

Pennsylvania Public School Employees' Retirement System

(A Component Unit of the Commonwealth of Pennsylvania)

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Comprehensive Annual Financial Report for the Fiscal Years Ended June 30, 2017 and 2016

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*Report prepared by the Public School Employees' Retirement System
Office of Financial Management Staff*

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5 North 5th Street
Harrisburg PA 17101-1905

Letter of Transmittal
COMMONWEALTH OF PENNSYLVANIA
PUBLIC SCHOOL EMPLOYEES' RETIREMENT SYSTEM

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October 27, 2017

The Honorable Thomas W. Wolf, Governor of Pennsylvania
Members of the PA General Assembly
Members of the Retirement System
Members of the Boards of PSERS' Employers
Pennsylvania Public School Employees' Retirement System Board of Trustees

Dear Governor Wolf, Legislators, Members, Employers' Board members, and PSERS Board of Trustees:

We are pleased to present the ninety-eighth edition of the Comprehensive Annual Financial Report (CAFR) for the Pennsylvania Public School Employees' Retirement System (PSERS, System, or Fund) for the fiscal years ended June 30, 2017 (FY 2017) and 2016 (FY 2016). This report is intended to provide financial, investment, actuarial, and statistical information in a single publication in accordance with the Government Finance Officers Association standards.

The management of the System is solely responsible for the accuracy and completion of this report, pursuant to section 24 Pa.C.S. §8502(n) of the Public School Employees' Retirement Code (Retirement Code). The entire report can be downloaded from PSERS' website at www.psers.pa.gov.

The System was established on July 18, 1917 to provide retirement benefits to public school employees of the Commonwealth of Pennsylvania (PA). The members eligible to participate in the System include all full-time public school employees, part-time hourly public school employees who render at least 500 hours of service in the school year, and part-time per diem public school employees who render at least 80 days of service in the school year in any of the 775 reporting entities in Pennsylvania. As of June 30, 2017, the System had nearly 256,000 active members with an estimated annual active payroll of \$13.3 billion.

The annuitant membership at June 30, 2017 was comprised of over 230,000 retirees and beneficiaries who receive over \$489 million in pension and healthcare benefits each month. The average yearly benefit paid to annuitants is \$25,287. The average benefit payment for each benefit type, grouped by years of credited service, is detailed in the Statistical Section of this report. See the Distribution of Annual Pension Amounts chart in the Introductory Section of this report.

In addition to retirement benefits, PSERS administers the Premium Assistance Program that provides a health insurance premium subsidy of up to \$100 per month for those retirees who qualify. At June 30, 2017, there are approximately 95,000 retirees who receive this benefit. PSERS also manages a health insurance program, PSERS Health Options Program, that is entirely funded through participating member premiums and provides Medicare Supplemental, Medicare Advantage, Prescription Drug, and Dental plans to over 95,000 retirees and their dependents.

PSERS provides a stable source of revenue for local economies throughout Pennsylvania. In FY 2017, PSERS distributed \$5.8 billion, or nearly 90%, in pension benefits to retired members who reside in Pennsylvania. These pension disbursements are a significant economic driver that benefit the economy of the Commonwealth. See the Pension Benefit Disbursement by County map in the Introductory Section of this report.

The System is a governmental cost-sharing, multiple-employer defined benefit pension plan, to which all members and 775 reporting units contribute. PSERS is administered by a staff of 317. The System is headquartered in Harrisburg, Pennsylvania, and has seven field offices in strategic areas of the Commonwealth to enable direct contact with the membership and the System's employers.

PSERS was established by law as an independent administrative board directed by a governing board of trustees (Board), which exercises control and management of the System, including the investment of its assets. PSERS is considered a component unit of the Commonwealth of Pennsylvania as defined by the Governmental Accounting Standards Board (GASB). An annual audit of the System by an independent certified public accounting firm is required by the Retirement Code. PSERS has contracted with SB & Company, LLC for this audit of its financial statements and has received an unmodified opinion as evidenced in the Report of Independent Public Accountants in the Financial Section of this CAFR. An unmodified opinion means that PSERS' financial statements fairly present, in all material respects, its financial condition. In addition, no significant findings were noted during the audit and therefore, a management letter was not issued. This is the eighth consecutive year that a management letter was not issued by the independent public accountants and is reflective of the hard work and dedication of PSERS' staff to continue to improve the internal controls, operations, and efficiency of the System.

Economic Summary

Economically, the fiscal year can be characterized as a “risk-on” period where taking concentrated equity risk paid off as opposed to holding a diversified portfolio of assets. Improving economic fundamentals, improving global growth, low but rising inflation, and increasing corporate profitability all contributed to strong equity performance. The MSCI All Country World Index, a global equity index, rose by 20.5% during this period. Conversely, commodities fell by 6.9% during the year as did U.S. long-term treasuries by 7.2%.

The U.S. economy improved but still experienced only modest growth this past fiscal year. While interest rates increased, they continued to be historically low which provided a low cost of borrowing so that broad economic conditions could continue to improve. The U.S. real Gross Domestic Product (GDP) increased year-over-year an average of 2.1% per quarter during the past fiscal year with a range of 1.2% to 2.8%. Concurrently, U.S. consumer confidence, as measured by the Conference Board's Consumer Confidence Index, improved from 97.4 at June 30, 2016 to 117.3 at June 30, 2017.

