

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

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Independent Auditors' Report

Board of Trustees
Oklahoma Teachers' Retirement System
Oklahoma City, Oklahoma

Report on the Financial Statements

We have audited the accompanying financial statements of the Oklahoma Teachers' Retirement System of Oklahoma (the System), a part of the financial reporting entity of the state of Oklahoma, which comprise the statement of fiduciary net position as of June 30, 2014, and the related statement of changes in fiduciary net position for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Oklahoma Teachers' Retirement System as of June 30, 2014, and the respective changes in its financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note N of the financial statements, in 2014 the System adopted Governmental Accounting Standards Board (GASB) Statement No. 67, *Financial Reporting for Pension Plans*. Our opinion is not modified with respect to this matter.

Report on Summarized Comparative Information

We have previously audited the System's fiscal year 2013 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated November 8, 2013. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2013, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Other Matters*Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and the required supplementary information, as listed in the table of contents, 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.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The information included in pages 34 through 36 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.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued a report dated November 10, 2014, on our consideration of the System's internal control over financial reporting and on 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* in considering the System's internal control over financial reporting and compliance.

Cole & Reed P.C.

Oklahoma City, Oklahoma
November 10, 2014

Management's Discussion and Analysis
Teachers' Retirement System of Oklahoma
June 30, 2014 and 2013

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, 2014 and 2013. 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 403(b) plan which is a tax-advantaged retirement savings plan available for public education organizations. 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 fiduciary net position*, 2) *statement of changes in fiduciary net position*, 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 fiduciary net position* presents information on all of the System's assets, deferred outflows of resources, liabilities, and deferred inflows of resources, with the difference between these reported as *net position restricted for pensions*. Over time, increases or decreases in plan net position 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 fiduciary net position* but is located in both the *notes to the financial statements* and the *required supplementary information*.

The *statement of changes in fiduciary net position* presents information showing how the System's net position changed during the most recent fiscal year. Changes in net position 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 Changes in Employers' Net Pension Liability, Schedule of Employers' Net Pension Liability, Schedule of Contributions from Employers and Other Contributing Entities and Schedule of Investment Returns. Other supplementary information includes the Schedule of Administrative Expenses, the Schedule of Investment Expenses, and the Schedule of Professional/Consultants Fees. These schedules provide additional analysis of the information provided in the financial statements.

Management's Discussion and Analysis (Continued)
Teachers' Retirement System of Oklahoma
June 30, 2014 and 2013

CONDENSED FINANCIAL INFORMATION

Fiduciary net position as of June 30:

	2014	2013	2014 % Change
ASSETS			
Cash	\$ 17,695,733	\$ 14,903,504	18.7%
Receivables	201,958,789	286,998,149	-29.6%
Long- and short-term investments, at fair value	14,531,814,990	12,133,453,542	19.8%
Capital assets, net	2,848,571	2,180,235	30.7%
TOTAL INVESTMENTS AND OTHER ASSETS	14,754,318,083	12,437,535,430	18.6%
Securities lending institutional daily assets fund	2,475,662,654	2,363,777,689	4.7%
TOTAL ASSETS	17,229,980,737	14,801,313,119	16.4%
LIABILITIES			
Investment settlements and other liabilities	314,844,654	397,929,117	-20.9%
Payable under securities lending agreement	2,475,662,654	2,363,777,689	4.7%
TOTAL LIABILITIES	2,790,507,308	2,761,706,806	1.0%
NET POSITION			
Net position restricted for pensions	<u>\$ 14,439,473,429</u>	<u>\$ 12,039,606,313</u>	<u>19.9%</u>

Changes in fiduciary net position for the year ended June 30:

	2014	2013	2014 % Change
ADDITIONS:			
Member contributions	\$ 301,300,811	\$ 290,044,395	3.9%
Employer contributions	386,895,127	373,789,020	3.5%
Matching contributions	24,352,831	26,995,423	-9.8%
Dedicated tax revenue	295,804,717	300,509,886	-1.6%
Member tax shelter contributions	3,026,532	2,910,706	4.0%
Net investment income gain (loss)	2,587,292,673	1,783,073,902	45.1%
Security lending net income	8,590,136	9,531,387	-9.9%
TOTAL ADDITIONS	3,607,262,827	2,786,854,719	29.4%
DEDUCTIONS:			
Benefit payments	1,153,051,607	1,095,144,055	5.3%
Refund of member contributions and tax sheltered annuity	50,061,499	52,732,344	-5.1%
Administrative expenses	4,282,605	4,156,867	3.0%
TOTAL DEDUCTIONS	1,207,395,711	1,152,033,266	4.8%
NET INCREASE IN NET POSITION	2,399,867,116	1,634,821,453	46.8%
NET POSITION RESTRICTED FOR PENSIONS			
BEGINNING OF YEAR	12,039,606,313	10,404,784,860	15.7%
END OF YEAR	<u>\$ 14,439,473,429</u>	<u>\$ 12,039,606,313</u>	<u>19.9%</u>

Management's Discussion and Analysis (Continued)
Teachers' Retirement System of Oklahoma
June 30, 2014 and 2013

FINANCIAL HIGHLIGHTS AND ANALYSIS

The increase in net position primarily is due to investment gains as a result of significant market improvement in fiscal year 2014. The total investment returns for fiscal year 2014 were positive 22.4%. Domestic and international equity compose 67.8% of the investment portfolio asset allocation; domestic equity returned 27.6% while international equity returned 21.1%.

	2014	2013
Plan net position	\$ 14,439,473,429	\$ 12,039,606,313
Yearly % change	19.9%	15.7%

The total investment return for the five year period of 16.1% is above the actuarial assumed rate of investment return. The continued strengthening of the United States and global markets has driven this rate up since 2009. The assumed actuarial rate of return is currently 8.0%.

