STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS

JUNE 30, 1988 COMPONENT UNIT FINANCIAL REPORT

STATE EMPLOYEES'
RETIREMENT SYSTEM
OF ILLINOIS

2815 West Washington Street
P.O. Box 19255 Springfield, Illinois 62794 • 9255

Prepared by the
Accounting Division

Printed by Authority of the State of Illinois

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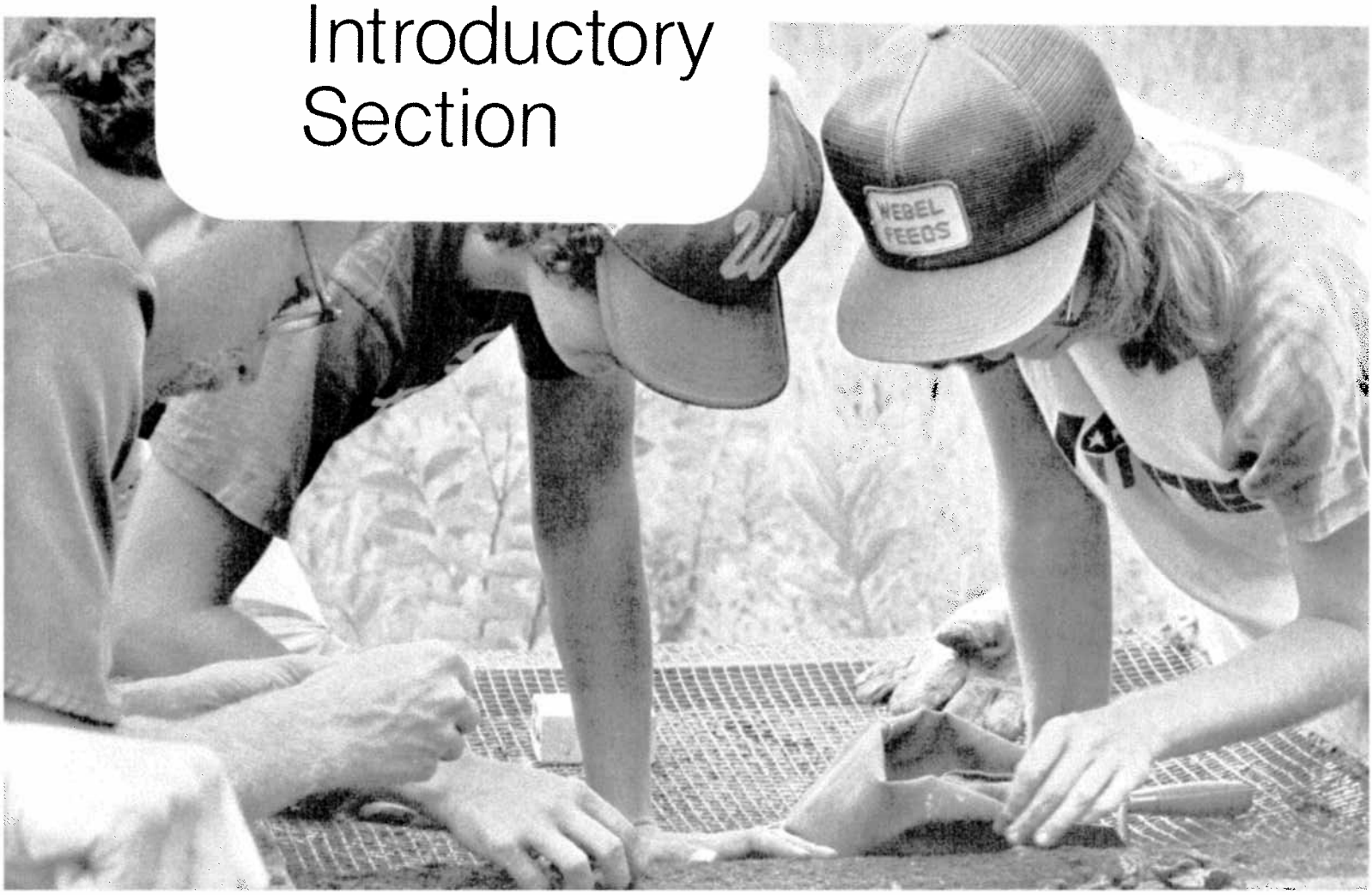
Introductory Section



STATE EMPLOYEES'
RETIREMENT SYSTEM
OF ILLINOIS

2815 WEST WASHINGTON, P.O. BOX 19255, SPRINGFIELD, IL 62794-9255, PH. 217/753-0444

The Board of Trustees
State Employees' Retirement System
of Illinois
Springfield, IL 62794

December 15, 1988

Dear Board Members:

The component unit annual financial report of the State Employees' Retirement System of Illinois for the fiscal year ended June 30, 1988 is hereby submitted. Responsibility for both the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with the System. To the best of our knowledge and belief, the enclosed data are accurate in all material respects and are reported in a manner designed to present fairly the financial position and results of operations of the various funds of the System. All disclosures necessary to enable the reader to gain an understanding of the System's financial activities have been included.

The report consists of six sections:

1. An Introductory Section which contains this letter of transmittal and the identification of the administrative organization;
2. The Financial Section which contains the report of the independent public accountants, the financial statements of the System, and the supplementary and additional financial information;
3. The Actuarial Section which contains the report of the Actuary as well as the summary of major actuarial assumptions and certain tables;
4. The Investment Section which contains a summary of the System's investment management approach and selected summary tables, including investment performance;
5. The Statistical Section which contains significant statistical data; and
6. A summary of the System's plan provisions.

The combined financial statements include the State Employees' Retirement System Trust Fund and the Social Security Contribution Fund, an Agency Fund. Based primarily upon the criteria of financial interdependency and ability to significantly influence operations and accountability for fiscal matters, the System has included the Social Security Contribution Fund in its combined financial statements.

REVENUES

Collection of employer and employee retirement contributions, as well as income from investments, provide the reserves necessary to finance retirement benefits. These income sources totaled $344.7 million during the fiscal year ending June 30, 1988, which is a significant decrease from revenue reported for fiscal year 1987, shown as follows:

Retirement System Trust Fund Contributions:	1988 (Millions)	1987 (Millions)	Increase/(Decrease) (Millions)	(Percentage)
Employees	$ 95.9	$ 90.1	$ 5.8	6.4%
Employers	100.0	109.6	(9.6)	(8.8%)
Investments	148.8	226.9	(78.1)	(34.4%)
	344.7	426.6	(81.9)	(19.2%)
Social Security Contribution Fund General Revenue, less balance lapsed	.1	.2	(.1)	(50.0%)
	$344.8	$426.8	$ (82.0)	(19.2%)

As indicated in the total above, a substantial portion of the total revenue is derived from investment income, including the realization of substantial gains on the sales of investments, during both fiscal years 1988 and 1987.

EXPENSES

The primary expense of a retirement system relates to the purpose for which it is created; namely the payment of benefits. The payments, together with the expense to administer the plan, constitute the total expenses of the System Trust Fund. Expenses of the System Trust Fund and Social Security Contribution Fund for 1988 and 1987 are shown for comparison purposes.

Retirement System Trust Fund	1988 (Millions)	1987 (Millions)	Increase/(Decrease) (Millions)	(Percentage)
Benefits:				
Retirement annuities	$132.2	$119.8	$12.4	10.4%
Survivors' annuities	20.3	18.9	1.4	7.4%
Disability benefits	14.7	14.5	.2	1.4%
Lump-sum death benefits	6.4	6.4	-	- %
	173.6	159.6	14.0	8.8%
Refunds	12.0	12.2	(.2)	(1.6)%
Administrative expenses	3.2	3.0	.2	6.7%
	$188.8	$174.8	$14.0	8.0%
Social Security Contribution Fund Administrative expenses	.1	.2	(.1)	(50.0)%
	$188.9	$175.0	$13.9	7.9%

The increase in benefit payment resulted primarily from a growth in the number of benefits paid and in the average benefit payment.

INVESTMENTS

Income from investments has, over the years, increasingly become a greater share of the total revenue of the System. Net investment income, combined with a net realized gain on the sale of investments, amounts to $148,802,057 during fiscal year 1988, a decrease of $78,127,546 from fiscal year 1987. This reflects the generally downward trend in the financial markets during the last fiscal year. Income from investments represents 43.2% of total fund revenue.

FUNDING AND RESERVES

Funding is the process of specifically allocating monies for current and future use. Proper funding includes an actuarial review of the fund balances to ensure that funds will be available for current and future benefit payments.

The actuarial determined liability of the System at June 30, 1988, amounted to $3.642 billion. The fund balances for participant contributions, interest accumulations and other future benefits amounted to $2.382 billion as of the same date. The amount by which the liability exceeds the reserves is called the "unfunded accrued benefit cost". The unfunded accrued benefit cost amounts to $1.260 billion and reflects the continuing state policy of appropriating funds based upon a percentage of the total amount of benefit payments made to current recipients. A detailed discussion of funding is provided in the Actuarial Section of this report.

ECONOMIC CONDITION AND OUTLOOK

The state's policy on pension funding has been based on variations of the pay-as-you-go approach. From fiscal year 1973 through fiscal year 1981, the state's contribution was approximately equal to 100% of payout (the dollar amount expected to be paid out in benefits each year).

Beginning in fiscal year 1982, however, state appropriations have been less than 100% of payout. In fiscal year 1982, the appropriation fell to 62.5% of payout, while in fiscal year 1983 the appropriation declined to just over 50% of payout. These reductions were due in large part to the state's poor fiscal condition. From fiscal year 1984 to fiscal year 1987, the state's appropriation was approximately 60% of payout. The fiscal year 1988 regular contribution was approximately 48% of payout.

Financing the retirement benefits that are being earned is one of the most important issues facing the State Employees' Retirement System. Over the years, a number of organizations have stressed the need for sound funding of the System. However, before funding needs can be discussed, attention must first be focused on the current financial condition of the System.

Assessing the financial status of any retirement system is a difficult task. The valuation of pension liabilities is a complex procedure requiring the application of actuarial techniques. It is not possible

to provide a simple measure of the financial status of a retirement system because no universally accepted measure of the financial status presently exists. By any reasonable actuarial standard, however, the System's present financial condition must be described as precarious due to the continually increasing dollar level of the unfunded liability. The current economic outlook for the State of Illinois as a whole does not allow us to assume that additional resources will be available under existing tax structures to allocate toward retirement funding. The events in the financial markets, especially the stock market during the past fiscal year, serve as a constant reminder of the fact that no source of revenue can be guaranteed and that the ultimate responsibility for a sound funding policy and the related liability for contributions rests ultimately with the State of Illinois.

MAJOR INITIATIVES for the System are detailed in the Report of the Chairman of the Board of Trustees.

ACCOUNTING SYSTEM AND INTERNAL CONTROL

This report has been prepared to conform with the principles of governmental accounting and reporting pronounced by the Governmental Accounting Standards Board and the American Institute of Certified Public Accountants. The accrual basis of accounting is used to record the assets, liabilities, revenues and expenses of the State Employees' Retirement Trust Fund. Revenues are recognized in the accounting period in which they are earned, without regard to the date of collection, and expenses are recorded when the corresponding liabilities are incurred, regardless of when payment is made. The administrative expenses of the Social Security Contribution Fund are appropriated annually by the Illinois State Legislature and included in the financial statements of the System's Trust Fund. The Contribution Fund uses the modified accrual basis of accounting. The State Employees' Retirement System also uses the State of Illinois, Comptroller's Uniform Statewide Accounting System (CUSAS) as a basis for the preparation of the financial statements. In developing the System's accounting system, consideration is given to the adequacy of internal accounting controls. These controls are designed to provide reasonable assurance regarding the safekeeping of assets and the reliability of financial records. Constant effort is directed by the System at improving this level to assure the participants of a financially sound retirement system.

PROFESSIONAL SERVICES

Independent consultants are retained by the Board of Trustees to perform professional services that are essential to the effective and efficient operations of the System. Actuarial services are provided by The Wyatt Company, Chicago, Illinois. The annual financial audit of the System was conducted by the accounting firm of Arthur Andersen & Company under the direction of the Auditor General of the State of Illinois. In addition to the annual financial audit, a two year compliance audit was also performed by the auditors. The purpose of the compliance audit was to determine whether the State Employees' Retirement System obligated, expended, received and used public funds of the state in accordance with the purpose for which such funds have been authorized by law. The System's investment function is managed by the Illinois State Board of Investment.

REPORTING ACHIEVEMENT

The Government Finance Officers Association (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the State Employees' Retirement System of Illinois for its component unit financial report for the fiscal year ended June 30, 1987. This was the second consecutive year that the System has received this prestigious award. In order to be awarded this certificate, a governmental unit must publish an easily readable and efficiently organized component unit financial report, in which the contents conform to program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements. A certificate of achievement is valid for a period of one year only. We believe our current report continues to conform to the Certificate of Achievement Program's requirements, and we are submitting it to the GFOA to determine its eligibilty for another certificate.

ACKNOWLEDGEMENTS

The preparation of this report reflects the combined efforts of the System's staff under the direction of the Retirement Board. It is intended to provide complete and reliable information as a basis for making management decisions as a means of determining compliance with legal provisions, and as a means for determining responsible stewardship for the assets contributed to the members in the State of Illinois.

On behalf of the Board of Trustees we would like to express our appreciation to the staff and professional consultants who worked so effectively to assure the successful operation of the System.

Respectfully submitted,

Michael L. Mory
Executive Secretary

Nicholas C. Merrill, Jr.
Chief Fiscal Officer

STATE EMPLOYEES'
RETIREMENT SYSTEM
OF ILLINOIS

December 15, 1988

To All Members, — State Employees' Retirement System of Illinois:

It is with mixed feelings that I report on the progress that was made during the spring session of the General Assembly to address long-term actuarial funding of the Retirement System. Senate Bill 1470 was passed which provided for funding of the System on an actuarial basis. The unfunded liability as of June 30, 1988 is $1.260 billion. The bill mandated that this be funded over a period of 40 years as a level percentage of active payroll. It is interesting to note that this legislation received almost unanimous approval from both houses. Efforts to secure funding for the new legislation through implementation of an increase in the state income tax were unsuccessful leaving no practical way to meet the mandate of the legislation during fiscal year 1989. Based on a failure to be able to fund the new legislation, the possibilities of a gubernatorial veto appeared likely. Fortunately, the Governor took a slightly different tack by exercising his amendatory veto power to postpone the implementation date to FY-90. To our disappointment; however, the amendatory veto was not accepted by the General Assembly during the fall 1988 veto session.

Failure to secure passage of a tax increase also eliminated any possibility of securing the benefit improvements endorsed by the System, such as increasing the basic pension formula and compounding the 3% cost of living allowance. It is unfortunate that the new funding legislation was considered based solely on the current benefit structure. We believe, based on comparison studies done with surrounding states, that the System's benefit proposals are totally justified. It must be recognized that without additional revenues, these improvements will not become a reality.

Although unimpressive in an absolute sense, the total rate of return on System investments for FY-88 was a positive 2.5%. In view of events which took place in the financial markets during October 1987, the end result is favorable on a comparative basis. The Illinois State Board of Investment invests nearly $2.4 billion for the System using the "prudent person rule". This means that they are required to make investments that they believe would provide a fair return over a long period of time based upon the degree of risk incurred. This requirement is met through diversification of the investment portfolio as opposed to attempting to time favorable market sectors. As a result, during October 1987, the System was not involved in the massive sell-off which further depressed market values. While it is hoped that we will not see a repeat of this turbulent condition in the financial markets, it certainly did provide a reminder that, over the long run we cannot expect to make up for inadequate employer contributions through excess investment returns.

Another area of continuing concern involves the ever increasing number of mandates which flow from the federal government. The most current example is the requirement that retirement benefits be paid to active employees in the year following attainment of age 70½. While this change came about as a result of perceived abuses of the federal tax laws, it mandates a situation which has always been considered improper for governmental employees, i.e. receiving salary and a pension at the same time. This point notwithstanding, our ability to comply with these mandates is severely restricted since any change to the Retirement Plan requires approval of legislation by the General Assembly. During this past year, a proposal was offered to allow the state-financed retirement systems to comply with federal mandates on an administrative basis. This proposal was not approved as it was thought to be an improper delegation of legislative authority. While we can appreciate the concern, this or similar authority should be considered in the future to prevent the assessment of penalties by the federal government against the System or its members due to compliance failures.

During March of this year, the System's Board of Trustees took initial action to approve the construction of a permanent office facility for the Retirement System. Since its inception in 1944, the System has rented office space in several locations. For the past nine years we have leased space from the

Teachers' Retirement System. With rental costs continually increasing, currently exceeding $200,000 per year, the Board has determined that leasing is not a cost effective option in the future. The new facility, which will be constructed in Springfield at the intersections of Greenbriar Boulevard and Veterans Parkway, is designed to meet the needs of the System for at least the next 30 years. Long-term savings from the project considering other investment alternatives, are expected to exceed $1.7 million.

During the past fiscal year several projects were initiated to provide more timely and accurate services for the System's membership. These projects included the development of an overall disaster plan for the Retirement System, including offsite storage and a backup data processing facility, and the development of a video tape program by the Field Services Division for presentation during benefit seminars. The video tape provides a broad perspective of the benefits available to the membership and is part of the ongoing goal to provide more education and assistance to the membership and beneficiaries of the System. On a continuing basis, each division within the System has worked towards a more automated and streamlined operating system through the use of computers while still providing personal service to members. Projects for Fiscal Year 1989 include a review of the existing employer contribution system, establishment of a data base for Field Services personnel, continued emphasis on the automation of internal reports and the location of members who are currently in an inactive account status.

While not all of our goals and objectives were met during the past fiscal year, significant accomplishments did occur. I believe that with the active support of the membership, this momentum can be maintained or even accelerated in the future. At the close of this very eventful fiscal year, I wish to thank the other members of the Board and staff for their dedication and service to the members and beneficiaries of the State Employees' Retirement System.

Respectfully submitted,

Kenneth W. Obrecht
Chairman

BOARD OF TRUSTEES

Seated, left to right, **DORIS M. CLARK,** Elected Annuitant — **KENNETH OBRECHT,** Chairman, Appointed by the Governor — **ALICE KIRBY,** Representing Roland W. Burris, Comptroller — Standing — **MICHAEL L. MORY,** Executive Secretary — **WILLIAM LEDBETTER,** Representing Robert L. Mandeville, Director, Bureau of the Budget — **JOSEPH T. PISANO,** State Employee, Appointed by the Governor — **DENNIS PATRICK,** Elected State Employee — **J. WAYNE CHAMBERS,** Annuitant, Appointed by the Governor.