The Euro Area economy has shown improvement from last year. Evidence can be found in the improvement in the Markit Eurozone Manufacturing PMI (Purchasing Managers Index) which increased 4.6 points during the past fiscal year from 52.8 to 57.4. Aggressive actions by the ECB (European Central Bank) have generated improvements in economic growth, employment, and inflation. The ECB has continued its policy of very accommodative overnight interest rates and is ratably purchasing significant amounts of euro-denominated sovereign and corporate debt in an effort to put liquidity into the economy as well as ease financial conditions.

Japan's economy has grown for six straight quarters, the longest streak in 11 years. As of the second quarter 2017, Japan's real GDP had increased by an annualized rate of 4.0%. Japanese policy makers continue to aggressively stimulate their economy through a combination of low interest rates, the purchase of higher risk assets by the Bank of Japan, coordinated diversification into higher risk assets by large public investors, and fiscal spending policies to encourage liquidity to move into riskier assets. China had robust growth compared to the other developed regions of the world. China's real GDP increased by 6.9% over the past year, slightly faster than the 6.7% pace as of June 2016. Inflation in China has remained relatively stable over the past year at 1.5% compared to 1.9% last year.

The Board has continued to fulfill its mission to maintain stability and the long-term optimum value of the Fund. This is evidenced in the long-term growth of the System's assets and the actuarial soundness of the Fund. The annualized time-weighted rate of return for the twenty-five year period ended June 30, 2017 was 8.03% and exceeded the Fund's long-term investment rate of return assumption. Of utmost importance to the Board is the assurance that the required reserves are available for payment of retirement benefits.

Status of Pension Funding Initiatives

Act 120 of 2010 made dramatic progress toward addressing the pension funding issue. Act 120 included significant benefit reductions and also increased employer contributions to PSERS in stepped increments to slowly raise employer contributions to the actuarially required amount. During FY 2017, a major funding milestone was reached as employers fully funded 100% of the actuarially required contributions to PSERS for the first time in fifteen years. Full actuarial funding from employers, along with member contributions and investment income are all necessary sources of funds that will pay down the unfunded liability of the System. While a challenging pension funding

Introductory Section

environment remains for school employers and the Commonwealth due to legacy debt issues, all of the sources of funding are now in place to bring PSERS back to fully funded status.

As of June 30, 2017, approximately 68,000 or 26% of PSERS' active membership is under the reduced benefit structure of Act 120. The annual savings from the reduced benefit structure continue to grow and exceeded \$120 million in FY 2017.

Act 120 also provided for an innovative shifting of investment risk to members through a "shared risk" concept. New members hired after July 1, 2011 now share a portion of the investment risk of the Fund, giving PSERS a defined contribution (DC) element. Under the "shared risk" concept, members share some of the risk when investments underperform.

The first risk share measurement occurred in 2014. As a result of PSERS exceeding the investment performance hurdle mandated by Act 120, the member rate did not change. PSERS' returns outperformed the Act 120 risk share target rate for the six years ended June 30, 2017, the second risk share measurement period. As a result, PSERS' board is expected to certify there will be no change to the TE-TF member contribution rate at the December 2017 board meeting.

Pension Legislation Update - Act 5 of 2017

Throughout FY 2017, PSERS staff was actively engaged in providing actuarial data, legislative analyses, and related technical information to members of the General Assembly and Executive Branch Officials on a range of pension policy proposals while remaining policy neutral on plan design elements of legislative proposals.

On June 12, 2017 Governor Wolf signed Act 5 of 2017 into law. This pension legislation represents a substantial change to PSERS' operations and made significant changes to PSERS benefit structure for future members. School employees who become new members of PSERS on July 1, 2019 and thereafter will choose one of three new retirement plan options for their retirement benefits. The new plan design options include two hybrid plans consisting of defined benefit and defined contribution components and a stand-alone defined contribution plan. The current stand-alone defined benefit plan will no longer be available to new members.

A major effort will be required from PSERS to implement the new plan designs by the implementation date of July 1, 2019. PSERS will continue discussions with the Administration and legislative leaders to make sure the necessary funding, staffing, and other resources needed are received in order to achieve a successful plan implementation that will ultimately serve our future PSERS members.

Act 5 does not affect already retired members or those whose retirement date was prior to June 12, 2017. Class T-C and Class T-D members active on July 1, 2019 will have the opportunity to switch from the current defined benefit plan to one of the three new retirement plan options if they so choose.

Act 5 allows an actuarially neutral Option 4 "lump sum" withdrawal of member contributions and interest for Class T-E and Class T-F members whose retirement date is on or after June 12, 2017, and makes modifications to the "shared risk" program that will allow members to benefit when the Fund outperforms its investment rate of return assumption. Class T-E and Class T-F members active on July 1, 2019 will also have the opportunity to switch from the current defined benefit plan to one of the three new retirement plan options if they so choose.