Total Returns	1 year	3 year	5 year	10 year
2014	22.4%	13.6%	16.1%	9.0%
2013	17.8%	14.0%	7.7%	8.8%

Benefit payments increased 5.3% in 2014 compared to 2013. The increase is a result of a 3.3% increase in the number of benefit recipients and a 0.5% increase in the average monthly benefit. Benefit payments in 2014 to retired members exceed contributions from contributing members and employers by \$173 million, or a ratio of 1.17 to 1. A ratio of less than one would signify that the System is receiving more contributions than it pays out in benefits. While that may be desirable, that would be very rare for a mature defined benefit retirement system. In a mature pension system like OTRS a significant percentage of the benefits are paid out of investment earnings that are not reflected in this ratio. The table on the following page reflects the ongoing employer and member contributions.

	2014	2013
Member contributions	\$ 301,300,811	\$ 290,044,395
Employer contributions	386,895,127	373,789,020
Matching contributions	24,352,831	26,995,423
Dedicated tax revenue	295,804,717	300,509,886
Total contributions	<u>\$ 1,008,353,486</u>	<u>\$ 991,338,724</u>
Benefit payments	\$ 1,153,051,607	\$ 1,095,144,055
Refund of contributions	28,718,256	28,894,193
Total payments	<u>\$ 1,181,769,863</u>	<u>\$ 1,124,038,248</u>

Management's Discussion and Analysis (Continued)
Teachers' Retirement System of Oklahoma
June 30, 2014 and 2013

FINANCIAL HIGHLIGHTS AND ANALYSIS (Continued)

The number of benefit recipients increased 3.3% in 2014 as compared to 3.5% in 2013. This is comparable the fiscal year 2013. The increase in the number of benefit recipients has remained consistent over the past year. There was a net increase of 1,808 and 1,865 members that entered retirement for fiscal year 2014 and fiscal year 2013, respectively.

	2014	2013
Benefit recipients	56,389	54,581
Yearly % change	3.3%	3.5%
Net increase	1,808	1,865

The following table reflects the average monthly benefit for service retirements. While the table above reflects an increase in the number of retirees in the past year of 3.3% the table below reflects the average benefit per retiree has only increased by 0.5% in 2014 as compared to 2013. The increase in benefit recipients was 3% higher than the increase in average benefit payment below. This is due to members retiring at a younger age and receiving a lower average benefit payment than in fiscal year 2013.

	2014	2013
Average benefit	\$ 1,599	\$ 1,591
Yearly % change	0.5%	2.3%

The ratio of active members to retired members of the System is 1.59 to 1 in 2014, compared to 1.64 to 1 in 2013. This change is caused by the longevity of the Plan's retiree population and an active population that has leveled off. Contributing members increased by 237 while benefit recipients increased by 1,808.

	2014	2013
Members contributing	89,570	89,333
Yearly % change	0.3%	1.8%
Benefit recipients	56,389	54,581
Yearly % change	3.30%	3.50%
Ratio contributing/retired	1.59	1.64

The manner of calculating the funded ratio changed during fiscal year 2014 due to the adoption of GASB Statement No. 67, *Financial Reporting for Pension Plans*. For this reason, there is no comparative presentation for fiscal year 2013.

	2014
Total pension liability	\$ 19,646,619,191
Plan fiduciary net position	142,229,481,368
Ratio of plan fiduciary net position to total pension liability	72.43%

Management's Discussion and Analysis (Continued)
Teachers' Retirement System of Oklahoma
June 30, 2014 and 2013

FINANCIAL HIGHLIGHTS AND ANALYSIS (Continued)

Under GASB Statement 67 this ratio represents the Total Pension Liability compared to the Plan's total net position at market value. Prior to GASB Statement 67 this ratio was calculated using the actuarial value of the Plan's net position.

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 FIDUCIARY NET POSITION

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

As of June 30, 2014 (with Comparative Totals as of June 30, 2013)

	401(a) Plan	403(b) Plan	Totals June 30	
	2014	2013		
ASSETS				
Cash	\$ 17,695,733	\$ -	\$ 17,695,733	\$ 14,903,504
Short-term investments	432,300,020	-	432,300,020	796,745,800
Accrued interest and dividends receivable	43,053,787	-	43,053,787	39,448,046
Member contributions receivable	17,342,295	-	17,342,295	17,143,101
Employer contributions receivable	26,714,511	-	26,714,511	26,082,418
Receivable from the State of Oklahoma	30,261,548	-	30,261,548	28,855,587
Due from brokers for securities sold	84,586,648	-	84,586,648	175,468,997
Security lending institutional daily assets fund	2,475,662,654	-	2,475,662,654	2,363,777,689
Long-term investments:				
Mutual funds	-	209,992,061	209,992,061	204,133,915
U.S. government securities	803,376,179	-	803,376,179	1,056,986,977
U.S. corporate bonds	1,915,066,646	-	1,915,066,646	1,657,819,302
International corporate bonds and government securities	135,500,052	-	135,500,052	117,154,794
Equity securities	9,856,801,852	-	9,856,801,852	7,357,893,901
Alternative investments	587,418,530	-	587,418,530	412,641,707
Real estate	591,359,650	-	591,359,650	530,077,146
Total long-term investments	13,889,522,909	209,992,061	14,099,514,970	11,336,707,742
Capital assets, net	2,848,571	-	2,848,571	2,180,235
TOTAL ASSETS	\$ 17,019,988,676	\$ 209,992,061	\$ 17,229,980,737	\$ 14,801,313,119
LIABILITIES				
Benefits in process of payment	\$ 75,135,942	\$ -	\$ 75,135,942	\$ 71,624,164
Due to brokers for securities purchased	226,440,313	-	226,440,313	317,047,427
Payable under security lending agreement	2,475,662,654	-	2,475,662,654	2,363,777,689
Other liabilities	13,268,399	-	13,268,399	9,257,526
TOTAL LIABILITIES	\$ 2,790,507,308	\$ -	\$ 2,790,507,308	\$ 2,761,706,806
NET POSITION				
Net position restricted for pensions	\$ 14,229,481,368	\$ 209,992,061	\$ 14,439,473,429	\$ 12,039,606,313

See notes to financial statements.

