

**2012**  
Summary  
Annual  
Financial  
Report



Funds of the State of Washington  
for the Year Ended June 30, 2012



Elated Customers. Best Practice Leader.  
Vigilant Resource Steward. Reliable Partner.  
Engaged Team Members.

Short and simple words, but powerful. They are the key goals we strive for in fulfilling our mission to ensure DRS' customers prepare for and enjoy a successful retirement.

These goals capture the essence of everything we do here at DRS. How do we know? Over the past several months, we've "mapped" DRS' core business processes to clearly identify our

fundamental work and how it supports the goals. It helps all team members connect their work to customer satisfaction, and it helps us identify opportunities for improvement.

Business mapping is one of several initiatives of the past year that move us toward our key goals. Others include:

- Customers can now apply for retirement online thanks to a new application launched in April. Modeled on popular online services for tax preparation, the application flows users through a series of user-friendly submittal screens. More than 23 percent of retirement applications are now being submitted online, and that number is growing.
- Working with the Washington State Investment Board and other partners, we assisted thousands of customers in transitioning to a new lineup of investment fund options for the state's hybrid defined contribution plans and the deferred compensation program. DRS has since received national recognition for its best practices in communicating the fund transition.

- DRS team members interviewed more than 1,100 customers, focusing on the question, "What would it take for you to be 100 percent satisfied as a customer of DRS?" Every team member is now involved in distilling those conversations into a concise set of criteria for customer expectations that will be used to regularly measure customer feedback and incorporate it into service and process improvements.
- Lean principles are being infused into the culture of the organization, providing both a skillset and a mindset that encourages team members to identify constraints, simplify processes and make improvements. More than 40 percent of DRS team members have participated in some form of Lean training, including 19 who are "Green Belt" certified and are already working to counsel teams around the agency on applying the Lean approach to process improvement.

Through these and other initiatives, DRS continues to deliver cost-effective service to our customers. CEM Inc., an international firm that benchmarks the performance of public pension plans, has again determined that DRS' administrative cost is significantly lower than what would be expected, even though Washington's plans are among the most complex in the country to administer.

While we take pride in these initiatives and accomplishments, we recognize they are part of a larger journey toward our key goals. We look forward to continuing the journey in the coming year, with the ultimate aim of excellence in fully meeting the needs and expectations of our customers.

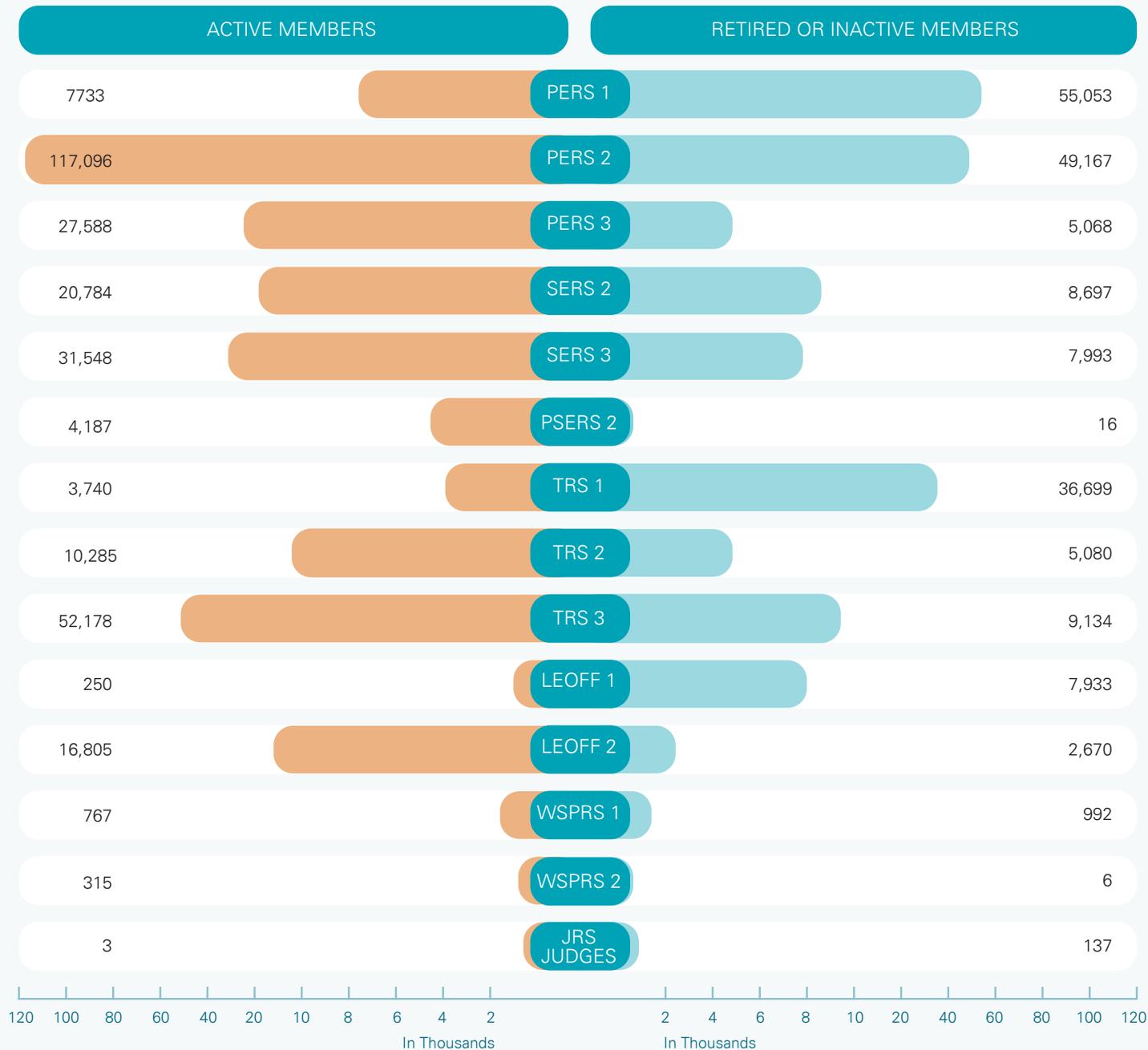
In the following pages, we offer our annual financial report for your review.