Other key provisions in Act 5 include:

- Established the Public Pension and Asset Investment Review Commission to study and make recommendations to the General Assembly and the Governor regarding PSERS investment performance and investment strategies.
- Provided for PSERS legal counsel to serve independently from the Governor's Office of General Counsel.
- Established Board training requirements of 8 hours per year.
- Added Secretary of Banking and Securities as Board member, ex officio and reduced gubernatorial appointments from 2 to 1.

Major Initiatives

Pension Administration System Upgrade

The multi-year effort to upgrade the System's entire core client-server based pension administration system will culminate with an implementation in FY 2018. This mission critical system is used by PSERS' staff members and employers to execute PSERS' primary pension administration functions for all member transactions, all employer transactions and for the production of various administrative reports.

This upgrade from the existing "classic" version to a new "browser-based" version not only helps ensure the viability of PSERS' core pension administration system into the future, but also provides an enhanced "baseline" platform with built-in features that will make future enhancements much easier to implement. Enhancements included with the initial introduction of this upgraded pension administration will provide opportunities for members and employers to conduct transactions for themselves that would have previously required staff intervention. Some of these initial self-service features include: updating home mailing address, phone number and email information; setting preferences for receiving paper or electronic documents; electing Class T-E or T-F at qualification; electing multiple service membership; designating and updating beneficiaries; creating personalized retirement estimates by using an online calculator; viewing disbursements; calculating federal tax withholding using an online calculator; viewing and updating pension payment tax withholding; viewing correspondence from PSERS such as letters, newsletters, Statement of Accounts, and 1099Rs; and receiving PSERS-related news and alerts. These changes will not only directly increase customer service opportunities, but will also generate financial savings while possibly enabling PSERS to redeploy staff to other critical needs as workloads shift.

Budgetary and Financial Governance

PSERS submits its administrative budget request to the Governor's Office of the Budget each October for review. Any changes proposed by the Governor's Budget Office are made and a final amount is provided to the Legislature for their consideration. The Legislature passes the final budget and submits it to the Governor for his signature, after which it becomes law. PSERS' administrative budget is not funded from the Commonwealth's General Fund, but rather from the earnings of the Fund itself. Historically, PSERS has underspent its approved budget, keeping more funds available to invest for PSERS' members.

PSERS continues to be prudent in its use of funds and managing its annual budget. In FY 2017, PSERS expanded upon the process to stop payments sooner when a member dies, saving PSERS both time and money collecting the funds from the members' estate and reducing the amount of potentially uncollectible accounts. Working with its actuary, PSERS continues to save actuarial fees by completing various analyses in-house. Other savings include near historical low levels of overtime, a decrease in copier and printer rentals, and a reduction in overall printing expenses, all part of PSERS' ongoing efforts to control costs and improve operational efficiency.

PSERS participates in an independent, international benchmarking survey evaluating its costs and service performance in comparison to other similar public pension funds. Based on the most recent survey, PSERS had a 14% lower pension administration cost per member than the average cost for its peer group. By running a lean and efficient operation, PSERS saves the Commonwealth and school employers approximately \$6.3 million annually in administrative expenses compared to its peers.

In addition, during FY 2017, PSERS continued its ongoing efforts to recover funds from securities class action litigation. FY 2017 was one of the highest recovery years in PSERS' history as the System received \$25.2 million in settlements from these cases.

Investment Management Fees

PSERS continues to be one of the most transparent among large public pension funds in the nation for the disclosure of investment management fees. For example, certain pension funds report no or very little management fees for alternative investments because they are considered part of the cost of the investment and are netted against performance rather than shown separately. PSERS, however, obtains management fee information from its limited partnerships, and collective trust fund investments. This information is then used to fully report all relevant management fees in the System's financial statements. In addition, PSERS reports all other investment expenses, including staff compensation and overhead, consultant, legal, and bank expenses incurred.

Introductory Section

PSERS aggressively negotiates fees with all of its partnerships and managers and works to structure fee arrangements that align the interests of the investment manager with those of PSERS. Additionally, PSERS has recently embarked on an effort to reduce base management fees in exchange for higher performance or profit sharing fees with an aim to increase the alignment of interests. This will have the effect of reducing management fees in years when the managers underperform. Conversely, when those managers do well, performance fees will increase. As a result, this may add volatility to the fees paid from year to year, but will provide greater incentives for outperformance. This past year, PSERS' active managers had a very good year and performance fees increased from \$36.6 million to \$82.4 million due to above benchmark returns.

Overall, investment expenses increased by \$58 million from \$416 million in FY 2016 to \$474 million in FY 2017 mainly attributable to an increase in performance fees due to investment performance and growth in the asset base in the fixed income, absolute return, and risk parity asset classes. As a percentage of total benefits and expenses, investment expenses increased from 5.7% in FY 2016 to 6.3% in FY 2017.

Over the last four years, investment expenses as a percentage of total benefits and expenses has decreased from a high of 8.2% in FY 2013 to 6.3% in FY 2017 due to a decrease in investment expenses from \$558 million in FY 2013 to \$474 million in FY 2017.

Customer Service

PSERS has continued to make enhancements to its processes to operate more efficiently and provide quality customer service to our stakeholders. PSERS continued its efforts to provide retirement benefits in an efficient manner through a one-step process. Approximately 91% of the retirement benefits processed in FY 2017 were paid in one-step versus 87% in FY 2016. This was done while decreasing the number of days to pay a benefit from 27 days in FY 2016 to 24 days in FY 2017. Additionally, members whose benefit was processed in two steps, received their finalized benefit in 3 months as opposed to 5 months in the previous fiscal year.