STATEMENTS OF CHANGES IN FIDUCIARY NET POSITION

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

For the Year Ended June 30, 2014 (with Comparative Totals for the Year Ended June 30, 2013)

	401(a) Plan	403(b) Plan	Totals Year Ended June 30	
			2014	2013
Additions:				
Members	\$ 301,300,811	\$ -	\$ 301,300,811	\$ 290,044,395
Members tax shelter	-	3,026,532	3,026,532	2,910,706
Employer statutory requirement from local school districts	386,895,127	-	386,895,127	373,789,020
Matching funds	24,352,831	-	24,352,831	26,995,423
Dedicated tax	295,804,717	-	295,804,717	300,509,886
Total contributions	1,008,353,486	3,026,532	1,011,380,018	994,249,430
Investment income:				
Interest & dividends	356,982,304	11,221,530	368,203,834	331,330,336
Net appreciation in fair value of investments	2,255,051,791	12,953,327	2,268,005,118	1,488,032,970
Investment expenses	(48,916,279)	-	(48,916,279)	(36,289,404)
Gain from investing activities	2,563,117,816	24,174,857	2,587,292,673	1,783,073,902
Income from securities lending activities:				
Securities lending income	10,106,042	-	10,106,042	11,213,396
Securities lending expenses:				
Management fees:	(1,515,906)	-	(1,515,906)	(1,682,009)
Net income from securities lending activities	8,590,136	-	8,590,136	9,531,387
Net investment gain	2,571,707,952	24,174,857	2,595,882,809	1,792,605,289
Total additions	3,580,061,438	27,201,389	3,607,262,827	2,786,854,719
Deductions:				
Retirement, death, survivor, and health benefits	1,153,051,607	-	1,153,051,607	1,095,144,055
Refund of member contributions and annuity payments	28,718,256	21,343,243	50,061,499	52,732,344
Administrative expenses	4,282,605	-	4,282,605	4,156,867
Total deductions	1,186,052,468	21,343,243	1,207,395,711	1,152,033,266
NET INCREASE (DECREASE) IN NET POSITION	2,394,008,970	5,858,146	2,399,867,116	1,634,821,453
NET POSITION RESTRICTED FOR PENSIONS, BEGINNING OF YEAR	11,835,472,398	204,133,915	12,039,606,313	10,404,784,860
NET POSITION RESTRICTED FOR PENSIONS, END OF YEAR	\$ 14,229,481,368	\$ 209,992,061	\$ 14,439,473,429	\$ 12,039,606,313

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

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. The plan's benefits are established and amended by State Statute and 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 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").

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 board of trustees is comprised of six appointees from the Governor's Office, two appointees by the Senate Pro Tempore, two appointees by the House Speaker and three Ex Officio positions. Out of the six appointees from the Governor's Office, one must be a Higher Education representative, one is a nonclassified optional personnel, and the remaining four must work in the public or private funds management, banking, law or accounting field. Out of the two Senate Pro Tempore's as well as the House Speaker's appointees, one must be an active classroom teacher while the other be a retired member of Oklahoma Teachers Retirement. The Ex Officio trustees are the State Superintendent, the Office of Management and Enterprise Services Director and the Career-Tech Director or their designee.

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 employees of 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. There are 607 contributing employers in the System. The DB Plan's membership consisted of the following as of June 30:

	2014
Inactive Plan Members or Beneficiaries Currently Receiving Benefits	56,389
Inactive Plan Members Entitled to But Not Yet Receiving Benefits*	10,704
Active Plan Members	89,570
	<u>156,663</u>

* Does not include 9,735 of nonvested terminated members entitled to a refund of their member contributions.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

NOTE A--DESCRIPTION OF THE SYSTEM--Continued

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.

The DC Plan had approximately 3,783 participants as of June 30, 2014. 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 \$17,500. Participants age 50 and older may contribute an additional \$5,500 if they qualify for the catch up provision.

NOTE B--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting: 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.

Budgetary Control: The System prepares and submits an annual budget of operating expenses on the cash basis for monitoring and reporting to the Office of Management and Enterprise Services. The System's budget process follows the budget cycle for State operations as outlined by the Office of Management and Enterprise Services.

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.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

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

Investments: 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. The Board reviews and updates the plan investment policy at least annually, making changes as deemed necessary to achieve policy goals. An investment policy change can be made anytime during the year at the discretion of the Board. There were no significant investment policy changes for FY-2014.

System investments are reported at fair value. The short-term investment fund is comprised primarily of investments in a money market fund, which are 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.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

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

Investments--Continued: 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.

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. 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, 2014.

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 position.

At June 30, 2014, the asset allocation guidelines established by the Board's investment policy were 40% in Domestic Equity, 17.5% in International Equity, 23.5% in Fixed Income, 5% in Private Equity, 7% in Real Estate and 7% in Master Limited Partnerships.

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 Note M and 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.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

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 \$202,000 at June 30, 2014.

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 position held in trust for pension benefits at the date of the financial statements and the actuarial information included in Note M and the required supplementary information as of the benefit information date, the changes in System net position 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.