ADMINISTRATIVE STAFF

MICHAEL L. MORY
Executive Secretary

ROBERT V. KNOX
Associate Executive Secretary

TERRY E. RADLIFF
Internal Auditor

BARBARA BAIRD
Manager, Chicago Division

MICHAEL K. BLANKENSHIP
Manager, Social Security Division

PATRICK P. CUMMINGS
Manager, Claims Division

DWIGHT N. GARMON
Manager, Data Processing Division

JOSEPH S. MAGGIO
Manager, Service and Refunds Division

NICHOLAS C. MERRILL, JR.
Manager, Accounting Division

WILLIAM T. WEIR
Manager, Administrative Services Division

Certificate of Achievement for Excellence in Financial Reporting

Presented to

State Employees' Retirement System of Illinois

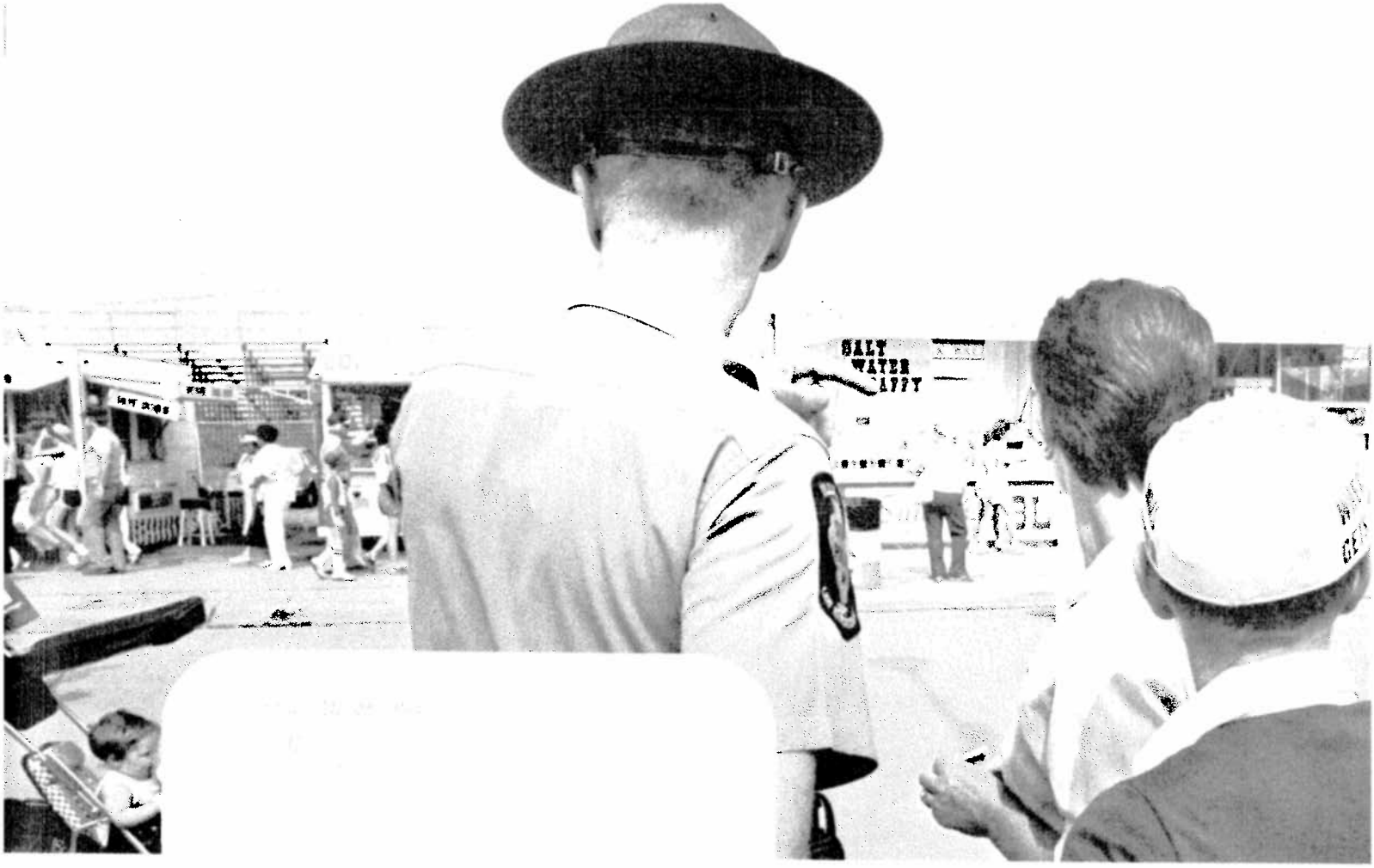
For its Comprehensive Annual Financial Report for the Fiscal Year Ended

June 30, 1987

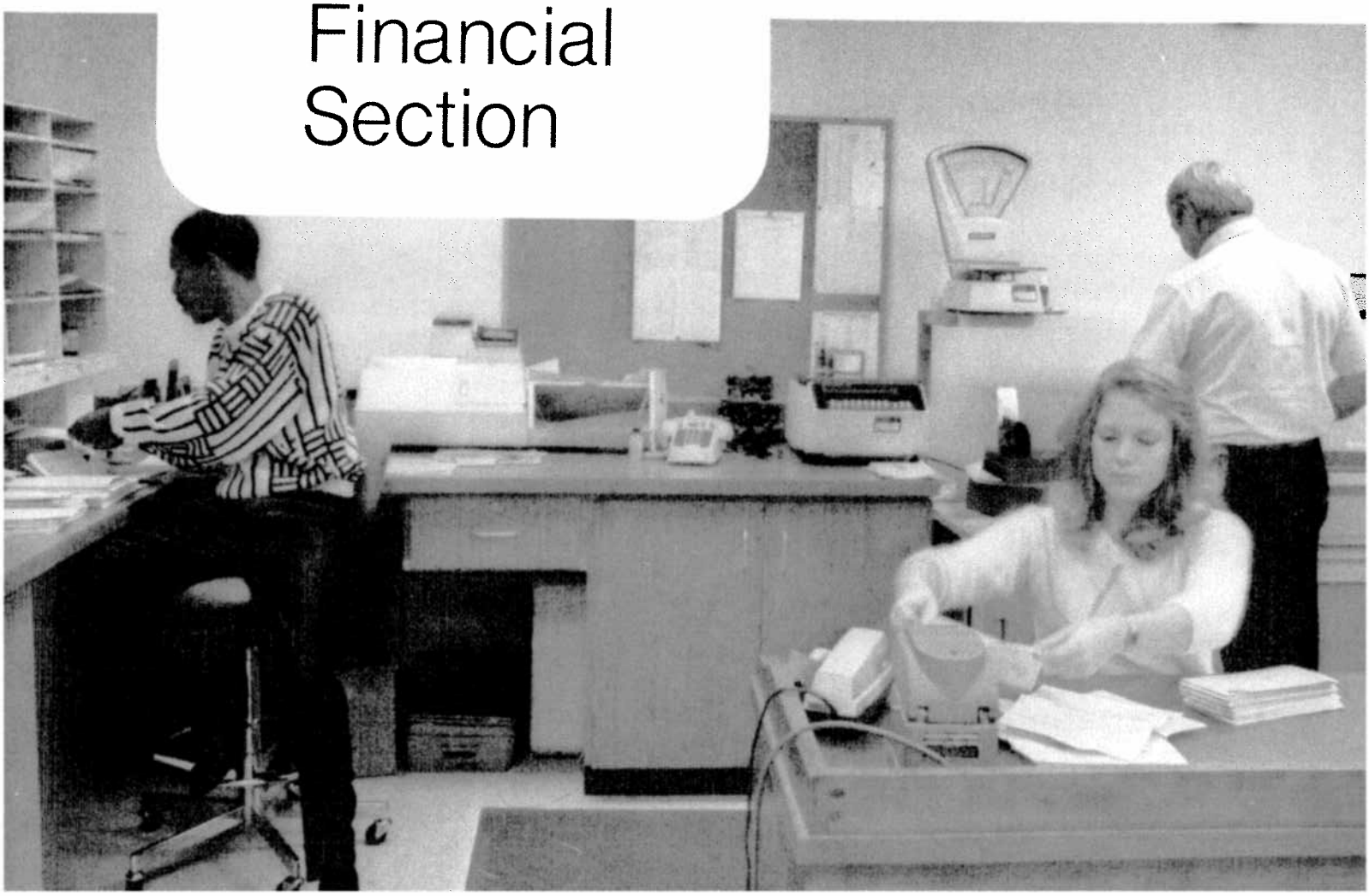
A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.

President

Executive Director



Financial Section



ARTHUR ANDERSEN & CO.

CHICAGO, ILLINOIS

Honorable Robert G. Cronson
Auditor General
State of Illinois

Board of Trustees
State Employees' Retirement
System of Illinois

We have examined the financial statements of the STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS as of and for the years ended June 30, 1988 and 1987, as listed in the table of contents. Our examinations were made in accordance with generally accepted auditing standards and the standards for financial audits contained in the U.S. General Accounting Office's Standards for Audits of Governmental Organizations, Programs, Activities and Functions and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of the State Employees' Retirement System of Illinois as of June 30, 1988 and 1987, and the results of its operations and the changes in its financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Our examinations were made for the purpose of forming an opinion on the financial statements taken as a whole. The statements of supplementary financial information listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements of the State Employees' Retirement System of Illinois. The supplementary financial information has been subjected to the auditing procedures applied in our examinations of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

Arthur Andersen & Co.

ARTHUR ANDERSEN & CO.

October 14, 1988

STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS

Combined Balance Sheets • June 30, 1988 and 1987

	1988	1987
Assets		
Cash	$ 9,893,839	$ 5,977,771
Cash, restricted for Social Security remittances	2,252,064	4,334,906
Receivables:		
Contributions receivable:		
Participants	3,937,685	4,506,275
Employing state agencies	2,454,280	5,269,062
Other accounts receivable	539,128	414,451
	$ 6,931,093	$ 10,189,788
Investments - held in the Illinois State Board of Investment Commingled Fund at cost (Market value: 1988, $2,485,230,297 1987, $2,416,626,806) (Note 4)	2,367,063,722	2,211,906,317
Property and equipment, net of accumulated depreciation (Notes 9 and 12)	823,484	168,785
Total Assets	$2,386,964,202	$2,232,577,567
Liabilities and Fund Balance		
Benefits payable	$ 1,476,752	$ 1,144,997
Refunds payable	375,069	223,318
Administrative expenses payable (Note 8)	409,660	411,370
Participants' deferred service credit accounts	644,591	579,830
Unremitted Social Security contributions	1,822,858	4,037,829
Amounts held for Social Security remittances	429,206	297,077
Total Liabilities	$ 5,158,136	$ 6,694,421
Fund Balance		
Actuarially determined accrued benefit cost (Notes 6 and 14)	3,641,579,030	3,361,722,501
Less unfunded accrued benefit cost representing an obligation of the State of Illinois	1,259,772,964	1,135,839,355
Total Fund Balance (Note 13)	$ 2,381,806,066	$ 2,225,883,146
Total Liabilities and Fund Balance	$2,386,964,202	$2,232,577,567

See accompanying notes to financial statements.

STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS

State Employees' Retirement System Trust Fund
Statements of Revenue, Expenses and Changes in Fund Balance
Years ended June 30, 1988 and 1987

	1988	1987
Revenue:		
Contributions:		
Participants	$ 95,928,239	$ 90,096,279
Employing State agencies and appropriations	99,990,922	109,559,940
Total Contributions revenue	195,919,161	199,656,219
Investments:		
Net investments income	132,301,594	119,922,351
Interest earned on cash balances	644,652	725,599
Net realized gain on sale of investments	15,855,811	106,281,653
Total Investments revenue	148,802,057	226,929,603
	344,721,218	426,585,822
General Revenue Fund appropriations, less balances lapsed	127,288	168,326
Total Revenue	344,848,506	426,754,148
Expenses:		
Benefits:		
Retirement annuities	132,265,411	119,758,023
Survivors' annuities	20,319,659	18,955,079
Disability benefits	14,660,199	14,521,296
Lump-sum death benefits	6,399,280	6,379,930
	173,644,549	159,614,328
Refunds	11,983,814	12,177,841
Administrative expense, System Trust Fund (Note 8)	3,169,935	3,000,932
Transfers to reciprocating retirement systems	-	4,258
	188,798,298	174,797,359
Administrative expense, Contribution Fund (Note 8)	127,288	168,326
Total Expenses	188,925,586	174,965,685
Excess of revenue over expenses	$ 155,922,920	$ 251,788,463
Fund Balance at beginning of year	2,225,883,146	1,974,094,683
Fund Balance at end of year	$ 2,381,806,066	$ 2,225,883,146

See accompanying notes to financial statements.

STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS

State Employees' Retirement System Trust Fund
Statements of Changes in Financial Position
Years ended June 30, 1988 and 1987

	1988	1987
Sources of working capital:		
Working capital provided by operations — excess of revenue over expenses	$ 155,922,920	$ 251,788,463
Add (Deduct) items not providing working capital —		
net realized (gain) on sale of investments	(15,855,811)	(106,281,653)
reinvested earnings	(132,301,594)	(119,922,351)
Depreciation expense	51,354	35,657
Other	7,070	4,923
Total sources of working capital	7,823,939	25,625,039
Uses of working capital:		
Amounts transmitted by SERS for investment purchases (net)	7,000,000	26,000,000
Additions to fixed assets	713,123	84,449
Total uses of working capital	7,713,123	26,084,449
Net (decrease) in working capital	$ 110,816	$ (459,410)
Elements of net (decrease) in working capital:		
Cash	$ 3,916,068	$ (1,641,038)
Receivables	(3,258,695)	1,258,171
Benefits payable	(331,755)	174,497
Refunds payable	(151,751)	(85,030)
Administrative expenses payable	1,710	(33,055)
Participants' deferred service credit accounts	(64,761)	(132,955)
Net increase (decrease) in working capital	$ 110,816	(459,410)

See accompanying notes to financial statements.

STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS

Notes to Financial Statements — June 30, 1988 and 1987

(1)Reporting Entity

The State Employees' Retirement System of Illinois (System) is a component unit of the State of Illinois and is composed of the State Employees' Retirement System, a trust fund (System Trust Fund) and the Social Security Contribution Fund, an agency fund (Contribution Fund). The System Trust Fund and the Contribution Fund are considered part of the State of Illinois financial reporting entity and are included in the state's comprehensive annual financial report as a pension trust fund and an agency fund, respectively.

The System has developed criteria to determine whether other state agencies, boards or commissions which benefit the members of the System should be included within its financial reporting entity. The criteria include, but are not limited to, whether the System exercises oversight responsibility on financial interdependency, selection of governing authority, designation of management, ability to significantly influence operations and accountability for fiscal matters, scope of public service and special financing relationships.

Based primarily upon the criteria of financial interdependency and ability to significantly influence operations and accountability for fiscal matters, the System has included the Social Security Contribution Fund in its combined financial statements.

(2)Plan Description

The System is the administrator of single-employer public employee retirement system (PERS) established and administered by the State of Illinois to provide pension benefits for its employees. At June 30, 1988 and 1987, the number of participating state agencies, boards and commissions totalled:

	1988	1987
State agencies	42	42
State boards and commissions	46	45
Total	88	87

At June 30, 1988 and 1987, the System Trust Fund membership consisted of:

	1988	1987
Retirees and beneficiaries currently receiving benefits:		
Retirement annuities	23,038	22,529
Survivors' annuities	8,296	8,015
Disability benefits	1,536	1,577
	32,870	32,121
Inactive employees entitled to benefits but not yet receiving them	2,262	2,129
Total	35,132	34,250
Current Employees:		
Vested:		
Coordinated with Social Security	34,901	32,567
Noncoordinated	8,652	9,185
Nonvested:		
Coordinated with Social Security	30,236	31,997
Noncoordinated	1,134	983
Total	74,923	74,732

Operation of the System Trust Fund and the direction of its policies are the responsibility of the Board of Trustees of the System.

(a) Eligibility and Membership

Membership is automatic for most state employees who are not eligible for another state-sponsored retirement plan. All persons entering state service, except those in positions subject to membership in other state sponsored retirement systems, persons employed after June 30, 1979 as public service employment program participants under the Federal CETA program, and enrollees in the Illinois Young Adult Conservation Corps, become members of the System upon completion of six months service. Employees appointed by the Governor and requiring confirmation by the State of Illinois Senate may elect to become members of the System Trust Fund.

(b) Contributions

Participating members contribute specified percentages of their salaries for retirement annuities and survivors' annuities. Contributions are excluded from gross income for Federal and State income tax purposes. The total contribution rate is 4% if the member is coordinated with Social Security and 8% if the member is not coordinated. Certain employment categories which are eligible for benefits under alternative formulas contribute at the rate of 5½% or 9½% depending upon whether or not the employee is coordinated with Social Security. Participants' contributions are fully refundable, without interest, upon withdrawal from state employment. The State of Illinois is obligated to make payment for the required departmental contributions, all allowances, annuities, any benefits granted under Article 14 of the Illinois Pension Code (Code) and all administrative expenses of the System Trust Fund to the extent specified in the Code.

(c) Benefits

The System is governed by Article 14 of the Code. Vesting and benefit provisions under the System Trust Fund are defined in the Code. Employees who retire at or after age 60 with 8 years of credited service (or at age 55 with at least 30 years of credited service with reduced benefits) are entitled to an annual retirement benefit, payable monthly for life, in an amount based upon final average compensation and credited service. Employees with 35 years of credited service may retire at any age with full benefits. Final average compensation for retirement and survivor annuities, is the employee's average salary, during a 48 consecutive month period within the last 120 months of service in which the total compensation was the highest.

Occupational and nonoccupational (including temporary) disability benefits are available through the System Trust Fund. To be eligible for nonoccupational (including temporary) disability benefits, an employee must have at least eighteen months of credited service with the System Trust Fund and be less than seventy years old. The nonoccupational (including temporary) disability benefit is equal to 50% of the monthly rate of compensation of the employee on the date of removal from the payroll. Occupational disability benefits are provided from the date of employment provided that the member is under age 70 and becomes disabled as a direct result of injuries or diseases arising out of and in the course of state employment. The monthly benefit is equal to 75% of the monthly rate of compensation on the date of removal from the payroll. This benefit amount is reduced by Workers' Compensation or payments under the Occupational Diseases Act.

Occupational and nonoccupational death benefits are also available through the System Trust Fund. Certain nonoccupational death benefits vest after eighteen months of credited service. Occupational death benefits are provided from the date of employment.

(3) Description of the Contribution Fund

The Contribution Fund was established pursuant to the 1951 Social Security Enabling Act, Article 21 of the Illinois Pension Code. It is a special fund in the State Treasury which serves as a clearinghouse account for the collection and transmittal of federal Social Security contributions of participating state employees and employing agencies and political subdivisions.

Effective January 1, 1987, the responsibility for the collection and transmittal of Social Security contributions for state agencies and participating state employees was transferred from the System to the Office of the Comptroller of the State of Illinois. As of that same date, political subdivisions of the state became responsible for their own remittance of Social Security contributions to the federal government. The balances in this fund are being maintained for final settlement of open years.

(4) Summary of Significant Accounting Policies and Plan Asset Matters

(a) Basis of Accounting — System Trust Fund

The financial transactions of the System Trust Fund are recorded on the accrual basis of accounting and

in conformity with generally accepted accounting principles. Employee and employer contributions are recognized as revenues in the period in which employee services are performed.

The System Trust Fund also recognizes revenue representing supplemental state funding on an accrual basis. This funding is the result of reduced appropriations to the System for the year ended June 30, 1983. The amount of the reduction in that period amounted to $11,000,000. The state has agreed to repay the under appropriation and interest at the rate of six percent over the succeeding five fiscal years. The System has not recorded the unpaid amounts as an asset because repayment in any given year is subject to state appropriation of funds, which is subject to numerous conditions. Consequently, repayment of principal and interest are recognized in the current year once the legislature has approved an amount to be provided to the System Trust Fund. Final payment of the under funding is recognized as revenue in the FY-88 financial statements.