The regional office in Pittsburgh was relocated from its downtown location to an updated facility with better accessibility in northern Pittsburgh. Due to the close proximity of other regional offices that provide the same service, PSERS closed its regional office in Fleetwood. This allowed positions to be relocated to neighboring regional offices for improved customer service in those locations.

Technology Upgrade

In March 2017, PSERS updated its websites to a Commonwealth-hosted content management solution. In addition to providing for operational efficiencies, this new medium allowed for the incorporation of a complete redesign using many industry best practices.

Understanding the importance of keeping our member data protected, PSERS appointed a Chief Information Security Officer (CISO) in August 2016 whose sole purpose is information security. The CISO has started to revamp the information security program at PSERS by completing a Commonwealth IT policy and compliance review and a General Information Security Assessment, along with a few other specific initiatives. PSERS is dedicated to ensuring the protection of member and employer data while still providing ease of access for members and staff. This is especially important as we move to the new Member Self Service Portal coming next year. As today's world changes with new and ever growing cyber security threats, PSERS maintains a focus on security and will continue to look for new ways to ensure member and employer data is protected.

Auditor General Report

During FY 2017, the Pennsylvania Department of the Auditor General completed a complex Special Performance Audit of PSERS. The objectives of the audit were (1) Pension Forfeiture Law compliance; (2) PSERS' Governance Structure and oversight of Investment Operations; (3) External Investment Manager fees; (4) Risk Management Strategies over the Investment Portfolio; and (5) Implementation of prior audit findings and recommendations from their report issued in September 2006. During the 9-month audit, PSERS responded to 72 detailed data requests and participated in multiple interviews and briefings with the Audit Team.

Overall, the Performance Audit Report opined that PSERS' reporting and transparency of investment expenses surpasses its peer public pension funds; PSERS' management of investment expenses appears standard; PSERS' attention to asset allocation, diversification and risk management appears adequate and reasonable; and PSERS has complied with the Public Employee Pension Forfeiture Act. There were no findings that suggest any fraud, waste or

abuse of funds or any instances where poor decisions, policies or practices of the PSERS Board or Staff have resulted in losses to the fund or violations of applicable laws or regulations. Many of the findings and recommendations were procedural and administrative in nature. PSERS Management accepted these findings and recommendations in the spirit of continuous improvement of the administration of the System.

Financial Highlights

The fair value of the System's fiduciary net position grew \$3.3 billion during FY 2017 to \$53.5 billion as of June 30, 2017 and the unfunded liability, on a market value basis, declined. The System is the 16th largest state-sponsored public defined benefit pension fund in the nation and the 28th largest among public and corporate pension funds in the nation. More specific information on the System's net position is detailed in the Statements of Fiduciary Net Position and Management's Discussion and Analysis included in the Financial Section of this report.

One of PSERS' mission critical objectives is the timely and accurate payment of benefits. In FY 2017, PSERS provided over \$6.9 billion in pension and healthcare benefits to its members.

The System's administrative budget request is appropriated by the PA General Assembly and funded by the investment income of the System. For FY 2017, the appropriation was \$44.7 million.

Funding

Funding is the process of specifically setting aside money for current and future use. Proper funding for a defined benefit pension plan entails an actuarial examination of the fund balances and liabilities to ensure money will be available for current and future benefit payments. The actuarial valuation measures the progress toward funding pension obligations of the System by comparing the actuarial assets to the actuarial liabilities of the System.

The results of PSERS' latest published actuarial valuation (as of June 30, 2016) indicated that the rates of contribution payable by the members and employers, when taken together with the current assets of the System, are adequate to fund the actuarial liabilities for all benefits payable under the System at that date. The total funded status as of the latest actuarial valuation was 57.3%. Additional comparative information on the funded status of PSERS can be found in the Financial Section and in the Actuarial Section of this report.

Investments

Over the past few years, PSERS' Board and investment staff made significant changes to the Fund's investment asset allocation, including further refining its investment strategy and increasing the diversification of assets. In particular, PSERS actively reduced its risk profile by significantly decreasing its equity exposure and by moving portions of the Fund's assets into asset classes that are less correlated to the equity markets.

Income from the investment portfolio represents the major source of revenue to the System, accounting for 63% of total revenues over the twenty-year period from FY 1998 to FY 2017. During FY 2017, net investment income was \$5.0 billion. The investment portfolio, which is one part of the System's net position, totaled \$52.5 billion, at fair value, as of June 30, 2017. For FY 2017, the time-weighted net rate of return on the System's investments was 10.14%.

The investment portfolio is well diversified to emphasize a long-term investment approach. The overall objective of the System is to provide benefits to its members through a carefully planned and well-executed investment program. The return objectives are to: (i) realize a return that exceeds the Policy Index (the Policy Index is a custom benchmark, based on the Board-established asset allocation structure that seeks to generate a return that meets the actuarial rate of return assumption); and (ii) invest the assets to maximize returns for the level of risk taken. The risk objectives are to: (i) diversify the assets of the System to minimize the risk of losses within any one asset class, investment type, industry or sector distribution, maturity date, or geographic location; and (ii) invest the assets so that the probability of investment losses (as measured by the Policy Index) in excess of 15.0% in any one year is no greater than 2.5% (or two standard deviations below the expected return). Additional information on the System's investments is contained in the Investment Section of this report.

