy of the current employer contribution rates, to describe the current financial condition of the System, and to analyze changes in the System's condition. This valuation shows the funded position of the System decreased from the funding level at June 30, 2011. Based on current statutes for determining the state, federal, and employer contribution rates, the funded period which is the number of years that would be required to amortize the unfunded actuarial accrued liability (the "UAAL") is 22.0 years. The actuarial accrued liability increased by 1,027.2 million and the actuarial value of assets increased $229.9 million. As a result, the System's unfunded actuarial accrued liabilities increased $797.4 million to $8,397.6 million at June 30, 2012. The funded ratio - actuarial value of assets divided by actuarial accrued liability - decreased from 56.7% to 54.8%.

The decrease in the UAAL is primarily due to a loss on assets with returns of only 1.3% on a market value basis and 3.3% on the actuarial value of assets compared to the assumed rate of 8.0%. Based on the current contribution schedule, assuming no actuarial gains or losses in the future, the UAAL is expected to continue increasing from the current level until fiscal year 2013 and decreasing through June 30, 2033 and beyond. The current contribution schedule results in contributions sufficient to cover the interest on the current UAAL plus the normal cost resulting in negative amortization.

NOTE M--DB PLAN FUNDING STATUS AND ACTUARIAL INFORMATION--Continued

The funded status of the System as of June 30, 2012, the most recent actuarial date, is as follows:

	(Amounts in Millions)	
Actuarial value of assets (a)	$ 10,190.5	
Actuarial accrued liability (AAL) (b)	$ 18,588.0	
Total unfunded actuarial accrued liability (UAAL) (b-a)	$ 8,397.6	
Funded ratio (a/b)		54.8%
Covered payroll	$ 3,924.8	
UAAL as a percentage of covered payroll		214.0%

The Schedule of Funding Progress immediately following the notes to the financial statements presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing relative to the actuarial accrued liability for benefits over time. The figures above (the UAAL, the funded ratio, and the funded period) are based on actuarial calculations that make use of the actuarial value of assets, not the fair value. Asset gains and losses (earnings greater or less than the 8% investment return assumption) are recognized 20% per year for five years in the actuarial value of assets; the current actuarial value ($10,190.5 million) is $4.2 million smaller than the market value of net assets ($10,194.7 million).

Significant actuarial assumptions employed by the actuary for funding purposes as of July 1, 2012 are as follows:

Funding Method: Costs are developed using the entry age normal cost method (based on a level percentage of covered payrolls). Under the method used for the System, the accrued liability and the present value of future normal costs are determined by summing the individual entry age results for each participant. The normal cost is then determined in aggregate by spreading the present value of future normal costs as a level percentage of expected future covered payrolls. Entry age is defined as the first day service is credited under the System.

Experience gains and losses (i.e., decreases or increases in accrued liabilities attributable to deviations in experience from the actuarial assumption) adjust the unfunded actuarial accrued liability.

Asset Valuation Method: The actuarial value of assets is equal to the market value, adjusted for a five-year phase in of actual investment return in excess of expected investment return. The actual return is calculated net of investment and administrative expenses, and the expected investment return is equal to the assumed investment return rate multiplied by the prior year's market value of assets, adjusted for contributions, benefits paid, and refunds.

Amortization: The unfunded actuarial accrued liability is amortized on a percent of pay method over a 30-year open period.

NOTE M--DB PLAN FUNDING STATUS AND ACTUARIAL INFORMATION--Continued

Investment Return: 8% per annum, compounded annually, (includes inflation of 3%).

Salary Increases: 4% to 12% per year (includes inflation of 3% and a productivity increase of 1%).

NOTE N--NEW PRONOUNCEMENTS

In December 2010, GASB issued Statement No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements (GASB 62) which is intended to enhance the usefulness of its Codification by incorporating guidance that previously could only be found in certain FASB and AICPA pronouncements. GASB 62 is effective for financial statements for periods beginning after December 15, 2011.

In June 2011, GASB issued Statement No. 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position (GASB 63) which provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources. Previous financial reporting standards do not include guidance for reporting those financial statement elements, which are distinct from assets and liabilities. GASB 63 is effective for financial statements for periods beginning after December 15, 2011.

In April 2012, the GASB issued Statement No. 65, Items Previously Reported as Assets and Liabilities (GASB 65). GASB 65 provides further guidance on determining which balances currently reported as assets and liabilities should instead be reported as deferred outflows or deferred inflows of resources. GASB 65 is effective for periods beginning after December 15, 2012, and will be applied on a retroactive basis.

In June 2012, the GASB issued Statement No. 67, Financial Reporting for Pension Plans (GASB 67). GASB 67 replaces the requirements of Statement No. 25, Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans and Statement 50, Pension Disclosures, as they relate to pension plans that are administered through trusts or similar arrangements meeting certain criteria. GASB 67 builds upon the existing framework for financial reports of defined benefit pension plans, which includes a statement of fiduciary net position (the amount held in a trust for paying retirement benefits) and a statement of changes in fiduciary net position. GASB 67 enhances note disclosures and required supplementary information (RSI) for both defined benefit and defined contribution pension plans. GASB 67 also requires the presentation of new information about annual money-weighted rates of return in the notes to the financial statements and in 10-year RSI schedules. The requirements of GASB 67 are effective for fiscal years beginning after June 15, 2013.