(b) Method Used to Value Investments

The System Trust Fund retains all of its available cash in a commingled investment pool managed by the Treasurer of the State of Illinois. "Available cash" is determined to be that amount which is required for the current operating expenditures of the System Trust Fund. The excess of available cash is tranferred to the Illinois State Board of Investment (ISBI) for purposes of long-term investment for the System Trust Fund.

Investments are managed by the ISBI pursuant to Article 22A of the Illinois Pension Code and are maintained in the ISBI Commingled Fund. Such investments are valued at the cost of the System Trust Fund's units of participation in the ISBI Commingled Fund. Units of the ISBI Commingled Fund are issued to the member systems on the last day of the month based on the unit net asset value calculated as of that date. Net investment income of the ISBI Commingled Fund is allocated to each of the member systems on the last day of the month on the basis of percentage of accumulated units owned by the respective systems. Management expenses are deducted monthly from income before distribution. Investment income is recognized when earned.

The investment authority of the ISBI is provided in Illinois Revised Statutes Chapter 108-½, Article 22A-112. The ISBI investment authority includes investments in obligations of the U.S. Treasury and other agencies, notes secured by mortgages which are insured by the Federal Housing Commission, real estate, common and preferred stocks, convertible debt securities, deposits or certificates of deposit of federally insured institutions and options. Such investment authority requires that all opportunities be undertaken with care, skill, prudence and diligence given prevailing circumstances that a prudent person acting in like capacity and experience would undertake.

Governmental Accounting Standards Board (GASB) Statement No. 3 entitled "Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements" requires certain financial statement disclosure of deposits and investments, such as the disclosure of carrying amounts by type of investment and classification into one of three categories based upon credit risk. Investments in pools managed by other governmental agencies, in general, are to be disclosed but not categorized because they are not evidenced by securities that exist in physical or book entry form.

The System Trust Fund transfers money to the ISBI for investment in the ISBI Commingled Fund. This money is then allocated among various investment managers to pursue a specific investment strategy. All investment transactions are initiated by the investment managers (either internal or external). The transaction settlement information is then forwarded to the agent bank's trust department under a master custodial agreement.

Custody of a majority of the actual physical securities is maintained at an agent of the agent bank's trust department using a book-entry system.

The agent of the master custodian is Depository Trust Company.

Listed below are the ISBI investments, as categorized in the ISBI annual financial report. They are categorized to indicate the level of risk assumed by the ISBI Board at year end. Category I includes investments that are insured or registered or for which the securities are held by the master custodian in the ISBI Board's name. Category II includes uninsured and unregistered investments for which the securities are held by the master custodian in the ISBI Board's name. Category III includes uninsured and unregistered investments for which the securities are held by an agent of the master custodian but not in the ISBI Board's name.

	Category I	Category II	Category III	Cost	Market Value
U.S. Government Obligations	$ 411,054,807			$ 411,054,807	$ 411,234,177
Foreign Obligations	31,214,160			31,214,160	33,028,684
Corporate Obligations	531,505,863			531,505,863	561,764,077
Convertible Bonds	91,002,948			91,002,948	94,705,344
Common Stock & Equity Fund	999,762,798			999,762,798	1,039,298,771
Convertible Preferred Stock	23,568,459			23,568,459	25,366,870
Preferred Stock	5,750,632			5,750,632	3,151,793
Money Market Instruments	161,880,525		$ 2,003,291	163,883,816	163,883,816
Real Estate Pooled Funds*				203,744,767	252,832,386
Venture Capital*				54,635,248	57,642,361
	$2,255,740,192	$ 0	$ 2,003,291	$2,516,123,498	$2,642,908,279

*Not classified by category since investments are not securities as defined.

The ISBI Board participates in a securites lending program whereby securities are loaned to brokers and, in return, the ISBI Board received collateral of amounts slightly in excess of the market value of securities loaned. Collateral consists solely of cash, letters of credit and commercial paper. As of June 30, 1988 and 1987, the ISBI Board had outstanding loaned investment securities having a market value of approximately $181,214,000 and $225,500,000, respectively, against which it had received collateral of approximately $188,263,000 and $230,468,000, respectively.

The System Trust Fund owns 93.1% of the ISBI Commingled Fund as of June 30, 1988.

(c) Fixed Assets

Expenditures for fixed assets are capitalized and depreciated over their estimated useful lives.

(d) Actuarial Experience Review

In accordance with Illinois Revised Statutes, an actuarial experience review is to be performed at least once every five years to determine the adequacy of actuarial assumptions regarding the mortality, retirement, disability, employment, turnover, interest and earnable compensation of the members and beneficiaries of the System. An experience review was performed as of June 30, 1985.

(e) Administrative Expenses

Expenses related to the administration of the System Trust Fund are budgeted and approved by the System's Board of Trustees. Administrative expenses for the Contribution Fund are appropriated annually by the State Legislature and are included in the financial statements of the System Trust Fund.

(f) Basis of Accounting — Contribution Fund

The collection and transmittal of federal Social Security contributions of participating state employees, employing agencies and political subdivisions through December 31, 1986, have been accounted for within the Contribution Fund on a modified accrual basis.

(5) Funding Status and Progress

The amount shown below as "pension benefit obligation" is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases, estimated to be payable in the future as a result of employee service to date. The measure is the actuarial present value of credited

projected benefits and is intended to help users assess the State Employees' Retirement System funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among PERS.

The measure is independent of the funding method used to determine contributions to the System Trust Fund, discussed in Note 6 below.

The pension benefit obligation was determined as part of an actuarial valuation at June 30, 1988. Significant actuarial assumptions used include (a) a rate of return on the investment of present and future assets of 8 percent per year compounded annually, (b) projected salary increase of 6½ percent per year compounded annually, attributable to inflation, (c) 85% of employees are presumed to be married, (d) the female spouse is assumed to be three years younger than the male spouse, (e) mortality rates are based upon the 1971 Group Annuity Mortality Table projected in 1986, (f) it is assumed that terminated employees will not be rehired, and (g) the rate of turnover without vested benefits assumes a high scale at younger age levels, becoming progressively lower as age advances.

At June 30, 1988 and 1987, the unfunded pension benefit obligation was $1,108,849,603 and $1,078,362,325 as follows:

	1988	1987
Pension benefit obligation:		
Retirees & beneficiaries currently receiving benefits	$ 1,546,828,161	$1,445,207,627
Terminated employees not yet receiving benefits	14,605,254	16,999,775
Current Employees:		
Accumulated employee contributions	947,077,130	859,782,136
Employer-financed vested	886,198,521	888,252,004
Employer-financed nonvested	50,132,422	52,828,986
Inactive members — Accumulated contributions	45,814,181	41,174,943
Total Pension benefit obligation	$3,490,655,669	$3,304,245,471
Net assets available for benefits, at cost	2,381,806,066	2,225,883,146
(market value at June 30, 1988 $2,499,972,641; 1987 $2,430,603,635)		
Unfunded pension benefit obligation	*$ 1,108,849,603	*$1,078,362,325

*The unfunded accrued benefit cost representing an obligation of the State of Illinois shown on the combined balance sheet has been determined on the actuarial basis of entry age normal described in note 6.

As a result of the passage of H.B. 2630, which provided for ad hoc benefit increases for annuitants and the granting of credit for unused sick leave to employees who defer retirement, there was an increase in the actuarial present value of credited projected benefits of $601,673.

(6) Contributions Required and Contributions Made

On an annual basis, a valuation of the liabilities and reserves of the System Trust Fund is performed by the System's actuarial consultants in order to determine the amount of contributions required from the State of Illinois.

The principal actuarial funding method used by the System Trust Fund is entry age normal. In addition, the actuarial consultants also submit to the System's Board of Trustees (Board) several alternative cost methods with various amortization periods for the unfunded prior costs. Each of these alternatives are considered an acceptable cost or funding method. These alternatives are presented to the Board as a result of the state's long standing funding policy described below. Employer contributions are expressed as a percentage of annual covered payroll. The Board evaluates the alternatives and certifies a contribution rate within the range of alternatives. This rate is then used as the "actuarial required contribution" rate. For fiscal years 1988 and 1987, the Board certified actuarial required contribution rates were 7.24% and 8.4%, respectively.

The Illinois State Legislature has followed a funding policy of appropriating funds based upon a percentage of benefit payout for those agencies which receive appropriated monies. The appropriated employer contribution rate for the legislatively funded agencies was 4.8% for fiscal year 1988 and 5.6% for fiscal year 1987.

State agencies which do not receive state appropriated funds for their share of employer retirement contributions contribute at the Board certified rate.

It has been interpreted that the laws of the State of Illinois regarding state finance provide for the Governor and the state legislature to have specific authority to reduce or increase monies appropriated for the employer share of retirement contributions regardless of the rate certified by the Board of Trustees.

Based upon the Board certified rate of 7.24%, the total amount of employer contributions required for the fiscal year ended June 30, 1988 amounted to $141,466,704. The total amount of employer contributions made was $99,990,922, thereby resulting in an underfunding of $41,475,782.

Schedule of Contributions Required and Contributions Made
(in thousands)

	1988	1987	1986	1985	1984
Covered Payroll	$ 1,953,960	$ 1,825,196	$ 1,713,755	$ 1,569,532	$ 1,437,546
Employer Contributions	99,991	109,560	102,214	94,457	86,464
Actual Employer Contribution %	5.12%	6.00%	5.96%	6.01%	6.01%
Board of Trustees Recommended Contribution %	7.24%	8.4%	7.532%	*8.09%	6.4%

*The contribution rate shown is the minimum rate recommended by the actuarial consultants. The actual Board approved rate for FY1985 was 5.8%.

Significant actuarial assumptions used to compute contribution requirements are the same as those used to compute the standardized measure of the pension obligation discussed in Note 5.

As a result of the passage of H.B. 2630, which provided for and ad hoc benefit increase for annuitants and the granting of credit for unused sick leave to employees who defer retirement, there was an increase in the actuarial present value of accrued benefit cost of $831,756.

(7)Historical Trend Information

Historical trend information designed to provide information about the System Trust Fund's progress made in accumulating sufficient assets to pay benefits when due is presented on pages 25-26.

(8)Administrative Expenses

A summary of the administrative expenses for the State Employees' Retirement System fiscal years 1988 and 1987 is as follows:

	1988		1987	
	System Trust Fund	Contribution Fund	System Trust Fund	Contribution Fund
Personal services	$1,431,770	$88,373	1,374,652	$114,164
Retirement contributions	104,458	4,400	115,595	6,600
Social Security contributions	88,966	5,703	85,450	6,610
Group insurance	57,000	-	58,858	-
Contractual services	720,398	21,006	690,034	28,867
Travel	38,745	1,790	33,575	4,115
Printing	39,323	-	33,174	1,245
Commodities	22,205	398	16,548	249
Telecommunications	34,224	2,797	38,477	3,100
Electronic Data Processing	525,384	2,821	470,936	3,376
Automotive	5,839	-	5,488	-
Depreciation	51,354	-	35,657	-
Other	50,269	-	42,488	-
Total	$3,169,935	$127,288	$3,000,932	$168,326

(9)Property and Equipment

Fixed assets are capitalized at their cost at the time of acquisition. Depreciation is computed using the straight-line method over the estimated useful life of the asset. The estimated useful lives are as follows: (1) office furniture - 10 years, (2) equipment - 6 years, and (3) automobiles and certain electronic data processing equipment - 3 years.

Land is carried at its original cost, including applicable legal fees, surveying costs, etc.

Construction in progress is composed primarily of architectural and engineering fees related to the construction of a new office facility.

A summary of the changes in fixed assets for 1988 and 1987 is as follows:

	1988			
	Beginning Balance	Additions	Deletions	Ending Balance
Land	$ -	$641,706	$ -	$641,706
Construction in progress	-	17,440	-	17,440
Fixed Assets	585,051	53,977	30,899	608,129
Accumulated Depreciation	416,266	51,354	23,829	443,791
Fixed Assets, net	$168,785	$661,769	$7,070	$823,484

	1987			
	Beginning Balance	Additions	Deletions	Ending Balance
Fixed Assets	$519,474	$84,449	$18,872	$585,051
Accumulated Depreciation	394,558	35,657	13,949	416,266
Fixed Assets, net	$124,916	$48,792	$ 4,923	$168,785

(10)Lease Agreement

The System leases its facilities under a sixty (60) month agreement in effect through June 30, 1990. Under the terms of this lease, the System is required to make monthly payments which include a provision for utilities and building maintenance. Office rental expense amounted to $262,705 and $246,468 for fiscal years 1988 and 1987, respectively.

(11)Accrued Compensated Absences

Employees of the State Employees' Retirement System are entitled to receive compensation for all accrued but unused vacation time and one-half of all unused sick leave earned after January 1, 1984 upon termination of employment. The value of accrued compensated absences as of June 30, 1988 and 1987 were $260,140 and $217,157, respectively.

(12)Land Acquisition and Future Building Site

The System purchased approximately 3.7 acres of land on June 30, 1988 to be used as the site for a proposed office building.

The System's Board of Trustees unanimously decided to proceed with the planning and the eventual construction of a new office facility to accommodate the System's current and long-term space requirements.

The total cost of the land (including legal fees, survey costs, etc.) amounted to $641,706. The building will be capitalized and depreciated in conformance with generally accepted accounting principles upon possession by the System. The total cost associated with the construction of the building during fiscal year 1988 amounted to $17,440. These costs included primarily attorney, appraisal, architectual and engineering fees.

(13)Analysis of Changes in Fund Balances — Reserved

The System Trust Fund maintains three reserve accounts which, when combined, comprise the total reserved fund balance. The reserves are defined as follows:

(a) Participants' contributions — accounts for assets contributed by each participant.

(b) Interest accumulations — accounts for interest credited to each participant's account.

(c) Other future benefits — accounts for all assets not otherwise specifically provided for in items a and b above.

STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS
State Employees' Retirement System Trust Fund
Statements of Changes in Fund Balances (Reserved)
Years ended June 30, 1988 and 1987

	Participants' contributions	Interest accumulations	Other future benefits	Total Fund Balance
Balance at June 30, 1986	$597,438,053	$223,613,728	$1,153,042,902	$1,974,094,683
Add (deduct)				
Excess of revenue over expenses	74,105,993	-	177,682,470	251,788,463
Reserve transfers:				
Accumulated contributions of members who retired during the year, less contributions of annuitants returning to active status	(26,795,012)	-	26,795,012	-
Interest credited to members' accounts	-	32,594,317	(32,594,317)	-
Balance at June 30, 1987	$ 644,749,034	$ 256,208,045	$ 1,324,926,067	$ 2,225,883,146
Add (deduct)				
Excess of revenue over expenses	80,086,786	-	75,836,134	155,922,920
Reserve transfers:				
Accumulated contributions of members who retired during the year, less contributions of annuitants returning to active status	(25,646,199)	-	25,646,199	-
Interest credited to members' accounts	-	37,493,645	(37,493,645)	-
Balance at June 30, 1988	$699,189,621	$293,701,690	$1,388,914,755	$2,381,806,066

(14) Retroactive Restatement

During fiscal year 1988, it was discovered that an error was made in the calculation of the survivors annuity for survivors of covered (i.e. coordinated with Social Security) employees in the actuarial valuation process. In the Illinois Revised Statutes Chapter 108½, Section 14-121 (i), the survivor is guaranteed a minimum benefit of 50% of the retirement annuity that would have been payable to the deceased on such date. In a related section (Section 14-121 (g)), however, it states that this survivors annuity shall be reduced by one-half of the survivors benefit to which the beneficiaries are eligible for under the Federal Social Security Act.

The actuarial consultants were using the guaranteed minimum benefit of the 50% of the retirement annuity exclusive of the reduction due to Social Security benefits received. As a result, the accrued benefit calculations were overestimating the future cost of the survivors annuity benefits.

The error related only to the projected future costs of the survivors annuities and had no affect on any survivors annuity currently or previously paid to the beneficiaries, nor did it affect the amount of net assets available for benefits.

A summary of the changes due to the correction of this error is as follows:

Fiscal Year	Description	Amount Previously Reported	Corrected Amount	Increase/ (Decrease)
1984	Actuarially determined accrued benefit cost	$ 3,127,247,588	$ 3,082,194,117	$ (45,053,471)
	Unfunded accrued benefit cost representing an obligation of the State of Illinois	1,545,921,300	1,500,867,829	(45,053,471)
1985	Actuarially determined accrued benefit cost	2,868,639,632	2,827,329,409	(41,310,223)
	Unfunded accrued benefit cost representing an obligation of the State of Illinois	1,161,380,170	1,120,069,947	(41,310,223)
1986	Actuarially determined accrued benefit cost	3,162,210,759	3,113,334,578	(48,876,181)
	Unfunded accrued benefit cost representing an obligation of the State of Illinois	1,188,116,076	1,139,239,895	(48,876,181)
1987	Actuarially determined accrued benefit cost	3,417,908,944	3,361,722,501	(56,186,443)
	Unfunded accrued benefit cost representing an obligation of the State of Illinois	1,192,025,798	1,135,839,355	(56,186,443)

Analysis of Funding Progress (in thousands of dollars)

FY	(1) Net Assets Available for Benefits*	(2) Pension Benefit Obligation	(3) Percentage Funded (1)÷(2)	(4) Unfunded Pension Benefit Obligation (2)−(1)	(5) Annual Covered Payroll	(6) Unfunded Pension Benefit Obligation as a % of Covered Payroll (4)÷(5)
1985	$1,707.2	$2,830.8	60.3%	$1,123.6	$1,569.5	71.6%
1986	1,974.1	3,082.8	64.0%	1,108.7	1,713.8	64.7%
1987	2,225.9	3,304.2	67.4%	1,078.3	1,825.2	59.1%
1988	2,381.8	3,490.7	68.2%	1,108.9	1,954.0	56.8%

Analysis of the dollar amounts of net assets available for benefits, pension benefit obligation, and unfunded pension benefit obligation in isolation can be misleading. Expressing the net assets available for benefits as a percentage of the pension benefit obligation provides one indication of the System Trust Fund's funding status on a going-concern basis. Analysis of this percentage over time indicates whether the System is becoming financially stronger or weaker. Generally, the greater this percentage, the stronger the public employees' retirement system (PERS). Trends in unfunded pension benefit obligation and annual covered payroll are both affected by inflation. Expressing the unfunded pension benefit obligation as a percentage of annual covered payroll approximately adjusts for the effects of inflation and aids analysis of the System Trust Fund's progress made in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the stronger the PERS.