Federal and State Tax Status

The System is a qualified trust fund under Section 401(a) of the Internal Revenue Code (IRC). As a result of the qualified status, the trust fund is entitled to an exemption, under Section 501(a) of the IRC, from federal income taxation on its investment earnings. Additionally, contributions made on behalf of the active members are tax deferred under Section 414(h) of the IRC. The trust fund and any benefits accruing to the members of PSERS are exempt from Pennsylvania state and municipal taxes. The Internal Revenue Service (IRS) issued a determination letter dated March 16, 2017 which stated that the plan and its underlying trust qualify under the provisions of Section 501(a) of the IRC and therefore are exempt from federal income taxes.

Act 93 of 2015

On December 28, 2015, Governor Wolf signed into law House Bill Number 1332, Printer's Number 1814, as Act 93 of 2015. This legislation amends the Retirement Codes of the Public School Employees' Retirement System and the State Employees' Retirement System (SERS) to ensure that PSERS and SERS will remain tax-qualified 401(a) governmental plans under the Internal Revenue Code (IRC).

Internal Controls and Reporting

PSERS' management is responsible for and has implemented internal controls designed to provide reasonable assurances for the safeguarding of assets and the reliability of financial records. This report has been prepared in accordance with accounting principles generally accepted in the United States of America. The System maintains a full accrual accounting system. More specific accounting information is detailed in the Summary of Significant Accounting Policies (Note 2) in the notes to the financial statements found in the Financial Section of this report.

A system of internal controls provides reasonable, but not absolute, assurance that assets are properly safeguarded and that financial statements are reliable. The concept of reasonable assurance recognizes that first, the cost of a control should not exceed the benefits likely to be derived, and second, the valuation of the cost and benefits requires estimates and judgments by management.

PSERS' management believes the internal accounting controls currently in place are adequate to meet the purpose for which they were intended and also believes the financial statements, supporting schedules, and statistical tables are fairly presented.

GASB OPEB Accounting and Financial Reporting Project (OPEB Project)

In June 2015, the Governmental Accounting Standards Board (GASB) approved a pair of related Statements that reflect substantial changes to the accounting and financial reporting of state and local government Postemployment Benefit Plans Other Than Pension Plans (OPEB). Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, addresses financial reporting for state and local government OPEB plans. Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, establishes new accounting and financial reporting requirements for governments that provide or finance OPEB.

Statement No. 74 replaced the requirements of Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pensions*, for most OPEB plans provided by state and local governments. Statement No. 75 replaces the requirements of Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, and Statement No. 57 *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, for most government employers providing or financing OPEB.

Statement No. 74 provides OPEB plans such as PSERS Health Insurance Premium Assistance Program guidance for financial reporting. Statement No. 74 significantly changed related financial reporting through note disclosures and new Required Supplementary Information (RSI) schedules. These changes are necessary for government employers to comply with Statement No. 75.

PSERS adopted Statement No. 74 for the fiscal year ended June 30, 2017. An analysis of Statement No. 74 can be found in the Management's Discussion and Analysis, notes to the financial statements, and RSI found in the Financial Section of this report.

Professional Services

Professional consultants are appointed by the Board of Trustees to perform services essential to the efficient operation of the System. An annual audit by an independent certified public accounting firm and an annual valuation by an actuarial consultant attest to the financial and actuarial soundness of PSERS. The investment performance of the System is reviewed by an investment evaluation firm on a quarterly basis. The consultants providing services to the System are listed in the Financial Section and Investment Section of this report.

Other Information

In compliance with the Retirement Code, actuarial tables and the computational procedures used by the System in calculating annuities and other benefits were published in the *Pennsylvania Bulletin* (Vol. 43, No. 18). This information can be found at <http://www.pabulletin.com/secure/data/vol43/43-18/841.html>.

System Awards

Government Finance Officers Association of the United States and Canada Certificate of Achievement for Excellence in Financial Reporting

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to PSERS for its Comprehensive Annual Financial Report for the fiscal year ended June 30, 2016. The Certificate of Achievement is a prestigious national award recognizing conformance with the highest standards for preparation of state and local government financial reports. To be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report whose contents conform to program standards. Such a comprehensive annual financial report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year. PSERS has received a Certificate of Achievement for 34 consecutive years from FY 1983 to FY 2016. A photograph of this award appears in the Introductory Section of this report. Its attainment represents a significant accomplishment by the System, whose Office of Financial Management holds general responsibility for the compilation and validity of the financial data presented in the Comprehensive Annual Financial Report.

The System believes the current report continues to conform to the Certificate of Achievement program requirements and will be submitting this report to GFOA to determine eligibility for the 2017 certificate.