A handwritten signature in black ink, appearing to read "Steve Hill". The signature is stylized and cursive.

Steve Hill  
Director  
October 2012

# Membership

Membership by system and plan as of June 30, 2012\*



The State of Washington provides secure retirement plans for public employees. The Department of Retirement Systems manages eight unique pension systems servicing more than 481,000 current, past and retired employees from state and local government, K-12 and higher education systems, fire, law enforcement and judicial agencies.

Active members, who are currently employed and paying contributions toward retirement, comprise 61 percent of the public pension participation. Remaining members are either retired or have separated from service.

\*Source for membership by system and plan is the State Actuary's latest valuation report, published June 30, 2011.

## CTF Investment Returns\*

The Washington State Investment Board (WSIB) manages retirement fund assets to maximize investment returns at a prudent level of risk. Investment decisions are made within the framework of WSIB Strategic Asset Allocation Policy.

During Fiscal Year 2012, the Retirement Funds, collectively called the Commingled Trust Fund (CTF) were allocated among seven asset classes and provided a 1.40 percent rate of return. The CTF annualized rate of return over the last three years was 11.62 percent and 1.17 percent over the last five years.

The table below shows the returns for the CTF on a total fund basis and by asset class:

Asset Class	1 Year	3 Year	5 Year
Liquidity	0.14%	0.16%	1.21%
Innovation	(9.79)%	n/a	n/a
Private Equity	5.26%	17.50%	2.91%
Public Equity	(5.78)%	11.89%	(2.55)%
Real Estate	8.57%	6.10%	(0.46)%
Tangible	2.11%	6.22%	1.77%
Fixed Income	5.51%	8.45%	7.94%
Total fund	1.40%	11.62%	1.17%

## Current Asset Allocation and Long-Term Target Allocations\*

Asset Type	Fixed Income	Tangible Assets	Real Estate	Public Equity	Private Equity	Innovation	Liquidity
Target Allocation	20.54%	1.35%	13.69%	36.27%	26.02%	0.57%	1.56%
Actual Allocation	22.16%	1.35%	13.69%	36.02%	26.02%	0.57%	0.19%

Investment performance is a result of two primary factors: individual asset selection and the allocation of the portfolio among asset classes (e.g. stocks, fixed income, real estate).

Accordingly, the WSIB sets a specific long-term target asset mix and adopts tight ranges around those targets to control the overall risk and return of the CTF. On a daily basis, the board reviews the asset allocation in relation to the established ranges. The staff shifts assets whenever the allocation range for an asset exceeds the approved range or when cash is needed elsewhere. The board reviews changes to the overall asset mix every three to four years.