*At cost

Revenues by Source and Expenses by Type

FY Ended June 30	Member Contributions	State Contributions	Investment Income	Sub Total	General Revenue Fund Appropriations, Less balances Lapsed	Total
1979	$56,328,543	$84,762,923	$61,496,348	$202,587,814	$98,762	$202,686,576
1980	59,448,493	94,056,122	79,438,744	232,943,359	119,341	233,062,700
1981	64,573,084	96,918,451	93,957,329	255,448,864	142,012	255,590,876
1982	69,300,949	61,500,375	101,697,502	232,498,826	145,503	232,644,329
1983	72,371,246	71,846,403	192,573,257	336,790,906	149,002	336,939,908
1984	73,442,196	86,464,279	150,170,315	310,076,790	168,700	310,245,490
1985	77,830,806	94,456,693	101,754,931	274,042,430	174,482	274,216,912
1986	84,563,536	102,213,693	240,235,534	427,012,763	186,885	427,199,648
1987	90,096,279	109,559,940	226,929,603	426,585,822	168,326	426,754,148
1988	95,928,239	99,990,922	148,802,057	344,721,218	127,288	344,848,506

Expenses by Type

FY Ended June 30	Benefits	Contribution Refunds	Administrative Expenses, System Trust Fund	Other Expenses*	Sub Total	Administrative Expenses, Contribution Fund	Total
1979	$76,000,765	$12,344,851	$1,456,878		$89,802,494	$98,762	$89,901,256
1980	81,342,048	12,328,329	1,752,078	$2,460,525	97,882,980	119,341	98,002,321
1981	89,147,299	12,352,136	1,973,475	5,034,562	108,507,472	142,012	108,649,484
1982	100,453,675	13,942,805	2,245,727	(2,480,124)	117,162,083	145,503	114,307,586
1983	111,852,846	14,009,169	2,290,492		128,152,507	149,002	128,301,509
1984	120,996,071	14,145,496	2,428,623		137,570,190	168,700	137,738,890
1985	132,316,478	13,240,326	2,552,452		148,109,256	174,482	148,283,738
1986	143,548,518	13,780,843	2,848,181		160,177,542	186,885	160,364,427
1987	159,614,328	12,182,099	3,000,932		174,797,359	168,326	174,965,685
1988	173,644,549	11,983,814	3,169,935		188,798,298	127,288	188,925,586

*Net realized loss or (gain) on investments undistributed by the Illinois State Board of Investment. Accumulated net losses from 1970 through 1979 amounted to $42,998,251. Since 1982 realized losses or gains have been distributed annually.

Analysis of Employer Contributions — Fiscal Year 1979 through 1988

Fiscal Year	(1) Board Approved Rate (A)	(2) Annual Earnings	(3) Employer Contributions Required (1×2)	Employer Contribution Made (4) Employer Contr. (B)	(5) State Pension (C)	(6) Senate Res. No. 33 (D)	(7) Other	(8) (4+5+6+7) Total	(8-3) Excess (Deficiency) of Contrib. Made Over Contr. Req.
1979	7.760%	$1,069,885,900	$83,023,146	$83,023,148	$1,095,000		$644,775	$84,762,923	$1,739,777
1980	8.000%	1,137,667,500	91,013,400	91,380,122	2,676,000			94,056,122	3,042,722
1981	7.500%	1,253,016,000	93,976,200	94,542,451	2,376,000			96,918,451	2,942,251
1982	6.820%	1,334,262,000	90,996,668	60,348,375	1,152,000			61,500,375	(29,496,293)
1983	5.550%	1,378,735,000	76,519,793	67,421,803	1,838,200	$2,586,400		71,846,403	(4,673,390)
1984	6.400%	1,437,546,000	92,002,944	81,358,279	2,378,000	2,728,000		86,464,279	(5,538,665)
1985	8.090%	1,569,532,000	126,975,139	89,482,193	2,378,500	2,596,000		94,456,693	(32, 518,446)
1986	7.532%	1,713,755,000	129,080,027	97,741,393	2,130,000	2,342,300		102,213,693	(26,866,334)
1987	8.400%	1,825,196,000	153,316,464	105,095,840	2,215,500	2,248,600		109,559,940	(43,756,524)
1988	7.240%	1,953,960,000	141,466,704	97,725,922	1,673,700	591,300		99,990,922	(41,475,782)

(A) = For fiscal years 1982 and 1985, the contribution rate shown is the minimum rate recommended by the actuarial consultants. The actual Board approved rate was 4.5% and 5.8% for FY 1982 and 1985, respectively. For all other years presented, the Board approved rate was at least equal to or greater than the minimum contribution rate recommended by the actuaries.

(B) = The System Trust Fund recognizes revenue based upon either the board approved rate or the state appropriated rate, as appropriate.

(C) = The System Trust Fund receives an annual appropriation from the State Pension Fund. The State Pension Fund receives proceeds from the sale of abandoned and unclaimed property.

(D) = In fiscal year 1983, House Amendment No. 1 to Senate Bill 177 was adopted by the state legislature. This bill reduced the dollar amount appropriated for the employer's share of retirement contributions. Senate joint resolution No. 33 provides that the System Trust Fund will be repaid the amount of the Senate Bill 177 reductions at the rate of 20% per year over the next five fiscal years, including interest at the rate 6% per annum.

Combining Balance Sheets
Years Ended June 30, 1988 and 1987

	1988			1987		
Assets	Pension Trust Fund State Employees' Retirement System	Agency Fund Social Security Contribution	Total	Pension Trust Fund State Employees' Retirement System	Agency Fund Social Security Contribution	Total
Cash	$ 9,893,839	$ -	$ 9,893,839	$ 5,977,771	$ -	$ 5,977,771
Cash, restricted for Social Security remittances	-	2,252,064	2,252,064	-	4,334,906	4,334,906
Receivables:						
Contributions receivable:						
Participants	3,937,685	-	3,937,685	4,506,275	-	4,506,275
Employing State Agencies	2,454,280	-	2,454,280	5,269,062	-	5,269,062
Other accounts receivable	539,128	-	539,128	414,451	-	414,451
	6,931,093	-	6,931,093	10,189,788	-	10,189,788
Investments	2,367,063,722	-	2,367,063,722	2,211,906,317	-	2,211,906,317
Property and equipment, net of accumulated depreciation	823,484	-	823,484	168,785	-	168,785
Total Assets	$2,384,712,138	$ 2,252,064	$2,386,964,202	$2,228,242,661	$ 4,334,906	$2,232,577,567
Liabilities and Fund Balance						
Benefits payable	$ 1,476,752	$ -	$ 1,476,752	$ 1,144,997	$ -	$ 1,144,997
Refunds payable	375,069	-	375,069	223,318	-	223,318
Administrative expenses payable	409,660	-	409,660	411,370	-	411,370
Participants' deferred service credit accounts	644,591	-	644,591	579,830	-	579,830
Unremitted Social Security contributions	-	1,822,858	1,822,858	-	4,037,829	4,037,829
Amounts held for Social Security remittances	-	429,206	429,206	-	297,077	297,077
Total Liabilities	2,906,072	2,252,064	5,158,136	2,359,515	4,334,906	6,694,421
Fund Balance						
Actuarially determined benefit cost	3,641,579,030	-	3,641,579,030	3,361,722,501	-	3,361,722,501
Less unfunded accrued benefit cost representing an obligation of the State of Illinois	1,259,772,964	-	1,259,772,964	1,135,839,355	-	1,135,839,355
Total Fund Balance	$2,381,806,066	$ -	$2,381,806,066	$2,225,883,146	$ -	$2,225,883,146
Total Liabilities and Fund Balance	$2,384,712,138	$ 2,252,064	$2,386,964,202	$2,228,242,661	$ 4,334,906	$2,232,577,567

Social Security Contribution Fund
Statements of Changes in Assets and Liabilities
Years Ended June 30, 1988 and 1987

	1988				1987			
Assets	Balance July 1, 1987	Additions	Deductions	Balance June 30, 1988	Balance July 1, 1986	Additions	Deductions	Balance June 30, 1987
Cash, restricted for Social Security remittances	$4,334,906	$4,037,868	$6,120,710	$2,252,064	$9,262,057	$125,257,128	$130,184,279	$4,334,906
Liabilities								
Unremitted Social Security contributions	$4,037,829	$ 53,377	$2,268,348	$1,822,858	$8,596,003	$125,257,128	$129,815,302	$4,037,829
Amounts held for Social Security remittances	297,077	132,129	-	429,206	666,054	-	368,977	297,077
	$4,334,906	$185,506	$2,268,348	$2,252,064	$9,262,057	$125,257,128	$130,184,279	$4,334,906

SYSTEM TRUST FUND — SUMMARY OF REVENUES BY SOURCE

Years Ended June 30, 1988 and 1987

	1988	1987
Contributions:		
Participants	$ 94,744,836	$ 88,972,543
Repayments of contributions refunded	381,535	367,175
Interest received from participants	801,868	756,561
Total participants contributions	$ 95,928,239	$ 90,096,279
Employing state agencies	$ 97,725,922	$105,095,840
State Pension Fund appropriation	1,673,700	2,215,500
Supplemental state contribution	591,300	2,248,600
Total state contributions and appropriations	$ 99,990,922	$109,559,940
Investments:		
Net investment income	$132,301,594	$119,922,351
Interest earned on cash balances	644,652	725,599
Net realized gain on sale of investments	15,855,811	106,281,653
Total investment revenue	$148,802,057	$226,929,603
Total Revenue	$344,721,218	$426,585,822

SYSTEM TRUST FUND — SUMMARY SCHEDULE OF CASH RECEIPTS AND DISBURSEMENTS

Years Ended June 30, 1988 and 1987

	1988	1987
Cash balance, beginning of year	$ 5,977,771	$ 7,618,809
Receipts:		
Member contributions	94,194,041	86,895,546
Employer contributions	101,134,320	107,037,914
State Pension Fund contribution	1,673,700	2,215,500
Transfers from Illinois State Board of Investment	30,000,000	14,000,000
Interest income on cash balance	632,914	737,476
Claims receivable payments	587,903	598,701
Installment payments - prior service credit	580,956	491,773
Other	132,314	117,309
Total cash receipts	$228,936,148	$212,094,219
Disbursements:		
Annuity payments:		
Retirement annuities	132,419,661	119,905,180
Widow's annuities	3,088,444	3,132,859
Survivor's annuities	16,790,980	15,467,935
Death benefits	6,739,930	6,928,282
Disability benefits	13,082,385	13,049,592
Refunds	12,058,436	12,257,597
Administrative expenses	3,840,244	2,993,812
Transfers to Illinois State Board of Investment	37,000,000	40,000,000
Total cash disbursements	$225,020,080	$213,735,257
Cash balance, end of year	$ 9,893,839	$ 5,977,771

REVENUES:

Total revenue of $344.7 million for FY 1988 was a $81.9 million decrease from the FY 1987 level of $426.6 million. Net income from investments and net realized gains on sales of investments were down significantly from the prior fiscal year. It should be noted, however, that the net realized gains on sale of investments in FY 1987 were unusually high as compared to prior fiscal years due to very favorable financial markets. It should not have been anticipated that the dollar amount of the gains would remain at that level in subsequent years.

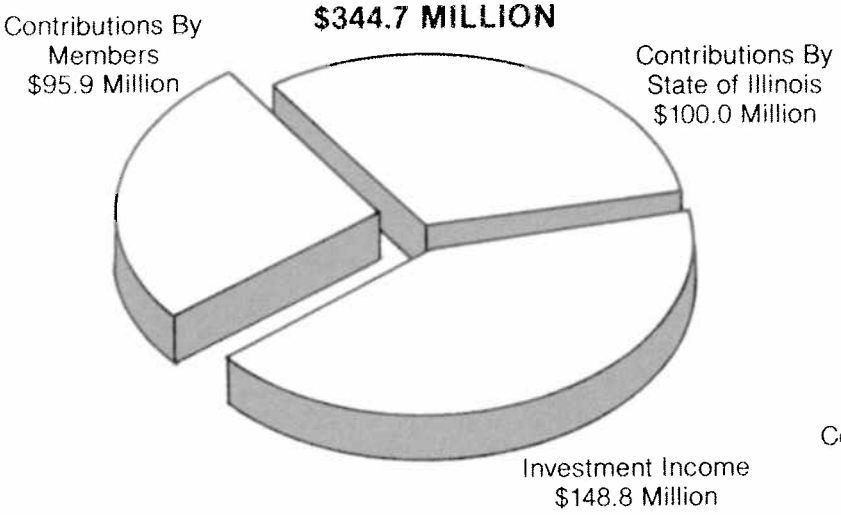
Revenue Source	FY 88 (Millions)	FY 87 (Millions)	Increase/(Decrease) Amount	Percentage
Member Contributions	$ 95.9	$ 90.1	$ 5.8	6.4 %
State Contributions	100.0	109.6	(9.6)	(8.8)%
Investment Income	148.8	226.9	(78.1)	(34.4)%
Total	$344.7	$426.6	$(81.9)	(19.2)%

There were 191 more active members as of June 30, 1988 than on June 30, 1987. This increase of .3% in membership and average wage increases of 6.5% resulted in an increase of 7.1% in wages subject to retirement contributions. State contributions show a decrease of 8.8% ($9.6 million). Member contributions were $5.8 million (6.4%) higher than for FY 1987. As shown in the table below, the average rate of contributions by members in FY 1988 was 4.91% compared to 4.94% in FY 1987.

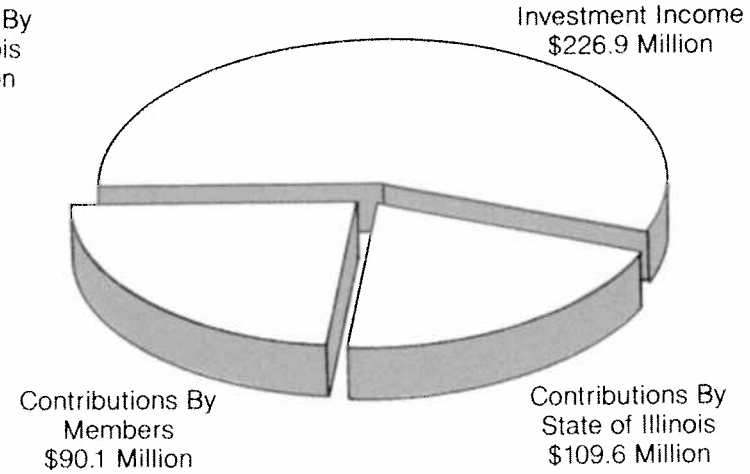
Active Membership	FY 88	FY 87	Increase/(Decrease) Number/Amount	Percentage
Coordinated Members	65,137	64,564	573	.9%
Noncoordinated Members	9,786	10,168	(382)	(3.8)%
Total Active Members	74,923	74,732	191	.3%
Earnings Reported				
All Members (Millions)	$1,954.0	$1,825.2	$128.8	7.1%
Average Rate of Contributions				
All Members	4.91%	4.94%		

The System has $512,723 of arrearages and overpayments as of June 30, 1988. There were 304 accounts with arrearages, 180 claim overpayments and 9 refund overpayments. The System employs several different methods for the collection of its outstanding receivables. These methods include collections by the System, use of the office of the Comptroller's involuntary offset system, contracting with private collection firms and legal action through the office of the Attorney General.

REVENUES BY SOURCE 1988
TOTAL REVENUES
$344.7 MILLION



REVENUES BY SOURCE 1987
TOTAL REVENUES
$426.6 MILLION



Gross investment income for 1988 of $137,942,491, less the Investment Board's administrative expenses of $5,640,897 and the net realized gain on sale of investments amounting to $15,855,811, resulted in net revenue from investments of $148,157,405. Transfers of funds to the Illinois State Board of Investment amounted to $37,000,000 and transfers from the Board of $30,000,000 resulted in a net transfer for investments of $7,000,000. The balance of investments at cost increased by $148,157,405 plus $7,000,000 or $155,157,405, from June 30, 1987 thru June 30, 1988. The following table shows a comparison of investment operations for FY 1988 and FY 1987.

	1988	1987	Increase/(Decrease) Amount	Percentage
Balance at beginning of year, at cost	$2,211,906,317	$1,959,702,313	$252,204,004	12.9%
Cash remitted for investment (net)	7,000,000	26,000,000	(19,000,000)	(73.1)%
Investment income:				
Commingled Fund income	137,942,491	124,595,843	13,346,648	10.7%
Less Expenses	(5,640,897)	(4,673,492)	(967,405)	20.7%
Distributed Net Realized Gain/ (Loss) on Sale of Investments	15,855,811	106,281,653	(90,425,842)	(85.1)%
Net investment income	148,157,405	226,204,004	(78,046,599)	(34.5%)
Balance at end of year, at cost	$2,367,063,722	$2,211,906,317	$155,157,405	7.0%
Market value	$2,485,230,297	$2,416,626,806	$68,603,491	2.8%

In addition, interest on the average balance in the System Trust Fund's account for FY 1988 was $644,652 compared to $725,599 during FY 1987.

EXPENSES:

The number of members receiving retirement annuities on June 30, 1988 was 2.3% above the June 30, 1987 level reflecting the normal pattern of increase during the past 10 years; however, the cost of these annuities increased by 10.4% over the FY 1987 level. Higher salaries for current retirees, post retirement increases granted each January 1, and an increase in the minimum retirement annuity resulted in costs rising at a more rapid pace than the number of annuitants. Survivor annuities increased at a near normal rate of 3.5% in number with a 7.4% increase in dollar costs. Continued review of the disability recipient eligibility helped reduce the number of recurring benefit payments for disability by 2.6% while rising salary rates increased the dollar amount of payments by 1.4%.

	FY 88 (Millions)	FY 87 (Millions)	Increase/Decrease Amount	Increase/Decrease Percentage
Retirement annuities	$132.2	$119.8	$12.4	10.4%
Survivors' annuities	20.3	18.9	1.4	7.4%
Disability benefits	14.7	14.5	.2	1.4%
Lump sum death benefits	6.4	6.4	-	-
Refunds	12.0	12.2	(.2)	(1.6)%
Administrative expense	3.2	3.0	.2	6.7%
TOTAL EXPENSES	$188.8	$174.8	$14.0	8.0%

NUMBER OF RECURRING BENEFIT PAYMENTS

	FY Ended June 30, 1987	New Claims Processed During FY 88	Benefits Ceased During FY 88	FY Ended June 30, 1988	Increase/(Decrease) Amount	Increase/(Decrease) Percentage
Retirement	22,529	1,506	997	23,038	509	2.3%
Survivors	8,015	617	336	8,296	281	3.5%
Disability	1,577	1,779	1,820	1,536	(41)	(2.6)%
TOTALS	32,121	3,902	3,153	32,870	749	2.3%

Lump sum death benefits are primarily refunds of member contributions and will vary from year to year. Refunds to members have been significantly decreasing in the past few years. There was a decrease of $.2 million (1.6%) in FY 1988. The decreasing trend in refunds is primarily due to the 6 month qualifying period required of new employees hired since January, 1984.

RESERVES:

As of June 30, 1988, the funds available for payment of current and future benefits were $2,381.8 million as shown in the following schedule:

Assets	FY 88 (Millions)	FY 87 (Millions)	Increase (Decrease)
Cash	$ 9.9	$ 6.0	$ 3.9
Receivables (less payables)	4.0	7.8	(3.8)
Investments	2,367.1	2,211.9	155.2
Fixed Assets (net of accumulated depreciation)	.8	.2	.6
NET ASSETS	$2,381.8	$2,225.9	$155.9

Total System Trust Fund revenues for FY 1988 of $344.7 less expenditures of $188.8 million resulted in a net increase to reserves of $155.9 million.