GFOA Popular Annual Financial Reporting Award

Government Finance Officers Association of the United States and Canada (GFOA) has given an Award for Outstanding Achievement in Popular Annual Financial Reporting to PSERS for its Popular Annual Financial Report for the fiscal year ended June 30, 2016, which PSERS refers to as its Summary Annual Financial Report. The Award for Outstanding Achievement in Popular Annual Financial Reporting is a prestigious national award recognizing conformance with the highest standards for preparation of state and local government popular reports.

In order to receive an Award for Outstanding Achievement in Popular Annual Financial Reporting, a government unit must publish a Popular Annual Financial Report, whose contents conform to program standards of creativity, presentation, understandability, and reader appeal.

An Award for Outstanding Achievement in Popular Annual Financial Reporting is valid for a period of one year only. This was PSERS' first Popular Annual Financial Report publication and award.

Public Pension Coordinating Council Public Pension Standards Award

The Public Pension Coordinating Council has awarded its Public Pension Standards Award to PSERS for 2016. This award is in recognition of meeting professional standards for plan design and administration as set forth in the Public Pension Standards.

The Public Pension Coordinating Council was formed in 1990 to assist the public employee retirement community. The Council is composed of representatives from three national associations whose members are directly involved in the administration of public employee retirement systems: the National Association of State Retirement Administrators

Introductory Section

(NASRA); the National Conference on Public Employee Retirement Systems (NCPERS); and the National Council on Teacher Retirement (NCTR). A reproduction of this award appears in the Introductory Section.

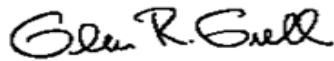
CIO Industry Innovation Award

On December 12, 2016, Chief Investment Officer Magazine awarded PSERS with the 2016 Industry Innovation Award for Public Defined Benefit Plans, \$15 billion to \$100 billion. This investment industry award recognizes innovation in institutional investing. PSERS was one of seven public plans nominated for this award.

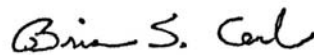
Acknowledgements

The preparation of this report reflects the combined efforts of PSERS' staff under the direction of the PSERS Board. It is intended to provide complete and reliable information in conformance with accepted standards and to document responsible stewardship of the System's assets.