## Ten Largest Public Equity Holdings\*

Apple Inc.	1.55%
Exxon Mobil Corp.	1.10%
Philip Morris International Inc.	0.69%
Johnson & Johnson	0.68%
Nestle SA	0.65%
Pfizer Inc.	0.64%
IBM Corp.	0.63%
Wells Fargo	0.61%
Novartis AG	0.61%
Microsoft Corp.	0.58%

\*As of June 30, 2012



## Statement of Fiduciary Net Position: Pension trust and other employee benefit trust funds by plan (as of June 30, 2012, expressed in thousands).\*

Assets	PERS Plan 1	PERS Plan 2/3	PERS Plan 3 Defined Contribution	SERS Plan 2/3	SERS Plan 3 Defined Contribution	PSERS Plan 2	TRS Plan 1	TRS Plan 2/3	TRS Plan 3 Defined Contribution	LEOFF Plan 1	LEOFF Plan 2	WSPRS Plan 1/2	JRS	Judges	Defined Contribution	Deferred Compensation	June 30, 2012	June 30, 2011
Cash and Pooled Investments	\$3,158	\$5,796	\$302	\$3,461	\$1,053	\$252	\$3,333	\$5,294	\$4,461	\$1,383	\$1,187	\$762	\$3,499	\$1,874	\$9	\$3,651	\$39,475	\$34,426
Total Receivables	154,487	464,009	24,996	69,282	24,078	5,366	128,494	170,630	85,001	99,404	150,777	18,282	4	-	3	2,498	1,397,311	1,870,917
Total Investments, Noncurrent	7,393,795	20,673,888	1,724,211	2,817,752	1,276,512	172,642	6,207,057	7,069,529	5,155,916	4,913,650	6,637,005	880,050	-	-	12,257	2,931,869	67,866,133	71,067,364
Other Assets	602	349	-	3	-	-	523	111	-	279	46	31	-	-	-	-	1,944	1,670
Total Assets	7,552,042	21,144,042	1,749,509	2,890,498	1,301,643	178,260	6,339,407	7,245,564	5,245,378	5,014,716	6,789,015	899,125	3,503	1,874	12,269	2,938,018	69,304,863	72,974,377
Total Liabilities	175,328	464,254	25,082	63,212	23,795	3,813	147,924	158,318	74,529	110,329	148,322	19,905	32	2	-	2,286	1,417,131	4,662,547
Total Fiduciary Net Position	\$7376,714	\$20,679,788	\$1,724,427	\$ 2,827,286	\$1,277,848	\$174,447	\$6,191,483	7,087,246	\$5,170,849	\$4,904,387	\$6,640,693	\$879,220	\$3,471	\$1,872	\$12,269	\$ 2,935,732	\$67,887,732	\$68,311,830
	Pension Assets Totals															Totals		

### Additions to fiduciary net position

The primary sources of additions to the retirement trust fund include contributions from employers, active system members and the state, and from investment earnings. Additions to the deferred compensation trust fund include participant contributions and investment earnings.

The totals are listed below (expressed in millions).

	Fiscal Year 2012	Fiscal Year 2011
Retirement Contributions	2,210.0	1,923.9
Deferred Compensation Participant Contributions	178.4	186.7
Net Investment Income	784.9	11,929.1
Charges for Services	27.7	28.0
Other Additions	4.0	13.0
Total	3,205.0	14,080.7

\*This is a summary of the Comprehensive Annual Financial Report (CAFR), which is presented consistent with generally accepted accounting principles (GAAP). The CAFR is available on the DRS website. As with the CAFR, the pension trust funds in this summary are presented using the flow of economic resources measurement focus and the accrual basis of accounting. However, this presentation differs from GAAP in the following respects: only selected financial data rather than financial statements are included, and this report only contains abbreviated note disclosures.

The Summary Annual Financial Report represents an accounting of the annual liabilities and required contributions, using methods set by the Governmental Accounting Standards Board. The Valuation (or Funding) Report issued by the State Actuary uses actuarial assumptions and methods prescribed by the Legislature to calculate the contributions that will be required, under existing funding policy, over the life of the plans.

### Deductions to fiduciary net position

The retirement systems' primary fund deductions (excluding transfers) include the payment of benefits to retirees and beneficiaries, the refund of contributions to former members and the cost of administering the retirement systems.

Benefit payments to members, including pension and annuity benefits, totaled \$3,084.4 million for Fiscal Year 2012. Refunds totaled \$509.6 million. Administrative expenses, which include pension expenses incurred by DRS and the offices of the State Actuary and Attorney General, totaled \$29.8 million. Expenses for the management of trust funds are incurred by the Washington State Investment Board and funded from earnings on investments.