Reserves	FY 88 (Millions)	FY 87 (Millions)	Net Increase
Member Contributions	$ 699.2	$ 644.8	$ 54.4
Future Operations	1,682.6	1,581.1	101.5
TOTAL ASSETS	$2,381.8	$2,225.9	$155.9

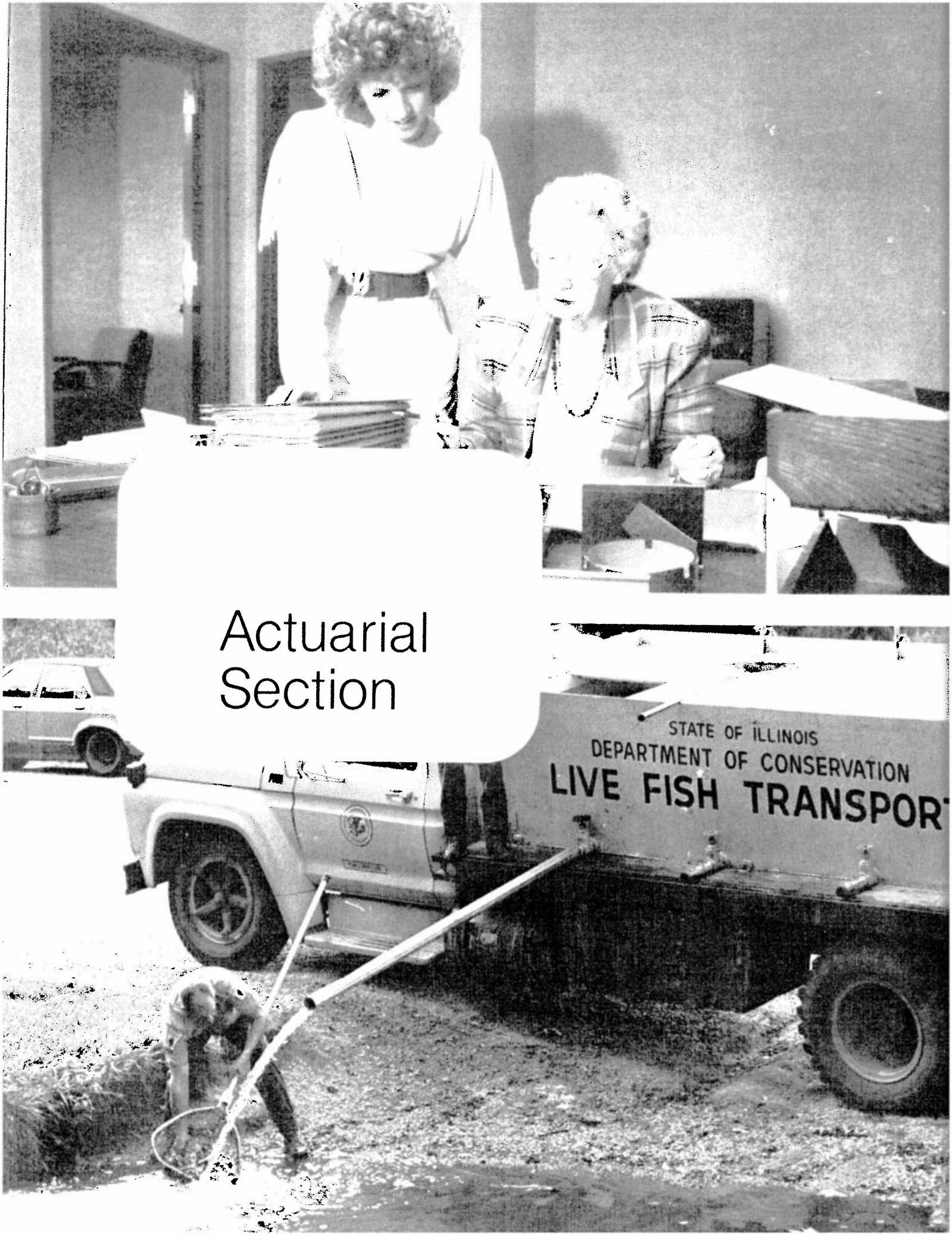
Member contributions transferred to the Reserve for Future Operations due to retirement or death of active members during the year amounted to $25.6 million.

SOCIAL SECURITY:

On September 15, 1953, the State of Illinois and the Federal Government signed an agreement making social security coverage available to public employees in Illinois. In addition to extending new coverage, the System, as State Administrator, collects and transmits social security contributions to the U.S Department of Health and Human Services for approximately 1,500 towns, villages and other political entities. Members of two retirement systems in the State of Illinois, the Illinois Municipal Retirement Fund (IMRF) and the State Employees' Retirement System (SERS), are also covered by social security. During fiscal year 1988 contributions collected and transmitted, including credits applied for the political entities amounted to $1.5 million and for the SERS, $2.5 million. Due to the passage of new federal legislation which mandated that state and local government employers conform to the same remittance schedule as private employers, the responsibility for the collection and remittance of Social Security and Medicare taxes was transferred from this agency to the Office of the Comptroller of the State of Illinois effective, January 1, 1987. Adjustments to Social Security or Medicare taxes for wages paid thru December 31, 1986, are processed through the Contribution Fund. Subsequent to January 1, 1987, any adjustments to Social Security or Medicare taxes are reported through the Office of the Comptroller.

The Social Security Division has a staff of two full-time employees. Data processing and accounting services are performed by other divisions of the System on a contractual basis. Expenses are appropriated by the General Assembly and subsequently recovered from the reporting entities on a pro-rated basis. The total amount of expenses appropriated from the General Revenue Fund for the administration of the Contribution Fund was $127,288 and $168,326 for fiscal years 1988 and 1987 respectively.

The contribution rate in 1988 was 7.51% for both the employee and the employer share on a maximum wage of $45,000. Collections and transmittals are administered through the Contribution Fund in custody of the Treasurer of the State of Illinois.



Actuarial Section

EMPLOYEE BENEFITS
COMPENSATION PROGRAMS
EMPLOYEE COMMUNICATIONS
ADMINISTRATIVE SYSTEMS
RISK MANAGEMENT
INTERNATIONAL SERVICES
ORGANIZATION SURVEYS

THE Wyatt COMPANY
ACTUARIES AND CONSULTANTS
SUITE 2400
303 WEST MADISON STREET
CHICAGO, ILLINOIS 60606-3308
(312) 704-0600

OFFICES IN PRINCIPAL CITIES
AROUND THE WORLD

October 31, 1988

Board of Trustees and Executive Secretary
State Employees' Retirement System of Illinois
P. O. Box 19255
2815 West Washington Street
Springfield, IL. 62794-9255

ACTUARIAL CERTIFICATION

We have completed the annual actuarial valuation of the assets and liabilities of the State Employees' Retirement System of Illinois as of June 30, 1988. This valuation was made using the same actuarial assumptions as used for the prior year. Since the last valuation there has been one amendment (HB2630/PA1472) which has affected SERS costs and liabilities. 158 members of the Teachers' Retirement System who were employed by the Department of Corrections elected to transfer to SERS as noncovered employees effective July 1, 1987. In addition, a correction was made in our calculation of survivor annuities, resulting in a decrease of approximately 1.5% in the total actuarial liabilities.

Pursuant to the law establishing the System, the actuary shall investigate the experience under the System at least once every five years and recommend as a result of such investigation the actuarial assumptions to be adopted. The Wyatt Company, as the actuary, completed such a review for the five years ending June 30, 1985 and the assumptions used for the current valuation were based on that study. We believe that, in the aggregate, the current assumptions relate reasonably to the past and anticipated experience of the plan.

A contribution rate has been determined using the entry age normal cost method providing for the current cost (normal cost) plus an amortization of the unfunded accrued actuarial liability as a level percentage of payroll by June 30, 2028. For ancillary benefits for

active employees, costs are computed assuming that employees were hired after June 30, 1980. This results in normal cost rates that decline gradually as a percentage of payroll. As the amortization contribution can be expected to remain level, the total contribution rate can be expected to decrease gradually as a percentage of payroll until June 30, 2028, and then drop to a constant normal cost rate. Employer contributions, however, have been insufficient in recent years to meet the financing objective so that future contribution requirements may be higher than expected.

For purposes of determining contribution rates, assets have been valued at cost as reported by the Illinois State Board of Investment. The liabilities have been valued based on employee data which is supplied by the administrative staff of the System and verified by the System's auditor. We have made additional tests to ensure its accuracy.

In our opinion, the following schedule of valuation results fairly presents the financial condition of the State Employees' Retirement System of Illinois as of June 30, 1988. The contribution rate determined complies with the applicable law in force as of the valuation date.

THE WYATT COMPANY

By S. Lynn Hill
S. Lynn Hill
Actuarial Assistant

By Lloyd L. Nordstrom
Lloyd L. Nordstrom
Fellow Of The Society of Actuaries

By Robert L. Barnes
Robert L. Barnes
Fellow Of The Society Of Actuaries

INTRODUCTION

For many years, the state contribution to the System Trust Fund has been based on projected benefit payments (payout). For FY 1988, regular state appropriations were made at a level of 48% of the System Trust Fund projected payout.

The System Trust Fund receives contributions from a number of sources which can be considered as employer contributions, with the largest source being the regular state appropriation. During FY 1988, the System Trust Fund received the last payment of the five-year repayment of funding reductions made in FY 1983. The System Trust Fund also received an appropriation from the State Pension Fund.

Annually, the System's actuarial consultants perform a valuation of the liabilities and reserves of the System Trust Fund in order to make a determination of the amount of contributions required from the state. These results are then certified to the Board.

The Board, in turn, has the duty of certifying a rate of contribution, based upon employees' compensation, required to be paid to the System during the succeeding fiscal year. The employers' contribution amount, together with members' contributions, income from investments and any other income received by the System, shall be sufficient to meet the cost of maintaining and administering the System on a funded basis in accordance with actuarial reserve requirements, pursuant to Article 14-131 of the Illinois Revised Statutes. The statutes define "actuarial reserves" as "An accumulation of funds in advance of benefit payments which will be sufficient with respect to each member and his beneficiaries, if any, to pay the prescribed benefits, computed according to the actuarial tables, without further contributions by or on behalf of the member."

The statutes do not currently specify any particular funding method to be utilized by the Syste; nor, is the amortization period to be used for prior unfunded service costs currently specified in the law.

The Board reviews and evaluates several alternative contribution rates supplied by the System's actuary for use as the current fiscal year employer contribution rate. Upon completion of this review, the Board certifies an employer contribution rate for all state agencies.

Based upon the state's funding method described above, the System, in recent years, has not received the minimum actuarially determined employer contribution amount.

The underfunding of employer contributions places undue pressure on one of the other major sources of revenue to the System, namely income from investments, to consistently provide an increasing percentage of total fund revenue. In recent years, the higher than assumed rate of return on investments distorts the fact that employer contributions have not kept pace with prior, current, and future estimated benefit costs.

In an attempt to address the pension funding dilemma, the state legislature passed S.B.1470, which provided for a standardized funding method (projected unit credit) and a specified term for the amortization of prior unfunded pension costs (40 years, level percentage of payroll).

Unfortunately this legislation, which was amendatorily vetoed by the Governor, to postpone the implementation date, was not accepted by the General Assembly during the fall 1988 veto session.

ACTUARIAL COST METHOD AND SUMMARY OF MAJOR ACTUARIAL ASSUMPTIONS

The System utilizes the entry age normal cost method. Under this method, the projected pensions at retirement age are first determined and the values thereof at the individual member's entry age or hire age are determined. The values so determined are divided by the value at entry age of all future compensation payable to the member to determine the normal cost as a level percentage of covered pay. The normal cost for a particular year is that percentage of covered compensation for the year.

The actual liability at any point in time is the value of the projected pensions at that time, less the value of future normal costs.

Ancillary benefits for active members, in particular disability benefits, death and survivor benefits, termination benefits and the post-retirement increments, use the same procedures outlined above except that the entry age is the age at the later of hire date or June 30, 1980.

A description of the actuarial assumptions utilized for FY-88 and FY-87 follows:

Mortality: 1986 Projected Experience Table, a table based on experience underlying the 1971 Group Annuity Mortality Table, without margins, with a projection for mortality improvements to 1986. Five percent of deaths amongst active employees are assumed to be in the performance of their duty.

Interest: 8% per annum, compounded annually.

Termination: Illustrative rates follow. It is assumed that terminated employees will not be rehired.

Age	Rate Males	Rate Females
20	.605	.397
25	.178	.164
30	.112	.116
35	.077	.092

Age	Rate Males	Rate Females
40	.064	.076
45	.054	.061
50	.044	.048
55	.000	.000

Salary Increases: 6½% per annum, compounded annually.

Retirement Rates: Retirement was assumed to occur at age 65 except for employees who retire under the "alternative formula", who were assumed to retire at age 60.

Assets: Assets available for benefits are valued at book value (cost).

Expenses: As estimated and advised by SERS staff, based on current expenses with an allowance for expected increases.

Marital Status: 85% of employees are assumed to be married.

Spouse's Age: The female spouse is assumed to be three years younger than the male spouse.

In addition to the above, other assumptions used included disability incidence, recovery from disability, mortality of disabled lives, remarriage rates, ages, and numbers of children and Social Security benefit levels.

VALUATION RESULTS

Actuarial Liability (Reserves)	FY-88	FY-87
For Annuitants:		
For Benefit Recipients:		
Retirement Annuities	$ 1,319,780,926	$ 1,220,936,191
Survivor Annuities	158,985,739	152,461,276
Disability Annuities	61,608,504	60,260,875
Deferred:		
Retirement Annuities	1,096,076	951,851
Survivor Annuities	5,356,916	5,228,433
Total	$ 1,546,828,161	$1,439,838,626
For Inactive Members:		
Eligible for Deferred Vested Pension Benefits	53,498,075	51,580,526
Eligible for Return of Contributions Only	6,921,360	6,344,548
Total	$ 60,419,435	$ 57,925,074
For Active Members:	$ 2,034,331,434	$ 1,863,958,801
Total	$ 3,641,579,030	$3,361,722,501
Assets, Book Value (Cost)	$ 2,381,806,066	$2,225,883,146
Unfunded Actuarial Liability	$ 1,259,772,964	$1,135,839,355

SHORT-TERM SOLVENCY TEST

A short-term solvency test is one means of checking a system's progress under its funding program. In a short-term solvency test, the plan's present assets (primarily cash and investments) are compared with: 1) active member contributions on deposit; 2) the liabilities for future benefits to present retired lives; 3) the liabilities for service already rendered by active members. In a system that has been following level percent of payroll financing, the liabilities for active member contributions on deposit (liability 3) should be partially covered by the remainder of present assets. If the system continues using level cost financing, the funded portion of liability 3 will increase over time, although it is very rare for a system to have its liability 3 fully funded.

The State of Illinois, however, has funded the System based on benefit payout, a level which increases over time reflecting a larger work force and higher salary levels. Consequently, it can be expected that a percentage of liability 3 has been funded to date. (It should also be noted that the improvement reflected in recent years results primarily from the significant realized gains on the sale of investments previously described.)

Computed Actuarial Values (in thousands of dollars)

Fiscal Year	Member Contributions (1)	Current Retirees and Beneficiaries (2)	Active and Inactive Members, Employer Financed Portion (3)	Net Assets Available For Benefits	Percentage of Actuarial Values Covered by Net Assets Available (1)	(2)	(3)
1979	$347,173	$ 598,170	$ 684,422	$ 799,803	100.0%	75.7%	0.0%
1980	378,468	791,289	764,297	934,864	100.0	70.3	0.0
1981	413,773	819,272	960,085	1,081,805	100.0	81.5	0.0
1982	448,908	914,281	1,144,618	1,200,142	100.0	82.2	0.0
1983	482,983	1,049,972	1,270,744	1,408,780	100.0	88.2	0.0
1984	517,008	1,150,634*	1,414,552*	1,581,326	100.0	92.5	0.0
1985	554,823	1,172,344*	1,100,162*	1,707,259	100.0	98.3	0.0
1986	597,438	1,287,644*	1,228,253*	1,974,095	100.0	100.0	7.2
1987	644,749	1,431,161*	1,285,813*	2,225,883	100.0	100.0	11.7
1988	699,190	1,546,828	1,395,561	2,381,806	100.0	100.0	9.7

*as restated

ANALYSIS OF FUNDING

In an inflationary economy, the value of the dollar decreases. This environment results in employees' pay and retirement benefits increasing in dollar amounts resulting in unfunded accrued liabilities which increase in dollar amounts, all at a time when the actual substance of these items may be decreasing. Looking at just the dollar amounts of unfunded accrued liabilities can be misleading. The ratio of the unfunded accrued liabilities to active employee payroll provides an index which clarifies understanding. The smaller the ratio of unfunded liabilities to active member payroll, the stronger the system. Observation of this relative index over a period of years will give an indication of whether the system is becoming financially stronger or weaker. (It should be noted that the improvement reflected in the following schedule for recent years results primarily from significant realized gains on the sale of investments previously described.)

(in thousands of dollars)

Fiscal Year	Total Actuarial Liability	Net Assets	Net Assets as a % of Actuarial Liability	Total Unfunded Actuarial Liability	Member Payroll	Unfunded Actuarial Liability as a % of Member Payroll
1979	$1,629,766	$ 799,803	49.1%	$ 829,962	$1,069,886	78%
1980	1,934,054	934,864	48.3	999,190	1,137,668	88
1981	2,193,130	1,081,805	49.3	1,111,325	1,253,016	89
1982	2,507,807	1,200,142	47.9	1,307,665	1,334,262	98
1983	2,803,699	1,408,780	50.2	1,394,919	1,378,735	101
1984	3,082,194*	1,581,326	51.3	1,500,907*	1,437,546	104
1985	2,827,329*	1,707,259	60.4	1,120,070*	1,569,532	71
1986	3,113,335*	1,974,095	63.4	1,139,240*	1,713,755	66
1987	3,361,723*	2,225,883	66.2	1,135,840*	1,825,196	62
1988	3,641,579	2,381,806	65.4	1,259,773	1,953,960	65

*as restated

ANALYSIS OF FINANCIAL EXPERIENCE

Gain (Loss) in Actuarial Liability for Fiscal Years ending June 30, 1988 and 1987 are as follows:

Activity	1988	1987
1. Actuarial Gains (Loss)		
(a) Age & Service Retirements	$ (17,237,492)	$ 13,711,529
(b) Incidence of Disability	(1,172,057)	(952,458)
(c) In-Service Mortality	(4,121,569)	(4,016,378)
(d) Retiree Mortality	3,971,693	1,997,299
(e) Disabled Mortality	(98,860)	47,745
(f) Termination of Employment	(13,237,063)	(4,684,310)
(g) Salary Increases	(11,318,379)	(21,918,010)
(h) Investment Income	(29,544,739)	68,026,803
(i) Other	(4,895,685)	7,478,295
Total Actuarial Gain (Loss)	$ (77,654,151)	$ 59,690,515
+		
2. Contribution (Income)	$ (55,477,149)	$ (54,142,748)
+		
3. Non Recurring Items		
(a) Plan Amendments (HB2630)	$ (831,756)	$ (28,033,700)
(b) Change in Method of Reporting Salaries	-	18,576,211
+		
(c) Correction in Calculation of Survivors Benefits	10,029,447	7,310,262*
=		
4. Total Financial Gain (Loss)	$ (123,933,609)	$ (3,400,540)

*as restated

RECONCILIATION OF UNFUNDED ACTUARIAL LIABILITY

	FY-88	FY-87
Unfunded Liability Beginning of FY	$ 1,135,839,355	$ 1,188,116,076
Restatement - Correction in Calculation of Survivors Benefits	-	(48,876,181)
Unfunded Liability Beginning of FY, as restated	1,135,839,355	1,139,239,895*
Contributions Due		
Interest on the Unfunded Liability	95,362,064	95,049,286
Total Normal Cost	151,592,824	154,242,862
Interest on Normal Cost	12,127,426	12,339,429
Total Due	$ 259,082,314	$ 261,631,577
Contributions Paid		
Participants	$ 95,928,239	$ 90,096,279
Employing State Agencies	99,399,622	107,344,440
State Pension Fund	591,300	2,215,500
Interest on Contributions	7,686,004	7,832,610
Total Paid	$ 203,605,165	$ 207,488,829
Increase in the Unfunded Liability	55,477,149	54,142,748
Actuarial (Gains) Losses		
From Investment Return (Greater) Lesser Than 8%	29,544,739	(68,026,803)
From Salary Increases (Greater) Lesser Than 6½%	11,318,379	21,918,010
From Other Sources	36,791,033	(13,581,722)
Total Actuarial (Gains) Losses	$ 77,654,151	$(59,690,515)
(Decrease) Due to Change in Method of Reporting Salaries	-	(18,576,211)
Plan Amendments	831,756	28,033,700
(Decrease) Due to Correction in Calculation of Survivors Benefits	(10,029,447)	(7,310,262)
Total Increase (Decrease) in Actuarial Liability	123,933,609	(3,400,540)
Unfunded Liability End of FY	$ 1,259,772,964	$ 1,135,839,355

*as restated

Investment Section

INVESTMENT REPORT

By state law the System's investment function is managed by the Illinois State Board of Investment. The Board was created in 1969 to provide a means of centralizing the investment management function for public employee pension funds and retirement systems operating in the state. At the end of the fiscal year, in addition to the assets of the State Employees' Retirement System, the Board also managed the investment function for the Judges' and General Assembly Retirement Systems. As of June 30, 1988, total net assets under management valued at market, amounted to $2.669 billion. Of the total assets under management, $2.485 billion or 93% represented assets of the State Employees' Retirement System.