Comparative Totals: The financial statements include certain prior year summarized comparative information in total but not at the level of detail required for a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the System's financial statements for the year ended June 30, 2013, from which the summarized information was derived.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

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, 2014, the carrying amount of the System's bank deposits was approximately \$17,696,000. The bank balance of the System's bank deposits at June 30, 2014 was approximately \$19,075,000.

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, 2014, the System had uninsured and uncollateralized cash and cash equivalents of approximately \$14,123,000 with its custodial agent. The System's custodial agent for the years ended June 30, 2014 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, 2014

NOTE C--CASH AND INVESTMENTS--Continued

Credit Risk--Continued:

Investment Type	S&P Ratings (Unless Noted)	Fair Value <i>(in Thousands)</i>	Fair Value as a Percent of Total Fixed Income Fair Value
U.S. Corporate Bonds	AAA	\$ 91,190	3.2%
	AA+	43,565	1.5%
	AA	8,095	0.3%
	AA-	7,384	0.3%
	A+	21,450	0.8%
	A	58,193	2.0%
	A-	102,703	3.6%
	BBB+	102,670	3.6%
	BBB	180,720	6.3%
	BBB-	268,419	9.4%
	BB+	148,025	5.2%
	BB	174,505	6.1%
	BB-	160,942	5.6%
	B+	96,638	3.4%
	B	112,772	4.0%
	B-	118,620	4.2%
	CCC+	72,055	2.5%
	CCC	14,821	0.5%
	CCC-	7,761	0.3%
	CC	293	0.0%
	D	1,338	0.1%
	NR	112,416	3.9%
Total U.S. Corporate Bonds		1,904,575	66.8%
International Corporate Bonds	AA-	3,307	0.1%
	A-	3,200	0.1%
	BBB+	1,726	0.1%
	BBB	4,242	0.1%
	BBB-	5,572	0.2%
	BB-	1,057	0.1%
	B+	3,462	0.1%
	B	3,006	0.1%
	CCC+	3,228	0.1%
	NR	2,576	0.1%
Total International Corporate Bonds		31,376	1.1%

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

NOTE C--CASH AND INVESTMENTS--Continued

Investment Type	S&P Ratings (Unless Noted)	Fair Value <i>(in Thousands)</i>	Fair Value as a Percent of Total Fixed Income Fair Value
International government securities	AAA	11,064	0.4%
	AA+	4,905	0.2%
	AA	2,908	0.1%
	AA-	691	0.0%
	A+	1,723	0.1%
	A	27,653	1.0%
	A-	301	0.0%
	BBB+	4,526	0.2%
	BBB	14,591	0.5%
	BBB-	2,194	0.1%
	BB+	3,507	0.1%
	BB-	218	0.0%
	B+	1,439	0.1%
	B	1,161	0.0%
	B-	1,011	0.0%
	CCC-	126	0.0%
	NR	26,106	0.9%
Total international government securities		104,124	3.7%
Municipal bonds	AAA	998	0.0%
	AA+	271	0.0%
	AA	412	0.0%
	AA-	2,149	0.1%
	A	3,192	0.1%
	A-	1,743	0.1%
	BBB+	1,218	0.0%
	NR	509	0.0%
Total municipal bonds		10,492	0.3%
U.S. government securities	AA+	802,741	28.1%
	A+	635	0.0%
Total U.S. government securities		803,376	28.1%
		<u>\$ 2,853,943</u>	<u>100.0%</u>

Short-term investments include \$407,911,051 invested in a money market mutual fund with an S&P rating of AAAm.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

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, 2014, the System had the following investments with maturities:

Investment Type	Investment Maturities at Fair Value (in Years)				
	<i>(in Thousands)</i>				
	Less than One	One to Five	Five to Ten	More than Ten	Total Fair Value
U.S. corporate securities:					
Asset-backed securities	\$ 36,103	\$ 51,822	\$ 12,817	\$ 9,827	\$ 110,569
CMO/REMIC/CMBS	83,892	1,138	5,116	42,156	132,302
Corporate bonds	72,981	405,992	957,389	225,342	1,661,704
	192,976	458,952	975,322	277,325	1,904,575
International corporate bonds	8,532	10,677	8,892	3,275	31,376
International governmental securities	30,185	19,600	31,861	22,478	104,124
Municipal bonds	-	-	-	10,492	10,492
U.S. government securities	47,278	210,156	26,037	519,905	803,376
	<u>\$ 278,971</u>	<u>\$ 699,385</u>	<u>\$ 1,042,112</u>	<u>\$ 833,475</u>	<u>\$ 2,853,943</u>

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. or Japan such limit shall be 35%. Investment in cash and cash equivalents, foreign equities, and fixed-income securities as of June 30, 2014 is shown in the following table by monetary unit to indicate possible foreign currency risk.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

NOTE C--CASH AND INVESTMENTS--Continued

Foreign Currency Risk--Continued:

<i>(in Thousands)</i>						
Currency	Equities	Corporate Bonds	Government Bonds	Foreign Exchange Contracts	Cash and Cash Equivalents	Grand Total
Australian Dollar	\$ 65,059	\$ 1,835	\$ -	\$ -	\$ 40	\$ 66,934
Brazilian Real	11,042	4,598	3,102	-	-	18,742
Canadian Dollar	37,191	289	-	-	-	37,480
Chilean Peso	245	-	1,245	-	-	1,490
Colombia Peso	3,250	-	266	-	-	3,516
Danish Krone	33,759	-	-	-	-	33,759
Euro	622,500	12,358	21,451	362	1,134	657,805
Hong Kong Dollar	107,335	-	-	(1)	(5)	107,329
Indonesian Rupiah	3,794	-	-	-	-	3,794
Israeli Shekel	892	-	-	-	-	892
India Rupee	-	-	2,289	-	-	2,289
Japanese Yen	458,771	-	-	(1,522)	124	457,373
Malaysian Ringgit	3,811	-	-	-	-	3,811
Mexican Peso	7,113	4,192	31,610	-	-	42,915
New Taiwan Dollar	20,567	-	-	-	-	20,567
New Turkish Lira	5,748	-	-	-	-	5,748
New Zealand Dollar	2,699	-	-	-	-	2,699
Norwegian Krone	27,266	1,164	-	-	-	28,430
Phillipine Peso	5,248	-	8,250	-	-	13,498
Polish Zloty	3,489	-	-	-	-	3,489
Pound Sterling	407,075	6,940	-	(44)	485	414,456
Qatari Rial	548	-	-	-	-	548
Singapore Dollar	27,171	-	-	-	-	27,171
South African Rand	15,442	-	-	-	-	15,442
South Korean Won	36,997	-	-	-	-	36,997
Swedish Krona	44,926	-	-	-	-	44,926
Swiss Franc	191,284	-	-	(2)	-	191,282
Thai Baht	4,151	-	-	-	-	4,151
UAE Dirham	1,555	-	-	-	-	1,555
	<u>2,148,928</u>	<u>31,376</u>	<u>68,213</u>	<u>(1,207)</u>	<u>1,778</u>	<u>2,249,088</u>
Not subject to foreign currency risk	<u>7,707,874</u>	<u>-</u>	<u>35,911</u>	<u>-</u>	<u>430,522</u>	<u>8,174,307</u>
Total	<u>\$ 9,856,802</u>	<u>\$ 31,376</u>	<u>\$ 104,124</u>	<u>\$ (1,207)</u>	<u>\$ 432,300</u>	<u>\$ 10,423,395</u>

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

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 changes in fair values of the System's investment derivatives are included in net appreciation in fair value of investments in the accompanying statement of plan net position. The fair values of the System's investment derivatives are included in due from brokers for securities sold and due to brokers for securities purchased in the accompanying statement of plan net position. The fair value balances and notional amounts of derivative instruments outstanding at June 30, 2014, classified by type, and the changes in fair value of such derivative instruments for the year then ended as reported in the 2014 financial statements are as follows:

Investment Derivatives	(in Thousands)		
	Change in Fair Value	Fair Value	Notional
Forward - foreign currency purchases	\$ 2,315	\$ (14)	\$ 4,766,933
Forward - foreign currency sales	(3,389)	(1,193)	8,068,731

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.

Rate of Return: For the year ended June 30, 2014, the annual money-weighted rate of return on pension plan investments, net of pension plan investment expense, was 21.95%. The money-weighted rate of return expresses investment performance, net of investment expense, as adjusted for the changing amounts actually invested.

NOTE D--COMMITMENTS

Commitments: At June 30, 2014, the System has total capital commitments related to alternative and real estate investments of \$1,913,000,000. Of this amount, \$882,424,723 remained unfunded.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

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, 2014 was approximately \$2,538,821,000. The underlying collateral for these securities had a fair value of approximately \$2,602,209,000 at June 30, 2014. Collateral of securities and letters of credit represented approximately \$126,546,000 of total collateral at June 30, 2014. 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 position. The following table describes the types of securities lent and collateral as of June 30, 2014.

Type of securities on loan	(in Thousands)	
	Market Value of Securities on Loan	Collateral Value
Government loans compared to non-cash collateral	\$ 87,384	\$ 89,147
Equity loans compared to cash collateral	2,414,925	2,475,663
Corporate loans compared to non-cash collateral	36,512	37,399
	<u>\$ 2,538,821</u>	<u>\$ 2,602,209</u>

At June 30, 2014, 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.

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, 2014, the weighted average maturity of the cash collateral investments was 61 days. 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.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

NOTE F--CAPITAL ASSETS

Capital assets consist of the following at June 30, 2014:

	<i>(in Thousands)</i>
Furniture and fixtures	\$ 3,098
Accumulated depreciation	<u>(250)</u>
Capital assets, net	<u>\$ 2,848</u>

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, 2014 was approximately \$208,000. The System's leases are one-year renewable contracts. Rental expense for all operating leases amounted to approximately \$215,000 for the year ended June 30, 2014.

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:

- 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. On April 7, 2014 the ING U.S., Inc publicly traded parent company officially changed its name to Voya Financial, Inc. This had no impact on the DC Plan and did not require the DC Plan to amend the contract or agreement. Voya Financial provides a comprehensive educational strategy and an array of investment options, clients have 24 hours a day access to their accounts on line, and dedicated customer service representatives are available each weekday from 7:00 A.M. to 7:00 P.M.
- 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:

	<i>(in Thousands)</i>
	<u>2014</u>
Teacher's deposit fund (DC Plan)	\$ 209,992
Expense fund	62,071
Capital assets fund	<u>2,848</u>
	<u>\$ 274,911</u>

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

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, 2014 were \$386,895,127. Employers satisfied 100% of their contribution requirements for 2014.

All members must contribute 7% of regular annual compensation, not to exceed the member's maximum compensation level, which for the year ended June 30, 2014 was the full amount of regular annual compensation.

The employers are required to contribute a fixed percentage of annual compensation on behalf of active clients. The employer contribution rate was 9.5% beginning on January 1, 2011 for all remitting entities other than comprehensive and four year regional universities. The employer contribution rate was 8.55% starting on January 1, 2011 for comprehensive and four year universities. The rates for fiscal years 2014 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.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

NOTE I--BENEFITS--Continued

- 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 are calculated based on each member's final average compensation, except for certain employees of the two comprehensive universities. 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 Employees Group Insurance Division ("EGID"), depending on the members' years of service during 2014. Such amounts were approximately \$30,136,000 in 2014 and are included in retirement and other benefits expense. The System performs no administrative functions related to the benefits provided by EGID, and the payments have a minimal and declining impact on the operation of the System.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

NOTE J--DEDICATED TAX

The plan receives funds provided by the State of Oklahoma, a non-employer contributing entity, through 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 \$295,805,000 from the State in 2014. Amounts due from the State were approximately \$30,262,000 at June 30, 2014.