Respectfully submitted,



Glen R. Grell
Executive Director

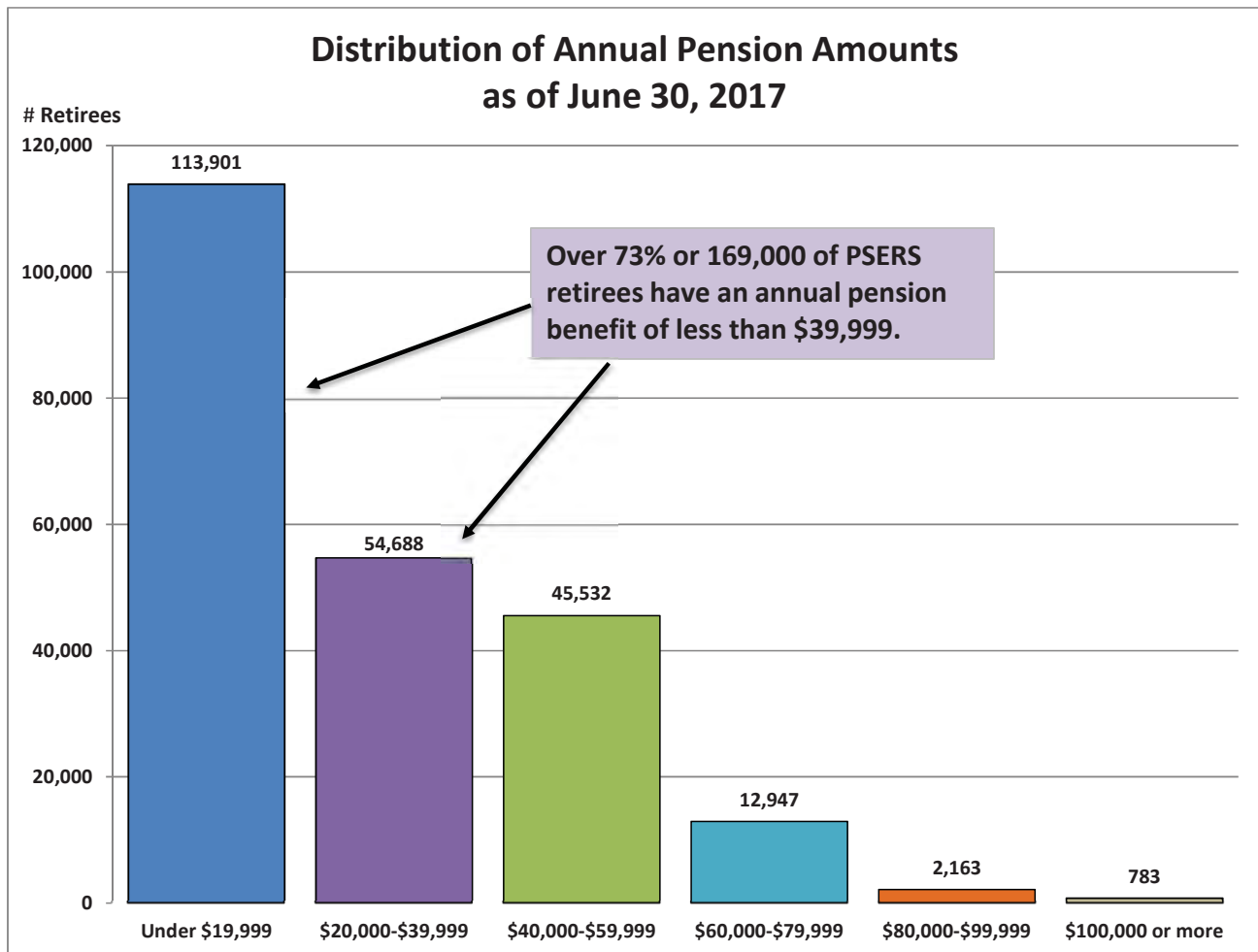


Brian S. Carl, CPA, CTP
Chief Financial Officer

Pension Benefit Disbursement Amounts Fiscal Year 2017 (Dollar Amounts in Millions)

The average PSERS retiree receives a modest pension of \$25,287 on an annual basis, a benefit earned through a lengthy career of 23 years in public education. During their career, members make mandatory contributions to PSERS to help fund their own retirement benefit. Most members contribute between 7.50% and 10.30% of their pay depending on their class of membership to help fund their own retirement benefit. In accordance with Act 120, new members as of July 1, 2011 and thereafter are funding the majority of the cost of their benefit. This is in contrast to many non-public (private) pension plans. In over 90% of such plans, members do not contribute and the employers bear 100% of the cost of the benefit.

Six figure pensions are rare. In FY 2017, there were approximately 783 retired members receiving an annual benefit over \$100,000 out of a total 230,000 PSERS retirees. These six-figure pension retirees spent an average of 38 years working in their public education careers and contributing to their benefit.





2012

2013

2014

2015

2016



GOVERNMENT FINANCE OFFICERS ASSOCIATION

Certificate of Achievement
for Excellence
in Financial Reporting

Presented to

Pennsylvania Public School
Employees' Retirement System

A handwritten signature in black ink, reading "Jeffrey A. Casan".

Executive Director / CEO



Public Pension Coordinating Council

*Public Pension Standards Award
For Funding and Administration
2016*

Presented to

***Pennsylvania Public School Employees'
Retirement System***

In recognition of meeting professional standards for
plan funding and administration as
set forth in the Public Pension Standards.

Presented by the Public Pension Coordinating Council, a confederation of

National Association of State Retirement Administrators (NASRA)
National Conference on Public Employee Retirement Systems (NCPERS)
National Council on Teacher Retirement (NCTR)

A handwritten signature in black ink that reads "Alan H. Winkle". The signature is written in a cursive style.

Alan H. Winkle
Program Administrator

Mission Statement



The Board of Trustees and the employees of the Public School Employees' Retirement System (System) serve the members and stakeholders of the System by:

- Providing timely and accurate payment of benefits*
- Maintaining a financially sound System*
- Prudently investing the assets of the System*
- Clearly communicating members' and employers' rights and responsibilities, and*
- Effectively managing the resources of the System*

adopted June 20, 2008

Administrative Organization PSERS Board of Trustees



Seated, front row: Stacey Connors, designee for Honorable Patrick M. Browne; Deborah J. Beck; Susan C. Lemmo; Melva S. Vogler, Board Chairman; Virginia M. Lastner; Lori Graham, designee for Secretary Pedro A. Rivera

Standing, second row: Christopher SantaMaria; Luc Miron, designee for Honorable John P. Blake; Bernard Gallagher, designee for Honorable Joseph F. Markosek; Glen R. Grell, PSERS' Executive Director, Board Secretary; Honorable Stephen Bloom; Jason M. Davis; Nathan G. Mains; Ambassador Martin J. Silverstein

Not pictured: Honorable Joseph M. Torsella, and Secretary Robin L. Wiessmann

PSERS Board of Trustees

Secretary of Education of the Commonwealth of Pennsylvania (ex officio)

Mr. Pedro A. Rivera

Secretary of Banking and Securities of the Commonwealth of Pennsylvania (ex officio)

Ms. Robin L. Wiessmann

Treasurer of the Commonwealth of Pennsylvania (ex officio)

Honorable Joseph M. Torsella

Executive Director of the Pennsylvania School Boards Association, Inc. (ex officio)

Mr. Nathan G. Mains

One member appointed by the Governor of the Commonwealth of Pennsylvania for a term of three years

Ambassador Martin J. Silverstein (term expires 12/31/17)

Three members elected from among the Active Certified Contributors of the System for a term of three years

Mr. Jason M. Davis (term expires 12/31/19)

Ms. Susan C. Lemmo (term expires 12/31/18)

Mr. Christopher SantaMaria (term expires 12/31/20)

One member elected from among the Active Non-Certified Contributors of the System for a term of three years

Ms. Deborah J. Beck (term expires 12/31/18)

One member elected from among the annuitants of the System for a term of three years

Ms. Melva S. Vogler (term expires 12/31/19)

One member elected by the members of Pennsylvania Public School Boards from among their number for a term of three years

Ms. Virginia M. Lastner (term expires 12/31/17)

Two members appointed by the Speaker of the House from the Pennsylvania House of Representatives, one representing the Majority Party and one representing the Minority Party