Management Approach

The Fund is managed by the Illinois State Board of Investment, in accordance with the "prudent person rule" as adopted by the Illinois General Assembly in 1982. The Board has established a long-range investment policy which, in line with the prudent person rule, affirms that the Fund's objective is to provide the greatest possible long-term benefits through maximization of the total return of the Fund, within prudent risk parameters. Further, it is the Board's philosophy that the assets owned by the participating systems and managed by the Board are held for the exclusive purpose of providing benefits to the participants and annuitants of the respective retirement systems and their beneficiaries.

In line with this philosophy, the Board from time to time evaluates its asset allocation which is considered by many to be the single most important factor in pension investment management. The three major assets classes are: bonds, equities and cash; with smaller positions being allocated to real estate, venture capital and other alternative investments.

Total Fund Results

Based on recent performance, a 2.5% rate of return seems rather insignificant. However, in reflecting on the economic environment over the twelve months, we believe a positive rate of return of even a slight amount is a significant achievement. In fact, the Fund was in the top half in performance by public funds during the last fiscal year. Although the stock market has recovered a portion of its prior loss, the fact that the Fund was well diversified enabled it to weather the crisis. Having commitments to fixed income securities and real estate created a stabilizing effect on the total portfolio and the positive returns from these sectors enabled the Fund to achieve a 2.5% return.

When viewed over a longer time frame, the Fund has produced a total rate return of 11.6% and 9.9% for the three and five year periods, respectively, ending June 30th. To date, the Fund has achieved its stated goal of producing a total return of 1½% to 3% in excess of the actuarial assumption used by the three retirement systems.

No major changes were made in asset allocation during the fiscal year. The Board did, however, diversify the fixed income portfolio with the addition of two new disciplines; namely, convertible bonds and high-yield bonds. After a search, the Board appointed Calamos Asset Management and Morgan Asset Management as convertible bond managers and Delaware Asset Management and Fidelity Management Trust to oversee the high-yield bond area.

Fixed Income Results

The bond portion of the portfolio contains all fixed income securities which have a maturity of one year or longer. While the fixed income market experienced a fair amount of volatility during the fiscal year, the Fund's fixed income segment produced a 9.3% total return. This figure compares very favorably as measured against the Shearson/Lehman Government Corporate Index return of 7.5%. The Board, this year, adopted an additional measure of performance for fixed income; namely, the Shearson/Lehman Aggregate Bond Index. This index includes mortgage securities (about 20% of the index) and, inasmuch as the Fund's fixed income portfolio contains approximately a similar amount of mortgage securities, it was deemed appropriate to add the additional performance standard.

Comparative rates of return of the Board's fixed income portfolio and the two indices are set forth below.

	One Year	Three Years	Five Years
ISBI	9.3%	10.8%	12.4%
Shearson Lehman G/C	7.5	10.7	12.2
Shearson Lehman A/G	8.1	11.0	12.6

Equity Results

The Board made no major changes in its equity management during the fiscal year. A comprehensive analysis is being undertaken as of the completion of this fiscal period which is the end of the three-year cycle since the Board realigned the equity management. The results of this strategic planning study will be the basis for the Board's review which will be conducted in fiscal year 1989.

As previously noted, the October crash of the stock market heavily impacted the overall performance of the equity segment of the portfolio. However, the Fund's equities, on a relative comparison, outperformed the benchmark of the S & P 500 by 2.3%. The Fund's equities were down 4.6% during the fiscal year, while the S & P 500 was off 6.9% for the same period. During the later part of the year, the Fund's position in small capitalization companies added to the performance; as those stocks had a more material come back than the rest of the market.

The total return generated by the equity segment of the portfolio for one, three, and five years is as follows:

	One Year	Three Years	Five Years
ISBI	−4.6%	12.8%	7.7%
S & P 500	−6.9	15.1	13.7

Real Estate and Venture Capital

Since 1981, the Fund has made a substantial commitment in the real estate market. All real estate investments are made through commingled funds and trusts, primarily of the closed-end style. During the fiscal year, the Board added one new investment with a commitment to the JMB/Cadillac Fairview acquisition. This investment increased exposure to the retail segment of the real estate market and brought further diversification through that entities' interests in Canadian real properties. During the fiscal year, a comprehensive review of the real estate portfolio was conducted at the Board's direction. The results of the review indicated through its investments over the past seven years, the Board has achieved a well diversified, high-quality real estate portfolio. Inasmuch as a substantial portion of the real estate investments are relatively new in duration, it is difficult to assess performance results; however, the Board has begun to receive cash flow from several of these investments. The total return reported by four of the major funds range from 6.1% to 11.1% for fiscal 1988.

The Board continued to review investments in the venture capital/LBO area. During the fiscal year, Prudential Venture Capital Limited Partnership II, a latter stage venture capital partnership, was added to the portfolio; as was Corporate Partners, a partnership headed by Lazard Freres. These two investments compliment the established portfolio and bring the venture/LBO segment to 2.2% of the total portfolio.

Management Expense

For this fiscal year, the ISBI operating expenses were $6,059,008, as compared to $5,023,977, for the past year. The major expenses are investment management fees which are tied to the value of the assets under management. The expense ratio (expense versus the assets under management) remained the same 2/10ths of 1%, which is below the norm for funds of their size. The State Employees' Retirement System's share to total operating expenses amounted to $5,640,897.

Additional Information

For additional information regarding the System's investment function, please refer to the Annual Report of the Illinois State Board of Investment, June 30, 1988. A copy of the report can be obtained from the Board at 180 North LaSalle Street, Suite 2015, Chicago, Illinois 60601.

INVESTMENT PORTFOLIO SUMMARY

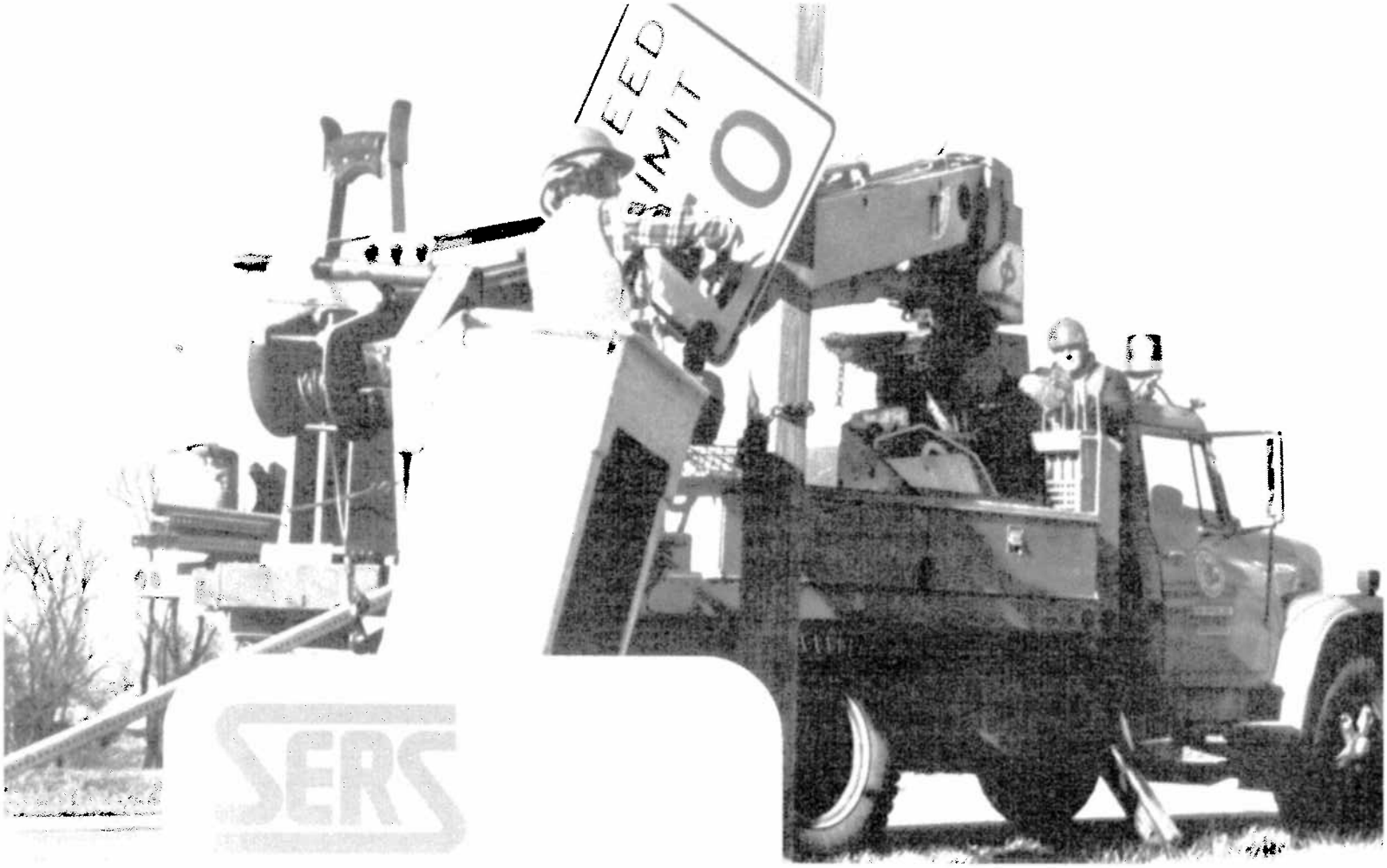
	June 30, 1988 Market Value	Percentage	June 30, 1987 Market Value	Percentage
Bonds	$ 1,100,732,282	41.2%	$ 981,127,321	37.8%
Equities	1,067,817,434	40.0	1,128,660,275	43.5
Cash	162,488,906	6.1	265,296,427	10.2
Real Estate	254,227,296	9.5	175,289,410	6.7
Venture Capital	57,642,361	2.2	27,509,451	1.1
	$ 2,642,908,279	99.0	$ 2,577,882,884	99.3
Other assets, less liabilities	26,276,144	1.0	19,124,773	.7
Net assets at market value	$ 2,669,184,423*	100.0	$2,597,007,657*	100.0
Net assets, at cost	$ 2,542,296,711*		$ 2,376,677,864*	

*These amounts represent the total assets under management of the Illinois State Board of Investment. The assets of the State Employees Retirement System at market and cost for fiscal year 1988 were $2,485,230,297 and $2,367,063,722, respectively. For fiscal year 1987 the market and cost values were $2,416,626,806 and $2,211,906,317, respectively.

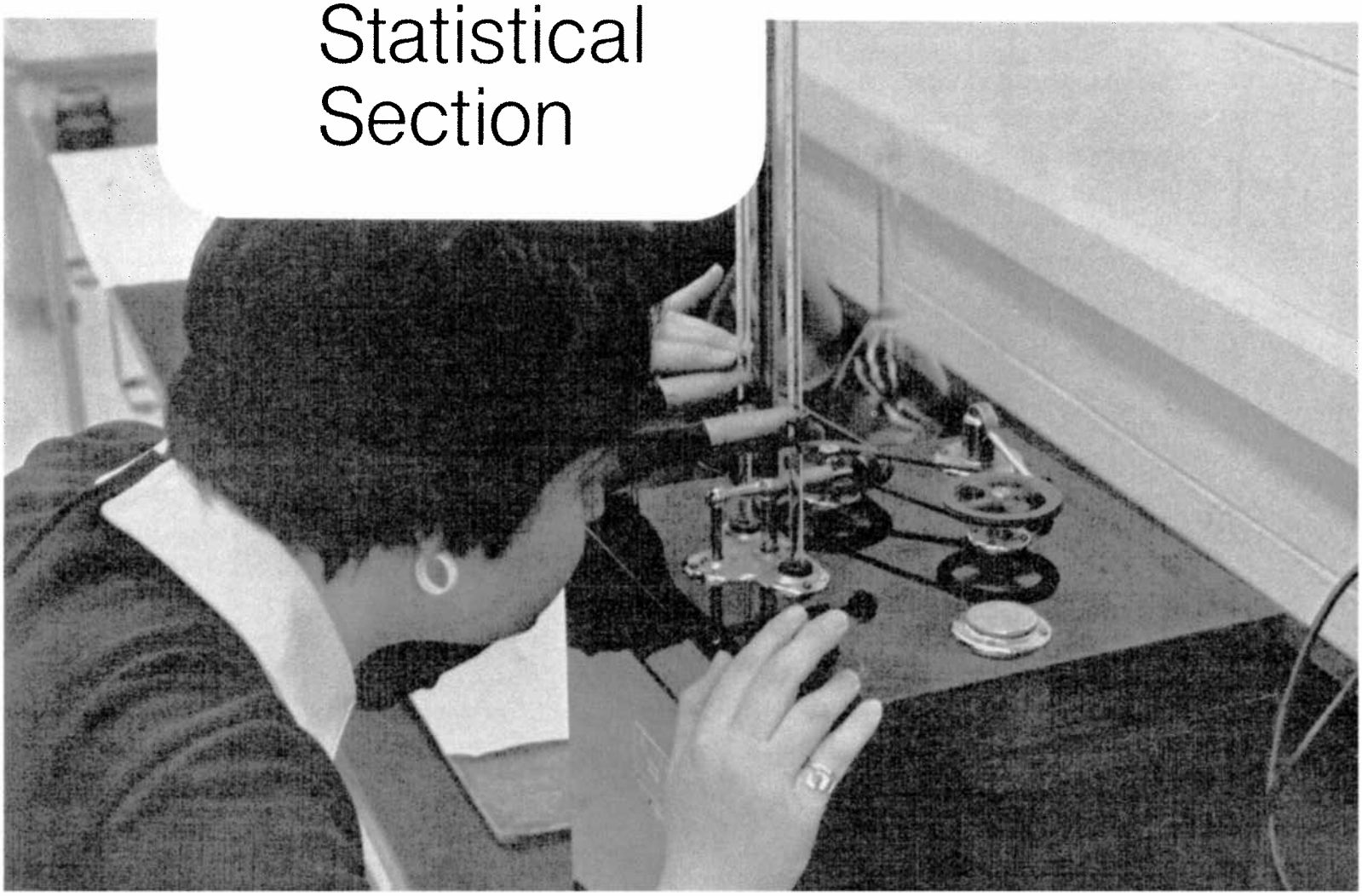
ANALYSIS OF INVESTMENT PERFORMANCE

	1988	1987	1986	1985	1984
Total Return* - Past 3 years	11.6%				
Total Return* - Past 5 years	9.9%				
Total Return* - year by year	2.5%	8.8%	24.6%	22.0%	(5.2)%
Actuarial Assumed Rate of Return	8.0%				7.5%
Average Net Income Yield*	5.6%	5.3%	6.4%	7.3%	7.3%
Comparative rates of return on fixed income securities					
Total fixed income — ISBI	9.3	5.7	17.9	34.9	(0.7)
Comparison index: Shearson Lehman Government/ Corporate Bond Index	7.5	4.7	20.6	28.7	1.8
Comparative rates of return on equities					
Total equities - ISBI	(4.6)	14.4	36.5	15.8	(12.9)
Comparison index: S & P 500	(6.9)	25.1	35.7	30.7	(4.7)

*Total return is the combined effect of income earned and market appreciation (depreciation). Average net income yield is the income earned for the year divided by the average market value of assets employed.



Statistical Section



EXPENSES BY TYPE — SYSTEM TRUST FUND*

FY Ended June 30	Benefits	Contribution Refunds	Administrative Expenses	Other Expenses**	Total
1979	$ 76,000,765	$12,344,851	$1,456,878		$ 89,802,494
1980	81,342,048	12,328,329	1,752,078	$2,460,525	97,882,980
1981	89,147,299	12,352,136	1,973,475	5,034,562	108,507,472
1982	100,453,675	13,942,805	2,245,727	(2,480,124)	114,162,083
1983	111,852,846	14,009,169	2,290,492		128,152,507
1984	120,996,071	14,145,496	2,428,623		137,570,190
1985	132,316,478	13,240,326	2,552,452		148,109,256
1986	143,548,518	13,780,843	2,848,181		160,177,542
1987	159,614,328	12,182,099	3,000,932		174,797,359
1988	173,644,549	11,983,814	3,169,935		188,798,298

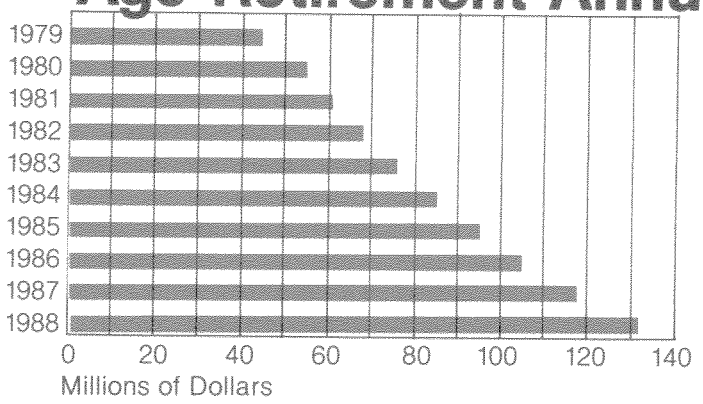
*These amounts do not include the General Revenue Fund Appropriations for the administrative expenses of the Contribution Fund.