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 \$158,000, \$168,000 and \$161,000 for the years ended June 30, 2014, 2013, and 2012, respectively. Total employer contributions paid by the System were approximately \$214,000, \$227,000, and \$219,000 for the years ended June 30, 2014, 2013, and 2012, respectively. The employer contributions for FY 2014, 2013, and 2012 were 117.3%, 113.1%, and 115.9%, 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 2014 legislative session resulted in no bills with an actuarial impact on the system.

NOTE M--DB PLAN NET PENSION LIABILITY AND ACTUARIAL INFORMATION

The Components of the net pension liability of the employers' at June 30, 2014, were as follows:

Total pension liability	\$ 19,646,619,191
Plan fiduciary net position	<u>(14,229,481,368)</u>
Employers' net pension liability	<u>\$ 5,417,137,823</u>
Plan fiduciary net position as a percentage of the total pension liability	72.43%

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

NOTE M--DB PLAN NET PENSION LIABILITY AND ACTUARIAL INFORMATION--Continued

The total pension liability as of June 30, 2014, was determined based on an actuarial valuation prepared as if June 30, 2014 using the following actuarial assumptions:

- Actuarial Cost Method - Entry Age Normal
- Amortization Method - Level Percentage of Payroll
- Amortization Period - Amortization over an open 30-year period
- Asset Valuation Method - 5-year smooth market
- Inflation - 3.00%
- Salary Increases - Composed of 3.00% inflation, plus 1.00% productivity increase rate, plus step-rate promotional increases for members with less than 25 years of service.
- Investment Rate of Return - 8.00%
- Retirement Age - Experience-based table of rates based on age, service, and gender. Adopted by the Board in September 2010 in conjunction with the five year experience study for the period ending June 30, 2009.
- Mortality - RP-2000 Combined Mortality Table, projected to 2016 using Scale AA, multiplied by 90% for males and 80% for females.

Measurement of the Net Pension Liability: The net pension liability is measured as the total pension liability, less the amount of the plan's fiduciary net position. In actuarial terms, this is analogous to the accrued liability as measured using the individual entry age normal actuarial cost method less the market value of assets (not the smoothed actuarial value of assets seen in actuarial valuations based on the Board's adopted assumptions and methods).

A single discount rate of 8.00% was used to measure the total pension liability as of June 30, 2013 and June 30, 2014. This single discount rate was based solely on the expected rate of return on pension plan investments of 8.00%. Based on the stated assumptions and the projection of cash flows, the pension plan's fiduciary net position and future contributions were projected to be available to finance all projected future benefit payments of current plan members.

Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

The projection of cash flows used to determine this single discount rate assumed that plan member and employer contributions will be made at the current statutory levels and remain a level percentage of payroll. The projection of cash flows also assumed that the State's contribution plus the matching contributions will remain a constant percent of projected member payroll based on the past five years of actual contributions.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

NOTE M--DB PLAN NET PENSION LIABILITY AND ACTUARIAL INFORMATION--Continued

Measurement of the Net Pension Liability--Continued: The long-term expected rate of return on pension plan investments was determined using a building block method in which best estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation

The target asset allocation and best estimates of arithmetic expected real rates of return for each major asset class as of June 30, 2014, are summarized in the following table:

Asset Class	Target Asset Allocation	Long-Term Expected Real Rate of Return
Domestic All Cap Equity*	7.0%	6.7%
Domestic Large Cap Equity	10.0%	6.2%
Domestic Mid Cap Equity	13.0%	6.9%
Domestic Small Cap Equity	10.0%	7.0%
International Large Cap Equity	11.5%	7.0%
International Small Cap Equity	6.0%	7.0%
Core Plus Fixed Income	17.5%	2.1%
High-yield Fixed Income	6.0%	4.5%
Private Equity	5.0%	7.9%
Real Estate**	7.0%	5.5%
Master Limited Partnerships	7.0%	7.9%
Total	100.0%	

* The Domestic All Cap Equity total expected return is a combination of 3 rates - US Large cap, US Mid Cap and US Small cap

** The Real Estate total expected return is a combination of US Direct Real Estate (unlevered) and US Value added Real Estate (unlevered)

Sensitivity of the Net Pension Liability to the Single Discount Rate Assumption: The following table provides the sensitivity of the net pension liability to changes in the discount rate as of June 30, 2014. In particular, the table presents the plan's net pension liability, if it were calculated using a single discount rate that is one-percentage-point lower or one-percentage-point higher than the single discount rate:

	1% Decrease (7.00%)	Current Discount Rate (8.00%)	1% Increase (9.00%)
Net pension liability	\$ 7,610,368,171	\$ 5,417,137,823	\$ 3,565,976,493

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

NOTE N--NEW PRONOUNCEMENTS

New Accounting Pronouncements Adopted in Fiscal Year 2014

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. The adoption of GASB 65 did not have a significant impact on the System's financial statements.

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. Adoption of GASB 67 had no impact on the System's net position but did result in changes to the presentation of the financial statements, notes to the financial statements, and RSI. Comparative information has not been presented for disclosures required by GASB 67 as presentation of the information for prior years was not practical.

In April 2013, the GASB issued Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees* (GASB 70). GASB 70 requires a government that extends a nonexchange financial guarantee to recognize a liability when qualitative factors and historical data, if any, indicate that it is more likely than not that the government will be required to make a payment on the guarantee. GASB 70 also provides additional guidance for intra-entity nonexchange financial guarantees involving blended component units and specifies information required to be disclosed by governments that extend and/or receive nonexchange financial guarantees. The adoption of GASB 70 did not significantly impact the System's financial statements.