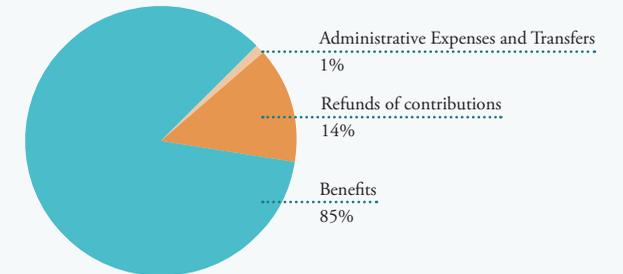


Photo Credit: Skagit Field of Tulips, Debbie Callar, DRS

# Summary of Plan Provisions

	Plan	Membership Eligibility	Vesting	Retirement Eligibility	Benefit
PERS	Plan 1	State employees, elected officials, employees of local governments, legislative committees, community/technical colleges, classified employees of school districts, district/municipal court judges, and some employees of the Supreme, Appeals and Superior Courts. (By 9/30/77)	After five years of eligible service	After 30 years of service, or at age 60 with five years of service, or at age 55 with 25 years of service	2% of average final compensation (AFC) per year of service, capped at 60% of AFC JBM Participants: 3.5% of AFC per year of service, capped at 75% of AFC
	Plan 2	Same as PERS Plan 1, except classified school district employees. (On or after 10/1/77 and new employees on or after 3/1/02 at state agencies and higher education, or on or after 9/1/02 at all other employers; who chose Plan 2)	After five years of eligible service	At age 65 with five years of service, or an actuarially reduced benefit at age 55 with 20 years of service	2% of AFC per year of service JBM Participants: 3.5% of AFC per year of service, capped at 75% of AFC
	Plan 3	Same as PERS Plan 2. (On or after 10/1/77 and new employees on or after 3/1/02 at state agencies and higher education, or on or after 9/1/02 at all other employers; who chose Plan 3)	Varies	At age 65 if vested, or an actuarially reduced benefit at age 55 with 10 years of service (defined benefit portion)	1% of AFC per year of service (defined benefit portion) JBM Participants: 1.6% of AFC per year of service, capped at 37.5% of AFC The defined contribution portion depends on the member's contribution level and on investment performance.
SERS	Plan 2	All classified employees of school districts or educational service districts. (By 8/31/00 and employees on or after 7/1/07 with no past PERS Plan 2 service who chose Plan 2)	After five years of eligible service	At age 65 with five years of service, or an actuarially reduced benefit at age 55 with 20 years of service	2% of AFC per year of service.
	Plan 3	All classified employees of school districts or educational service districts. (On or after 9/1/00 and employees on or after 7/1/07 with no past PERS Plan 2 service who chose Plan 3)	Varies	At age 65 if vested, or an actuarially reduced benefit at age 55 with 10 years of service (defined benefit portion)	1% of AFC per year of service (defined benefit portion) The defined contribution portion depends on the member's contribution level and on investment performance.
PSPERS	Plan 2	All full-time public safety officers at select state agencies, counties and cities except Seattle, Spokane and Tacoma. (On or after 7/1/06)	After five years of eligible service	At age 65 with five years of service, at age 60 with 10 years of PERS service, or at age 53 with 20 years of service reduced three percent for each year under age 60	2% of AFC per year of service
TRS	Plan 1	All certificated public school employees who work in an instructional, administrative or supervisory capacity. (By 9/30/77)	After five years of eligible service	Any age with 30 years of service, or at age 60 with five years of service, or at age 55 with 25 years of service	2% of monthly AFC per year of service, capped at 60% of monthly AFC. JBM Participants: 3.5% of monthly AFC per year of service, capped at 75% of monthly AFC.
	Plan 2	Same as TRS Plan 1. (On or after 10/1/77 and by 6/30/96, and employees on or after 7/1/07 who chose Plan 2)	After five years of eligible service	At age 65 with five years of service, or an actuarially reduced benefit at age 55 with 20 years of service	2% of AFC per year of service.
	Plan 3	Same as TRS Plan 1. (On or after 7/1/96, and employees on or after 7/1/07 who chose Plan 3)	Varies	At age 65 if vested, or an actuarially reduced benefit at age 55 with 10 years of service (defined benefit portion)	1% of AFC per year of service (defined benefit portion) The defined contribution portion depends on the member's contribution level and on investment performance.
LEOFF	Plan 1	All full-time, fully compensated law enforcement officers and fire fighters. (By 9/30/77)	After five years of eligible service	At age 50 with five years of service	20+ years of service: 2% of final average salary (FAS) per year of service. 10-19 years of service: 1.5% of FAS per year of service. 5-9 years of service: 1% of FAS per year of service.
	Plan 2	All full-time, fully compensated law enforcement officers, fire fighters and emergency medical technicians. (On or after 10/1/77)	After five years of eligible service	At age 53 with five years of service, or a benefit at age 50 with 20 years of service reduced 3% for each year under age 53	2% of FAS per year of service
WSPRS	Plan 1	Commissioned employees of the Washington State Patrol. (On or after 8/1/47 and by 12/31/02)	No requirement for active members; after five years of eligible service for inactive members	At age 55 or after 25 years of service	2% of average final salary (AFS) per year of service, capped at 75% of AFS.
	Plan 2	Same as WSPRS Plan 1. (On or after 1/1/03)	No requirement for active members; after five years of eligible service for inactive members	At age 55 or after 25 years of service	2% of AFS per year of service, capped at 75% of AFS.
JRS		Judges elected or appointed to the Supreme Court, the Court of Appeals and Superior Courts. (On or after 8/9/71 and by 6/30/88 – New judges on or after 7/1/88 join PERS)	After 15 years of service	At age 60	15 years of service: 3.5% of FAS per year of service, capped at 75% of FAS. 10-14 years of service: 3% of FAS per year of service, capped at 75% of FAS.
Judges		Judges elected or appointed to the Supreme Court, the Court of Appeals and Superior Courts. (By 8/8/71)	After 12 years of service	At age 70 with 10 years of service or any age with 18 years of service	1/2 of the monthly salary