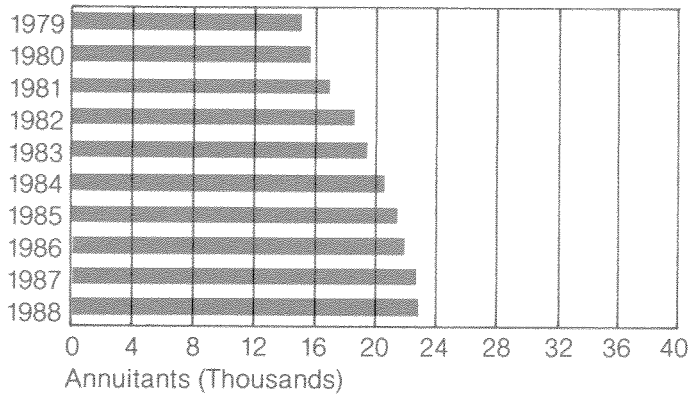
**Net realized loss or (gain) on investments undistributed by the Illinois State Board of investment. Accumulated net losses from 1970 through 1979 amounted to $42,998,251. Since 1982 realized losses or gains have been distributed annually.

BENEFIT EXPENSES BY TYPE — SYSTEM TRUST FUND

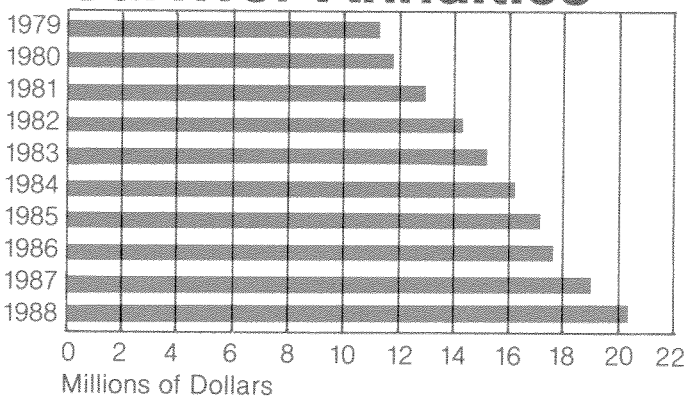
FY Ended June 30	Retirement Annuities	Survivors Annuities	Disability Benefits	Lump Sum Death Benefits	Total
1979	$ 50,360,362	$11,249,401	$11,481,378	$2,909,624	$ 76,000,765
1980	55,063,529	11,902,744	11,327,382	3,048,393	81,342,048
1981	60,675,795	12,939,271	11,598,809	3,933,424	89,147,299
1982	68,602,104	14,236,031	13,163,602	4,451,938	100,453,675
1983	77,472,708	15,253,035	14,101,575	5,025,528	111,852,846
1984	86,651,697	16,114,837	13,985,426	4,244,111	120,996,071
1985	95,965,469	17,086,453	14,164,732	5,099,824	132,316,478
1986	106,475,314	17,856,166	14,452,304	4,764,734	143,548,518
1987	119,758,023	18,955,079	14,521,296	6,379,930	159,614,328
1988	132,265,411	20,319,659	14,660,199	6,399,280	173,644,549

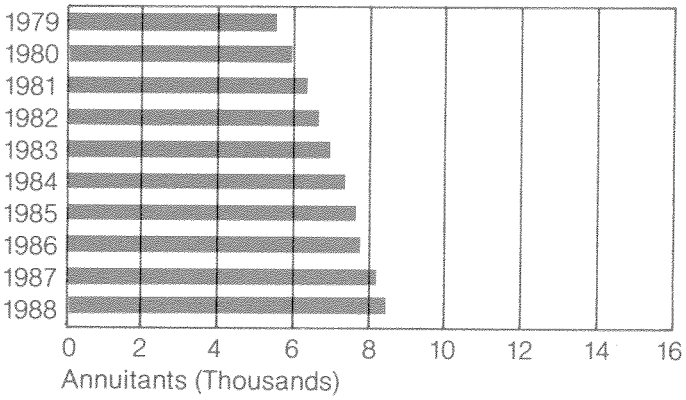
Age Retirement Annuities



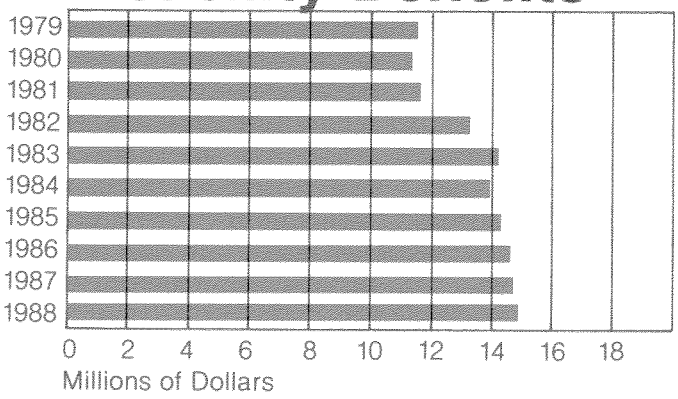


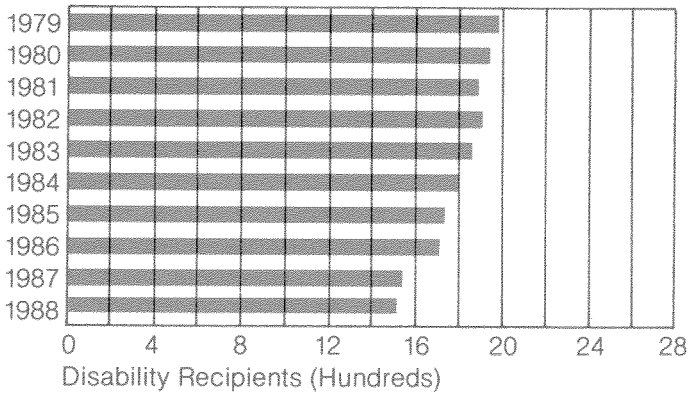
Survivor Annuities



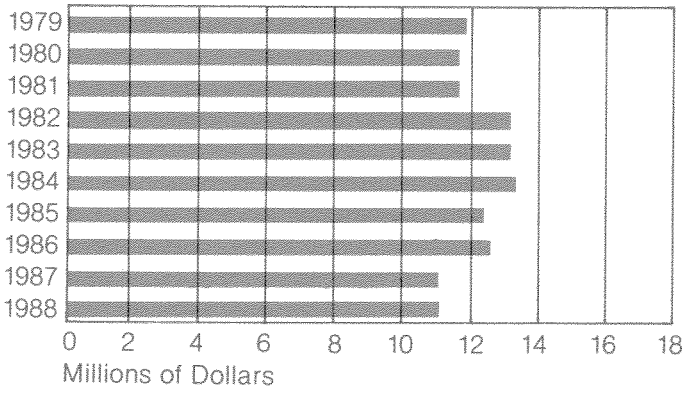


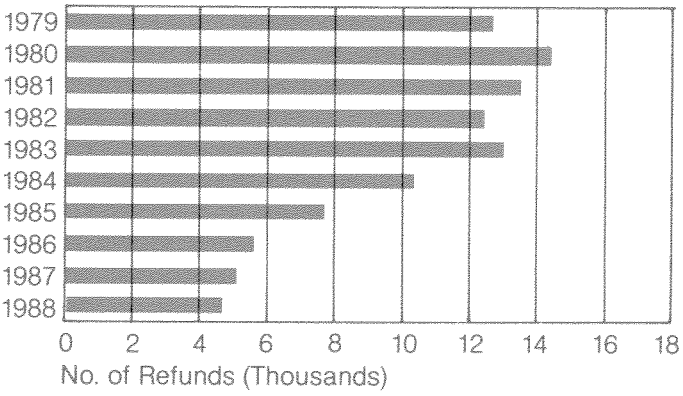
Disability Benefits





Termination Refunds





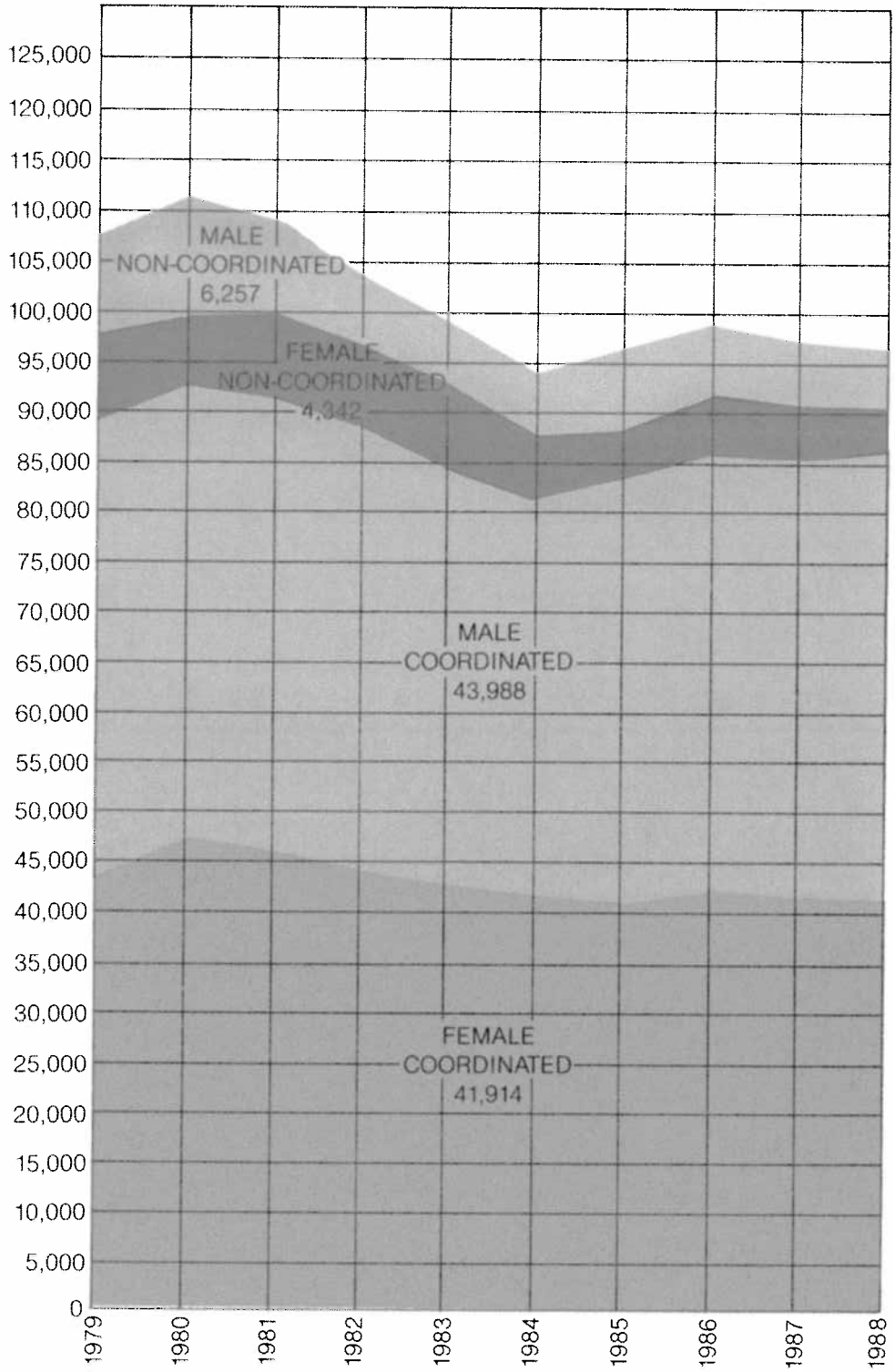
TOTAL MEMBERSHIP — COORDINATED/NONCOORDINATED

FY Ended June 30	COORDINATED MEMBERS			NONCOORDINATED MEMBERS			Total Male Members	Total Female Members	Total Members
	Male	Female	Total	Male	Female	Total			
1979	45,310	43,705	89,015	9,824	9,109	18,933	55,134	52,814	107,948
1980	46,029	46,626	92,655	9,339	8,446	17,785	55,368	55,072	110,440
1981	45,713	46,153	91,866	8,876	7,775	16,651	54,589	53,928	108,517
1982	43,764	44,376	88,140	8,315	7,096	15,411	52,079	51,472	103,551
1983	42,009	42,122	84,131	8,024	6,585	14,609	50,033	48,707	98,740
1984	40,547	40,136	80,683	7,338	5,915	13,253	47,885	46,051	93,936
1985	42,349	40,966	83,315	6,977	5,415	12,392	49,326	46,381	95,707
1986	43,762	41,935	85,697	6,716	4,997	11,713	50,478	46,932	97,410
1987	43,865	41,736	85,601	6,416	4,631	11,047	50,281	46,367	96,648
1988	43,988	41,914	85,902	6,257	4,342	10,599	50,245	46,256	96,501

ACTIVE MEMBERSHIP — COORDINATED/NONCOORDINATED

FY Ended June 30	COORDINATED MEMBERS			NONCOORDINATED MEMBERS			Total Male Members	Total Female Members	Total Active Members	Annual Earnings Reported
	Male	Female	Total	Male	Female	Total				
1979	29,144	31,695	60,839	8,763	8,259	17,022	37,907	39,954	77,861	$1,069,885,900
1980	30,482	34,095	64,577	8,392	7,605	15,997	38,874	41,700	80,574	1,137,667,500
1981	30,462	33,642	64,104	7,991	7,035	15,026	38,453	40,677	79,130	1,253,016,000
1982	29,801	33,100	62,901	7,517	6,486	14,003	37,318	39,586	76,904	1,334,262,000
1983	28,868	31,229	60,097	7,037	5,916	12,953	35,905	37,145	73,050	1,378,735,000
1984	27,457	29,488	56,945	6,636	5,394	12,030	34,093	34,882	68,975	1,437,546,000
1985	29,763	30,583	60,346	6,349	4,952	11,301	36,112	35,535	71,647	1,569,532,000
1986	31,486	31,832	63,318	6,135	4,559	10,694	37,621	36,391	74,012	1,713,755,000
1987	32,294	32,270	64,564	5,924	4,244	10,168	38,218	36,514	74,732	1,825,196,000
1988	32,567	32,570	65,137	5,804	3,982	9,786	38,371	36,552	74,923	1,953,960,000

Total membership — Coordinated/Noncoordinated



NUMBER OF RECURRING BENEFIT PAYMENTS — SYSTEM TRUST FUND

FY Ended June 30	Retirement Annuities	Survivors' Annuities	Disability* Benefits	Total
1979	15,560	5,894	1,976	23,430
1980	16,445	6,187	1,927	24,559
1981	17,307	6,485	1,871	25,663
1982	18,247	6,863	1,888	26,998
1983	19,306	7,139	1,851	28,296
1984	20,157	7,371	1,799	29,327
1985	20,969	7,626	1,734	30,329
1986	21,771	7,823	1,703	31,297
1987	22,529	8,015	1,577	32,121
1988	23,038	8,296	1,536	32,870

*Includes individuals receiving total temporary disability payments under the Workers' Compensation Act.

TERMINATION REFUNDS — NUMBER/AMOUNT — SYSTEM TRUST FUND

1979	14,354	$11,900,531
1980	13,449	11,799,600
1981	12,171	11,810,898
1982	12,893	13,212,484
1983	10,252	13,149,550
1984	7,664	13,349,332
1985	5,638	12,339,874
1986	5,118	12,587,868
1987	4,930	11,192,197
1988	4,431	11,015,216

RETIREMENT ANNUITIES — SYSTEM TRUST FUND
Average Monthly Benefit By Type

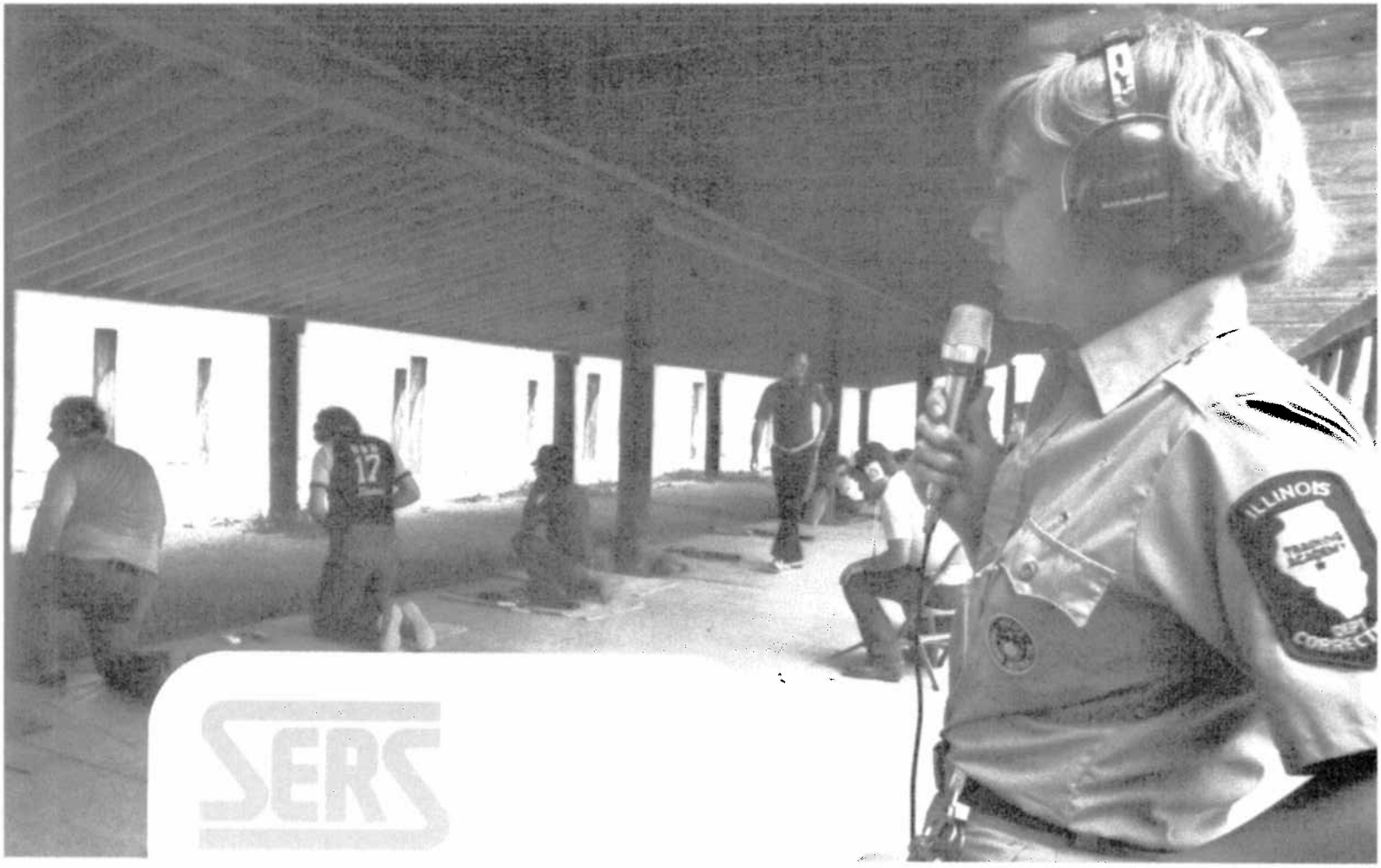
	Fiscal Year Ending June 30 1988	1987	1986	1985	1984
Not Coordinated with Social Security	$ 924.09	$ 830.86	$ 803.52	$ 693.20	$ 664.83
Coordinated with Social Security	347.06	325.96	300.00	274.50	260.98
Alternative Formula	2,340.52	2,134.07	1,973.15	1,755.84	1,530.09
Dept. of Corrections — Special Formula — Not Coordinated with Social Security	1,370.91	1,126.09	1,273.90	932.42	745.38
Dept. of Corrections — Special Formula — Coordinated with Social Security	891.39	993.61	845.20	429.15	283.50
Total Average	$ 251.41	$ 248.60	$ 248.99	$ 242.46	$ 239.52