New Accounting Pronouncements Issued, Not Yet Adopted

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.

NOTES TO FINANCIAL STATEMENTS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

NOTE N--NEW PRONOUNCEMENTS--Continued

New Accounting Pronouncements Issued, Not Yet Adopted--Continued

In January 2013, the GASB issued Statement No. 69, *Government Combinations and Disposals of Government Operations* (GASB 69). GASB 69 establishes guidance for 1) determining whether a specific government combination is a government merger, a government acquisition, or a transfer of operations; 2) using carrying values to measure the assets, deferred outflows of resources, liabilities, and deferred inflows of resources combined in a government merger or transfer of operations; 3) measuring acquired assets, deferred outflows of resources, liabilities, and deferred inflows of resources based upon their acquisition values in a government acquisition; and 4) reporting the disposal of government operations that have been transferred or sold. The requirements of GASB 69 are effective for fiscal years beginning after December 15, 2013.

In November 2013, the GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – an Amendment of GASB Statement No. 68* (GASB 71). GASB 71 addresses an issue regarding application of the transition provisions of GASB 68. Contributions to a defined benefit pension plan between the measurement date of the reported net pension liability and the end of the reporting period are required to be recognized as deferred outflows of resources. The requirements of GASB 71 are effective simultaneously with GASB 68.

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

SCHEDULE OF CHANGES IN EMPLOYERS' NET PENSION LIABILITY (UNAUDITED)

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

Fiscal Year Ending June 30, 2014

TOTAL PENSION LIABILITY

Service cost	\$ 409,199,801
Interest	1,491,722,137
Benefit changes	-
Difference between actual & expected return	(105,344,633)
Assumption changes	-
Benefit payments	(1,153,051,607)
Refunds	<u>(28,718,256)</u>

NET CHANGE IN TOTAL PENSION LIABILITY 613,807,442

TOTAL PENSION LIABILITY - BEGINNING 19,032,811,749

TOTAL PENSION LIABILITY - ENDING (a) \$ 19,646,619,191

PLAN FIDUCIARY NET POSITION

Contributions- Employer/State	\$ 707,052,675
Contributions-Members	301,300,811
Net investment income	2,571,707,952
Benefit payments	(1,153,051,607)
Refunds	(28,718,256)
Administrative expense	(4,282,605)
Other	<u>-</u>

NET CHANGE IN PLAN FIDUCIARY NET POSITION 2,394,008,970

PLAN FIDUCIARY NET POSITION - BEGINNING 11,835,472,398

PLAN FIDUCIARY NET POSITION - ENDING (b) \$ 14,229,481,368

PLAN'S NET PENSION LIABILITY (ASSET) (a)-(b) \$ 5,417,137,823

See independent auditors' report.

SCHEDULE OF EMPLOYERS' NET PENSION LIABILITY (UNAUDITED)

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

Fiscal Year Ending June 30, 2014

Total pension liability	\$	19,646,619,191
Plan Fiduciary Net Position		<u>14,229,481,368</u>
Plan's Net Pension Liability	\$	<u>5,417,137,823</u>
Plan fiduciary net position as a percentage of the total pension liability		<u>72.43%</u>
Covered-employee payroll	\$	4,304,297,300
Plan's Net Pension Liability (Asset) as a percentage of covered-employee payroll		125.85%

See independent auditors' report.

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYERS
AND OTHER CONTRIBUTING ENTITIES (UNAUDITED)

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

	2014	2013	2012	2011	2010	2009	2008	2007	2006	2005
Actuarially determined contributions	\$ 602,936,966	\$ 619,805,640	588,287,377	822,419,996	742,286,289	714,367,558	590,495,652	575,745,142	535,228,038	722,095,783
Contributions in relation to the actuarially determined contribution:										
Employers (Schools)	386,895,127	373,789,020	376,635,234	364,025,589	366,282,238	338,974,512	308,804,479	271,012,403	241,174,959	227,791,719
State of Oklahoma, a non-employer contributing entity	320,157,548	327,505,309	304,995,663	274,452,205	254,375,139	279,672,051	288,036,554	264,904,170	218,294,582	177,966,919
Contribution deficiency (excess)	<u>\$ (104,115,709)</u>	<u>\$ (81,488,689)</u>	<u>\$ (93,343,520)</u>	<u>\$ 183,942,202</u>	<u>\$ 121,628,912</u>	<u>\$ 95,720,995</u>	<u>\$ (6,345,381)</u>	<u>\$ 39,828,569</u>	<u>\$ 75,758,497</u>	<u>\$ 316,337,145</u>
Covered-employee payroll	<u>\$ 4,304,297,300</u>	<u>\$ 3,933,100,000</u>	<u>\$ 3,924,800,000</u>	<u>\$ 3,773,300,000</u>	<u>\$ 3,854,800,000</u>	<u>\$ 3,807,900,000</u>	<u>\$ 3,751,400,000</u>	<u>\$ 3,598,900,000</u>	<u>\$ 3,354,900,000</u>	<u>\$ 3,175,200,000</u>
Contributions as a percentage of covered-employee payroll	<u>16.43%</u>	<u>17.83%</u>	<u>17.37%</u>	<u>16.92%</u>	<u>16.10%</u>	<u>16.25%</u>	<u>15.91%</u>	<u>14.89%</u>	<u>13.70%</u>	<u>12.78%</u>

NOTES TO SCHEDULE:

Actuarially determined contribution rates are calculated as of June 30.