\* PERS, SERS and TRS Plan 3 are defined benefit plans with a defined contribution component. Employers contribute to the defined benefit portion of the plan. Employees determine their own contributions. The defined contribution portion of the benefit depends on the member's contribution level and on investment performance. DRS publishes handbooks describing the rights and benefits for each system and plan, including disability and survivor benefits. These handbooks are provided to members by their employers. They are also available on the DRS website.

# Pension System Roles & Responsibilities

Organization	Responsibility	Membership and Contact Information
Department of Retirement Systems	Collects and accounts for employer and employee contributions, maintains retirement records, pays benefits, communicates pension information, provides investment education, and administers the Deferred Compensation Program.	PO Box 48380 Olympia, WA 98504-8380  Phone: 360.664.7000 Toll free: 800.547.6657 Website: <a href="http://www.drs.wa.gov">www.drs.wa.gov</a>
Pension Funding Council	Adopts economic assumptions for pension funding and member and employer pension contribution rates for LEOFF Plan 1, PERS, PSERS, SERS, TRS and WSPRS.	Can be contacted through DRS.
DRS Advisory Committee	Serves in an advisory role to the director of DRS.	Can be contacted through DRS.
Legislative Fiscal Committees	Review and report on retirement bills to the full Legislature.	House Ways and Means Committee PO Box 40600 Olympia, WA 98504-0600  Senate Ways and Means Committee PO Box 40482 Olympia, WA 98504-0482  Phone: 360.786.7155 Toll free: 800.562.6000 Website: <a href="http://www.leg.wa.gov">www.leg.wa.gov</a>
Office of Financial Management	Advises the governor on pension and funding policies and issues.	PO Box 43113 Olympia, WA 98504-3113  Phone: 360.902.0555 Website: <a href="http://www.ofm.wa.gov">www.ofm.wa.gov</a>
Washington State Investment Board	Invests and accounts for pension funds.	PO Box 40196 Olympia, WA 98504-0916  Phone: 360.956.4600 Website: <a href="http://www.sib.wa.gov">www.sib.wa.gov</a>
Office of the State Actuary	Acts as an advisory agency to the Legislature and to the director of DRS. Performs actuarial studies and reports on retirement bills. Creates formulas used to compute benefit payment adjustments that are based on early retirement, cost-of-living or long-term survivor benefits.	PO Box 40914 Olympia, WA 98504-0914  Phone: 360.786.6140 Website: <a href="http://www.osa.leg.wa.gov">www.osa.leg.wa.gov</a>
Select Committee on Pension Policy	Studies pension issues and retirement finances. Develops pension policies and recommends pension legislation.	Can be contacted through the State Actuary's Office.
Law Enforcement Officers' and Fire Fighters' Plan 2 Retirement Board	Policy-making board that studies pension issues, acts as fiduciary of LEOFF Plan 2, sets contribution rates and recommends pension policy to the Legislature for LEOFF Plan 2 members.	PO Box 40918 Olympia WA 98504-0918  Phone: 360.586.2320 Website: <a href="http://www.leoff.wa.gov">www.leoff.wa.gov</a>



Photo Credit: Naches Loop, Christine Tobin, DRS