NOTE N--NEW PRONOUNCEMENTS--Continued

In June 2012, the GASB issued Statement No. 68, Accounting and Financial Reporting for Pensions (GASB 68). GASB 68 replaces the requirements of Statement No. 27, Accounting for Pensions by State and Local Governmental Employers and Statement No. 50 as they relate to governments that provide pensions through pension plans administered as trusts or similar arrangements that meet certain criteria. GASB 68 requires governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability for the first time, and to more comprehensively and comparably measure the annual costs of pension benefits. GASB 68 also enhances accountability and transparency through revised and new note disclosures and RSI. The requirements of GASB 68 are effective for fiscal years beginning after June 15, 2014.

The System is currently evaluating the effects the above GASB Pronouncements will have on its financial statements.

SCHEDULE OF FUNDING PROGRESS AND SCHEDULE OF EMPLOYERS' CONTRIBUTIONS (UNAUDITED)

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

(Dollar Amounts in Millions)

Actuarial Valuation Date	Actuarial Value of Assets (AVA) (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL) (b) - (a)	Funded Ratio (a / b)	Annual Covered Payroll	UAAL as % of Covered Payroll ((b-a) / c)
June 30, 2007	$ 8,421.9	$ 16,024.4	$ 7,602.5	52.6%	$ 3,598.9	211.2%
June 30, 2008	9,256.8	18,346.9	9,090.1	50.5%	3,751.4	242.3%
June 30, 2009	9,439.0	18,950.9	9,512.0	49.8%	3,807.9	249.8%
June 30, 2010	9,566.7	19,980.6	10,414.0	47.9%	3,854.8	270.2%
June 30, 2011	9,960.6	17,560.8	7,600.2	56.7%	3,773.3	201.4%
June 30, 2012	10,190.5	18,588.0	8,397.6	54.8%	3,924.8	214.0%

SCHEDULE OF EMPLOYERS' CONTRIBUTIONS (UNAUDITED)

Fiscal Year Ended June 30,	Annual Required Contribution	Percentage Contributed
2007	$ 575,745,142	93.1%
2008	590,495,652	101.1%
2009	714,367,558	86.6%
2010	742,286,289	83.6%
2011	822,419,996	77.6%
2012	588,287,377	115.9%

The employer contribution rates are established by the Oklahoma Legislature. The annual required contribution is performed to determine the adequacy of such contribution rates.

Unaudited – see accompanying independent auditor's report.

SCHEDULE OF INVESTMENT EXPENSES

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

	Year Ended June 30	
	2012	2011
Investment managers	$ 34,057,188	$ 35,208,804
Investment consultants	702,000	702,000
Investment information services	22,800	22,800
Total investment expenses	$ 34,781,988	$ 35,933,604

See accompanying independent auditors' report.

SCHEDULE OF ADMINISTRATIVE EXPENSES

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

	Year Ended June 30	
	2012	2011
Salaries and benefits	$ 2,937,489	$ 3,293,768
General and miscellaneous	838,699	826,192
Professional/consultant fees	356,438	446,770
Travel and related expenses	83,645	106,717
Depreciation expense	56,918	43,033
Total administrative expenses	$ 4,273,189	$ 4,716,480

See accompanying independent auditors' report.

SCHEDULE OF PROFESSIONAL/CONSULTANT FEES

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

	Year Ended June 30 2012	Year Ended June 30 2011
Actuarial	$ 61,709	$ 123,661
Medical	8,700	9,590
Legal	101,549	88,714
Audit	46,100	44,800
Data processing	-	12,518
Miscellaneous	138,380	167,487
Total professional/ consultant fees	$ 356,438	$ 446,770

See accompanying independent auditors' report.

Independent Auditors' Report on
Internal Control over Financial Reporting and on
Compliance and Other Matters Based on an Audit of Financial
Statements Performed in Accordance with *Government Auditing Standards*

Board of Trustees
Teachers' Retirement System of Oklahoma

We have audited the financial statements of Teachers' Retirement System of Oklahoma (the "System"), which is a component unit of the state of Oklahoma, as of and for the year ended June 30, 2012, and have issued our report thereon dated December 11, 2012, which includes explanatory paragraphs related to the System's unfunded actuarial accrued liability, required supplementary information and other supplementary information. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements of the System as of and for the year ended June 30, 2012, in accordance with auditing standards generally accepted in the United States of America, we considered the System's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, we do not express an opinion on the effectiveness of the System's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

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Our consideration of internal control was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Board of Trustees, the Oklahoma State Auditor and Inspector, and management and is not intended to be and should not be used by anyone other than these specified parties.

Cole & Reed P.C.

Oklahoma City, Oklahoma
December 11, 2012