RETIREMENT ANNUITIES — SYSTEM TRUST FUND
Current Age of Active Recipients

Age	Fiscal Year Ending June 30 1988	1987	1986	1985	1984
Under 51	2	6	13	5	3
51-55	196	189	166	146	118
56-60	700	714	666	436	411
61-65	3,684	3,623	3,549	3,064	2,898
66-70	5,628	5,522	5,468	5,343	5,378
71-75	5,478	5,508	5,393	5,382	5,124
76-80	4,018	3,839	3,596	3,558	3,363
81-85	2,095	1,974	1,853	1,896	1,778
86-89	805	754	688	728	720
Over 89	432	400	379	411	364
Total	23,038	22,529	21,771	20,969	20,157
Average age	72.19	72.05	71.97	72.45	72.38

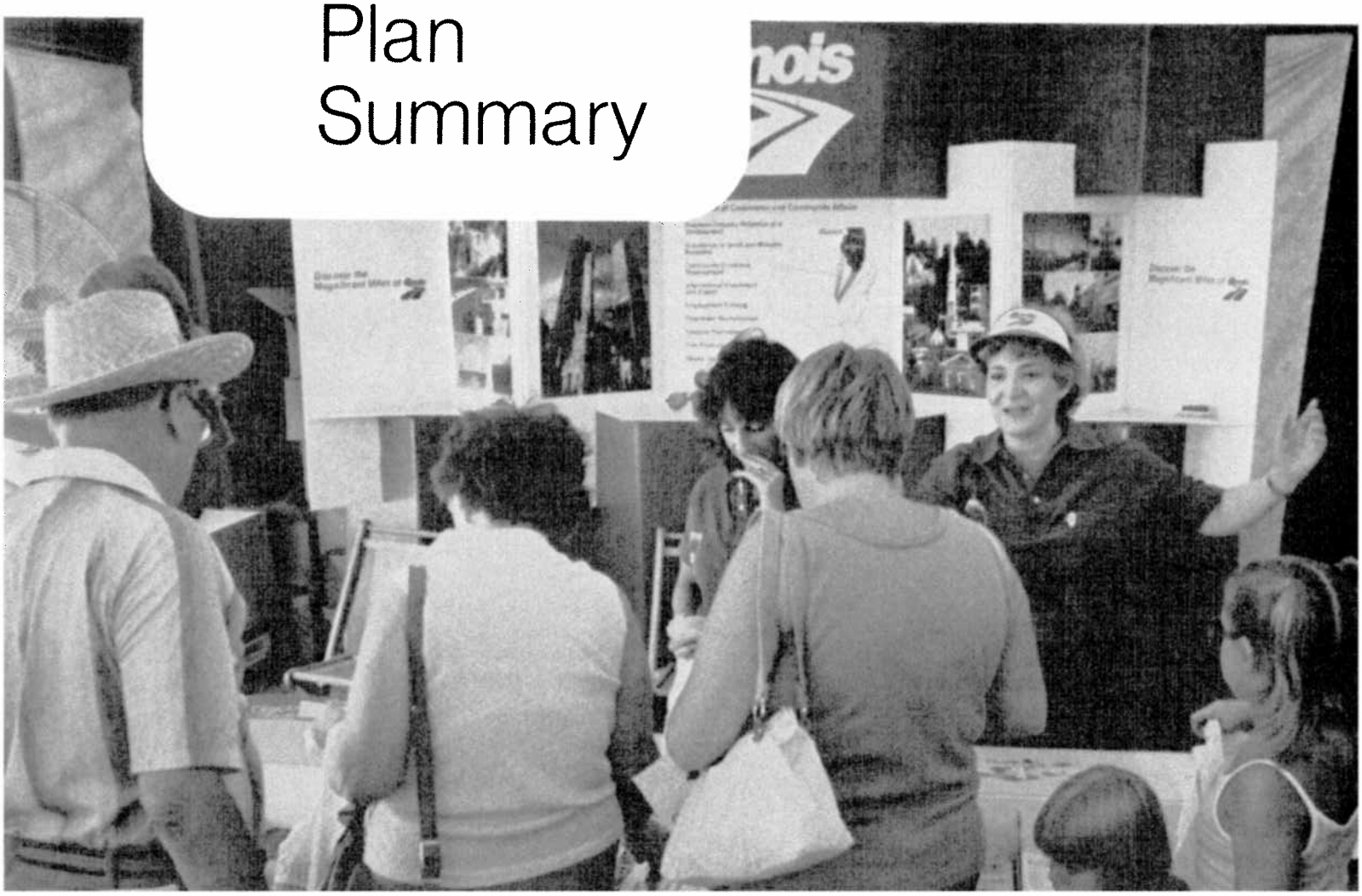
RETIREMENT ANNUITIES — SYSTEM TRUST FUND
Average Service (in months) at Effective Date of Benefit

	Fiscal Year Ending June 30 1988	1987	1986	1985	1984
Not Coordinated with Social Security	316.25	306.72	310.73	298.34	293.96
Coordinated with Social Security	198.45	194.84	191.48	184.97	180.19
Alternative Formula	340.07	342.90	330.02	326.40	313.42
Dept. of Corrections — Special Formula — Not Coordinated with Social Security	323.25	296.43	332.75	296.73	276.69
Dept. of Corrections — Special Formula — Coordinated with Social Security	272.34	261.44	283.84	204.36	177.35
Total Average	251.41	248.60	248.99	242.46	239.52



SERS

Plan Summary



SUMMARY OF RETIREMENT SYSTEM PLAN
(As of June 30, 1988)

1. PURPOSE

The State Employees' Retirement System of Illinois, a state agency, provides an orderly means whereby aged or disabled employees may be retired from active service without prejudice or hardship and enables the employees to accumulate reserves for old age, disability, death and termination of employment.

2. ADMINISTRATION

Responsibility for the operation of the System and the direction of its policies is vested in a Board of Trustees consisting of seven members. The administration of the detailed affairs of the System is the responsibility of the Executive Secretary who is appointed by the Board of Trustees. Administrative policies and procedures are designed to insure an accurate accounting of funds of the System and prompt payment of claims for benefits within the applicable statute.

3. EMPLOYEE MEMBERSHIP

All persons entering state service become members of the System after serving a six-month qualifying period unless their position is subject to membership in another state supported system. Any enrollee of the Young Adult Conservation Corps is excluded from membership. Employees appointed by the Governor and requiring confirmation by the State of Illinois Senate may elect to become members of the System.

4. MEMBER CONTRIBUTIONS

Members are required to contribute a percentage of salary as their share of meeting the cost of the various benefits. Contribution rates are as shown below:

A. Members Coordinated With Social Security - 4% of Salary

B. Members Without Social Security - 8% of Salary

C. State Police, Special Agents, Firefighters, Secretary of State Investigators, Conservation Police Officers, Department of Revenue Investigators, Central Management Services Security Police and Mental Health Police Officers - 9½% of Salary

D. Full Time Security Employees of the Department of Corrections; Air Pilots —
   (1) Coordinated with Social Security - 5½% of Salary
   (2) Without Social Security - 9½% of Salary

Members coordinated with social security also pay the current social security tax rate.

5. RETIREMENT PENSION

A. Qualification of Member

Upon termination of state service, a member is eligible for a pension at age 60 with at least eight years of pension credit; at any age with 35 or more years of credit; between ages 55 and 60 with 30 to 35 years of credit with the pension reduced by one-half of 1% for each month the member is under age 60. Department of Corrections security employees not eligible for the Alternative Formula must have at least 20 years of membership service to qualify for the special pension formulas which will apply only to the service earned while in a security position.

Members in Alternative Formula positions are eligible at age 50 with at least 25 years of eligible creditable service or at age 55 with at least 20 years of eligible creditable service in such a position.

Department of Corrections security employees are eligible at age 55 with at least 25 years of eligible creditable service in a security position. These employees will be eligible at age 50 with at least 25 years of eligible creditable service or age 55 with at least 20 years of eligible creditable service when the Alternative Formula is fully phased in over a five year period that began in 1985.

B. Amount of Pension

The pension is based on the member's final average compensation and the number of years of pension credit that has been established.

The pension formula reflects a graded or progressive method according to length of service as follows:

Years of Credit	Employees Under Social Security	Employees Not Under Social Security	Full Time Security Employees — Dept. of Corrections* Under S.S./Not Under S.S.		Alternative Formula, i.e. Police and other positions Under S.S./Not Under S.S.	
Each of the first 10 years of credit	1.0%	1.67%	1.67%	1.9%	1.67%	2.25%
Each of the next 10 years of credit	1.1%	1.9%	1.9%	2.1%	1.9%	2.5%
Each of the third 10 years of credit	1.3%	2.1%	2.1%	2.25%	2.1%	2.75%
Each year above 30	1.5%	2.3%	2.3%	2.5%	2.3%	2.75%

*Who are not eligible for the Alternative Formula. The Alternative Formula for the Department of Corrections employees will be fully phased in by 1991.

The maximum pension payable is 75% of final average compensation. The minimum pension payable is $7.50 for each year of covered employment and $15.00 for each year of noncovered employment.

C. Optional Forms of Payment

Reversionary Annuity — A member may elect to receive a smaller pension during his lifetime in order to provide a spouse or a designated dependent with a lifetime income. That payment would be in addition to any other benefit payable by the System.

Level Income — A member who contributes to social security as a state employee may elect to have his pension payments increased before age 62/65 and reduced after that age to provide a uniform pension income throughout his retired life. To be eligible for this election the member must have established eligibility for a social security pension.

D. Annual Increases in Pension

Post retirement increases of 3% of the original pension are granted to members effective each January 1 after receipt of benefits for one full year.

6. SURVIVORS' ANNUITY

A. Qualification of Survivor

If death occurs while in state employment, the member must have established at least 18 months of pension credit. If death occurs after termination of state service and the member was not receiving a retirement pension, the member must have established at least eight years of pension credit.

An eligible spouse qualifies at age 50 or at any age if there is in the care of the spouse any unmarried children of the member under age 18 or over 18 if mentally or physically disabled; unmarried children under age 18 if no spouse survives; dependent parents at age 50 if neither an eligible spouse nor eligible children survive the member.

A spouse that is the sole nominated beneficiary and sole survivor may elect other death benefits in number 9 on page 59.

B. Amount of Payment

If the member's death occurs before retirement, the named beneficiary receives a lump sum refund of all the member's pension contributions plus interest credited to the member's account, excluding contributions for widow and survivors benefits. A single lump sum payment of $1,000 is also made immediately to the survivor beneficiary of the member.

An eligible spouse receives a monthly annuity equal to 30% of the member's final average compensation subject to a maximum of $400. If children of the member are under the care of the spouse, the annuity is increased for each child, subject to a maximum of $600 or 80% of final average compensation. If only eligible children survive, the monthly annuity may not exceed the lessor of $600 or 80% of final average compensation. The maximum combined monthly payment to parents may not exceed $400. If the member's death occurs after retirement or after termination of state employment but before the member receives a pension, the monthly benefit is the same as during active employment or 80% of the earned pension at date of death. Monthly benefits payable to survivors of a member who was covered by social security as a state employee are reduced by one-half of the amount of benefits they are entitled to from social security as a widow(er). The minimum total survivor benefit payable to the survivors' annuity beneficiaries of a deceased member or annuitant shall be 50% of the amount of retirement annuity that was or would have been payable to the deceased member on the date of death. If the minimum total benefit exceeds the maximum described above, the minimum shall be payable.

C. Duration of Payment

The monthly annuity payable to a spouse terminates upon death or remarriage prior to attainment of age 55; to children upon death, marriage, or attainment of age 18, except for a child who at age 18 is physically or mentally disabled and unable to accept gainful employment, which terminate at death or gainful employment. Dependent parents' benefits terminate at death or remarriage.

7. WIDOW'S ANNUITY OPTION

The widow of a male member who was a participant in the System prior to July 19, 1961, may have the option of taking a Widow's Annuity rather than the Survivor's Annuity.

A. Qualification of Widow

An eligible widow receives a Widow's Annuity if she is age 50 or over or has in her care any of the member's unmarried children under age 18. If she is not age 50 and has no such children in her care, she becomes eligible at age 50.

B. Amount of Payment

The Widow's Annuity consists of a lump sum payment of $500, plus a monthly annuity equal to 50% of the pension earned or received by the member at the date of death. If the widow has in her care eligible children of the member, the monthly annuity is increased 5% because of each child, subject to a maximum payment equal to 66⅔% of the earned pension. Monthly benefits payable to a widow of a member who was covered by Social Security as a state employee are reduced by one-half of the amount of benefits she is entitled to from social security as a widow.

C. Duration of Payment

The monthly payment to the widow continues for her lifetime whether or not she remarries. If the amount of benefit was increased because of eligible children, it is adjusted downward as these children's benefits are terminated (death, marriage or attainment of age 18).

8. OCCUPATIONAL DEATH BENEFIT

A. Qualification of Survivors

If a member's death results from an injury on the job or a job related cause, the spouse may be eligible for an Occupational Death benefit. If only unmarried children under age 18 survive, they may be eligible for the benefit. If neither spouse nor eligible children survive, a dependent father or mother may be eligible.

B. Amount of Payment

The nominated beneficiary receives a lump sum payment consisting of all contributions made by the member plus interest credited to the member's account. A surviving spouse is entitled to a monthly benefit equal to 50% of the member's final average compensation. If children under age 18 also survive, the annuity is increased by 15% of such average because of each child sub-

ject to a maximum of 75%. If there is no eligible spouse and children under 18 survive, each child receives a monthly allowance of 15% of final average compensation. The combined payment to children may not exceed 50% of the member's final average compensation. If there is no eligible spouse or eligible children, a benefit of 25% of final average compensation is payable to each surviving dependent parent for life. The monthly benefit is reduced by any payments awarded under the Workers' Compensation or Occupational Diseases Acts.

C. Duration of Payment

The monthly annuity payable to a spouse terminates at death, or remarriage before age 55; to children at death, or attainment of age 18, or marriage.

9. OTHER DEATH BENEFITS

If the beneficiaries of the member do not qualify for any of the previously described death benefits, one of the following benefits is payable.

A. Before Retirement

If a member's death occurred while in state service the benefit consists of: (1) a refund of all contributions plus interest credited to the member's account; (2) a payment equal to one month's salary for each full year of pension credit not to exceed six month's salary. The minimum payment is equal to one month's salary.

If the member had terminated state service but not yet qualified for a pension, the benefit consists of a refund of all of the member's contributions to the System plus the interest credited to the member's account.

B. After Retirement

The benefit consists of a lump sum payment equal to the excess of contributions plus interest credited to the member's account over the total amount of pension payments made to the member. The minimum payment is $500.

10. NONOCCUPATIONAL DISABILITY BENEFITS

A. Qualification and Amount of Payment

Available to any member under age 70 who has established at least one and one-half years of creditable service and who has been granted a disability leave of absence by the employing agency. The benefit is 50% of final average compensation plus a credit to the member's account of service and contributions. It begins on the 31st day of absence from service on account of disability.

If the member has social security coverage as a state employee, the benefit payable by the System is reduced by the amount of any disability or retirement payment to which he is entitled under social security.

B. Duration of Payment

The member is eligible for the monthly benefit until the occurrence of any of the following events: (1) disability ceases; (2) resumption of gainful employment; (3) payments are made for a period of time equal to one-half of the pension credit established as of the date disability began; or (4) attainment of age 65, if benefit commenced prior to the attainment of age 50; or (5) the fifth anniversary of the effective date of the benefit if the benefit commenced on or after the attainment of age 60, but not beyond age 70; or (6) death of the member.

11. OCCUPATIONAL DISABILITY BENEFIT

A. Qualification and Amount of Payment

Provided for any member under age 70 who becomes disabled as the direct result of injury or disease arising out of and in the course of state employment.

The benefit is 75% of final average compensation plus a credit to the member's account of service and contributions. The cash benefit is reduced by any payment received under the Workers'

Compensation or Occupational Diseases Acts.

B. Duration of Payment

Monthly benefits are payable until the occurrence of any of the following events; (1) disability ceases; (2) resumption of gainful employment; or (3) attainment of age 65, if benefit commenced prior to the attainment of age 60; or (4) the fifth anniversary of the effective date of the benefit if the benefit commenced on or after the attainment of age 60, but not beyond age 70; or (5) death of the member.

12. TEMPORARY DISABILITY BENEFIT

A. Qualification and Amount of Benefit

Available to any member under age 70 who becomes disabled, has established at least one and one-half years of creditable service, has been denied benefits under the Workers' Compensation Act or the Workers' Occupational Diseases Act, and has filed an appeal with the Industrial Commission of Illinois. The benefit is 50% of final average compensation plus credit to the member's account of service and contributions. The benefit shall begin to accrue on the 31st day of absence from service and shall be payable upon the expiration of 180 days from the day the member last received compensation.

If the member has social security coverage as a state employee, the benefit payable by the System is reduced by the amount of any disability or retirement payment to which he is entitled to under social security.

B. Duration of Payment

The member is eligible for the monthly benefit until the occurrence of any of the following events: (1) disability ceases; (2) resumption of gainful employment; (3) payments are made for a period of time equal to one-half of the pension credit established as of the date disability began; or (4) attainment of age 65, if the benefit commenced prior to the attainment of age 60; or (5) the fifth anniversary of the effective date of the benefit if the benefit commenced on or after the attainment of age 60, but not beyond age 70; or (6) death of the member.

13. SEPARATION BENEFITS

Upon termination of state employment a member may obtain a refund of the contributions made to the System. By accepting a refund, a member forfeits all accrued rights and benefits in the System for himself and his beneficiaries.

LEGISLATION

LEGISLATIVE AMENDMENTS - Amendments with an effective date during fiscal year 1988 having an impact on the System were:

HOUSE BILL 2715

This bill allowed for transfer of service from this System to the County Employees' and Benefit Fund and Sanitary District Employees' Benefit Fund.

HOUSE BILL 2712

Excludes from membership any member of the Illinois Health Care Cost Containment Council. Defines retroactive pay adjustment as payment for employment where service credit has already been established. Defines an award for back pay under a statute as payment for employment where service credit was not already established. Permits members of the Judges' Retirement System to establish credit with this System.

NEW LEGISLATION - Amendments with an effective date subsequent to June 30, 1988, affecting the operation of the System.

SENATE BILL 236

Allows a county sheriff under Article 7 to transfer up to 5 years of credit from this System to the Article 7 fund.