Members and employers contribute based on statutorily fixed rates. The State of Oklahoma contributes 5.0% of revenues from sales taxes, use taxes, corporate and individual income taxes and lottery proceeds. An additional contribution is made for members whose salary is paid from federal funds or certain grant money.

Methods and assumptions used to determine contribution rates:

Actuarial cost method	Entry age normal
Amortization method	Level percentage of payroll
Amortization period	Amortization over an open 30-year period
Asset valuation method	5-year smooth market
Inflation	3.00%
Salary increase	Composed of 3.00% inflation, plus 1.00% productivity increase rate, plus step-rate promotional increases for members with less than 25 years of service
Investment rate of return	8.00%
Retirement age	Experience-based table of rates based on age, service and gender. Adopted by the Board in September 2010 in conjunction with the five year experience study for the period ending June 30, 2009
Mortality	RP-2000 Combined Mortality Table, projected to 2016 using Scale AA, multiplied by 90% for males and 80% for females

See independent auditors' report.

SCHEDULE OF INVESTMENT RETURNS (UNAUDITED)

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

Fiscal Year Ending June 30, 2014

Annual money-weighted rate of return, net of investment expenses	21.95%
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See independent auditors' report.

SCHEDULE OF INVESTMENT EXPENSES

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

For the Year Ended June 30, 2014

Investment managers		\$ 48,214,279
Investment consultants		<u>702,000</u>
	Total investment expenses	<u>\$ 48,916,279</u>

See independent auditors' report.

SCHEDULE OF ADMINISTRATIVE EXPENSES

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

For the Year Ended June 30, 2014

Salaries and benefits	\$ 2,736,103
General and miscellaneous	584,535
Professional/consultant fees	813,057
Travel and related expenses	69,519
Depreciation expense	<u>79,392</u>
Total administrative expenses	<u><u>\$ 4,282,605</u></u>

See independent auditors' report.

SCHEDULE OF PROFESSIONAL/CONSULTANT FEES

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

For the Year Ended June 30, 2014

Actuarial	\$	90,921
Medical		7,500
Legal		85,481
Audit		122,852
Data processing		231,387
Miscellaneous		<u>274,916</u>
Total professional/ consultant fees	\$	<u><u>813,057</u></u>

See 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

The Board of Trustees
Oklahoma Teachers' Retirement System

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Oklahoma Teachers' Retirement System (the System), a part of the financial reporting entity of the state of Oklahoma, which comprise the statement of fiduciary net position as of June 30, 2014, and the related statement of changes in fiduciary net position for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated November 10, 2014.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the System's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of reportable findings, we identified a deficiency in internal control that we consider to be a material weakness.

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 a 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. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in the accompanying schedule of reportable findings as Finding 2014-01 to be a material weakness.

System's Response to Findings

The System's response to the finding identified in our audit is described in the accompanying schedule of reportable findings. The System's response was not subjected to the auditing procedures applied in the audit of the financial statements, and, accordingly, we express no opinion on it.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's financial statements are free from 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*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Cole & Reed P.C.

Oklahoma City, Oklahoma
November 10, 2014

SCHEDULE OF REPORTABLE FINDINGS

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

Finding 2014-01

Criteria: The Plan should maintain a system of internal controls that ensures financial statements and footnote disclosures are accurately prepared in accordance with accounting principles generally accepted in the United States of America. Governmental Accounting Standards Board (GASB) Statement No. 67, *Financial Reporting for Pension Plans*, requires that the Plan disclose its net pension liability in the footnotes of the Plan's financial statements.

Condition: The Plan relies on an actuary to calculate the net pension liability as disclosed in the notes to the financial statements. As part of the actuarial valuation process, the Plan must provide the actuary with accurate and complete information about Plan participants. The Plan does not currently have sufficient internal controls to ensure that participant data provided to the actuary is accurate and complete.

Cause: The Plan recently implemented a new accounting system where participating employers upload participant data directly to the Plan's portal and there is no review to verify the information uploaded is accurate and complete. Also as part of the change, participant statements are no longer available for participant review to verify the correct information was provided to the Plan.

Effect and Potential Effect: The Plan's lack of internal control could cause the data sent to the actuary to be incomplete and inaccurate causing the net pension liability to be materially misstated.

Recommendation: We recommend that the Plan implement additional controls to help mitigate the risk that the data sent to the actuary might be materially misstated. The additional controls should ensure that participant and payroll information uploaded by the employers into the OTRS system is reviewed by plan participants and/or an employee at OTRS to verify its completeness and accuracy.

Plan Response: Oklahoma Teachers Retirement substantially agrees with this finding. Every multi-employer plan is heavily reliant on data submitted by its participating employers. OTRS cannot be a guarantor that it is 100% accurate. However, OTRS acknowledges that it needs a better system to make sure the data is as reliable as possible. OTRS will begin to collect data from participating employers on new employees for the FY-2015 fiscal year. This data will be checked against what the schools have sent through the online payroll reporting portal that was loaded into ALICE (OTRS' pension administration system). Exceptions will be investigated and corrected as needed. The OTRS Finance Department has asked the software developer of ALICE to modify a program to add a check box on the client screen so that reports can be run to indicate which employees still need to be verified. OTRS can begin doing this immediately.

SCHEDULE OF REPORTABLE FINDINGS--Continued

TEACHERS' RETIREMENT SYSTEM OF OKLAHOMA

June 30, 2014

Finding 2014-01--Continued

Plan Response--Continued: OTRS is working with its software developer to finish development of an online client portal for active and retired employees. We are assessing whether to wait for all client accounts to be audited or to go live with the new site with data that is good. OTRS will provide access on its portal to a personalized statement as recommended by the auditors. OTRS will encourage clients to review the information on these statements and report any discrepancies they find. It is anticipated that this will be completed by the end of fiscal year 2015.