Honorable Stephen Bloom (term expires 12/31/18)

Honorable Joseph F. Markosek (term expires 12/31/18)

Two members appointed by the President Pro Tempore of the Pennsylvania Senate, one representing the Majority Party and one representing the Minority Party

Honorable John P. Blake (term expires 12/31/18)

Honorable Patrick M. Browne (term expires 12/31/18)

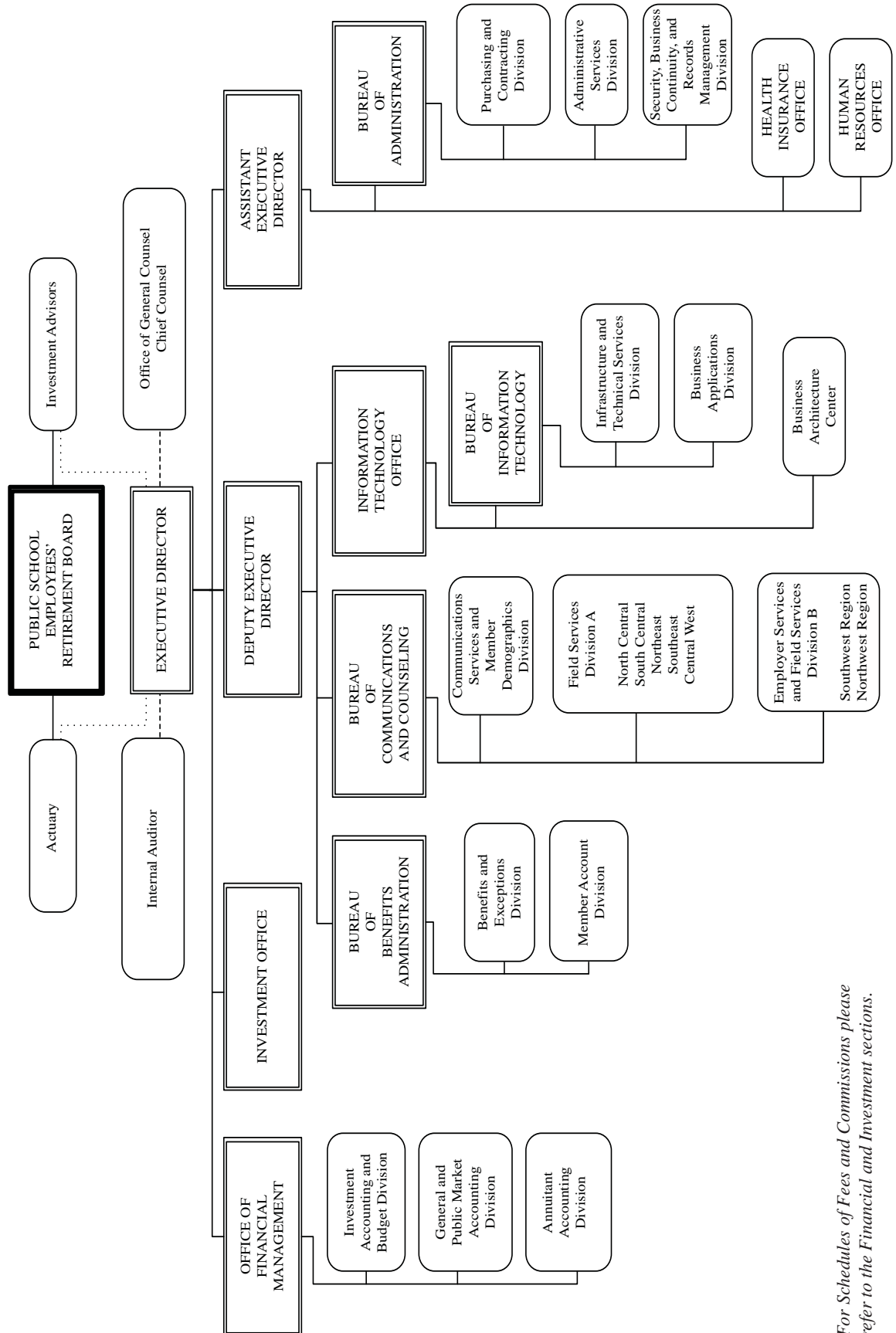
2017 Board Committees

<p style="text-align: center;">Appeals/Member & Employer Services</p> <p style="text-align: center;">Ms. Beck, Chair Senator Blake Representative Bloom Mr. Davis Ms. Lemmo Mr. SantaMaria</p>	<p style="text-align: center;">Audit/Compliance</p> <p style="text-align: center;">Representative Bloom, Chair Senator Blake Ms. Lastner Mr. Mains Representative Markosek Treasurer Torsella</p>	<p style="text-align: center;">Budget/Finance</p> <p style="text-align: center;">Representative Bloom, Chair Senator Blake Ms. Lastner Mr. Mains Representative Markosek Treasurer Torsella</p>
<p style="text-align: center;">Bylaws/Policy</p> <p style="text-align: center;">Representative Markosek, Chair Senator Browne Mr. Davis Ms. Lemmo Mr. Mains Mr. Rivera</p>	<p style="text-align: center;">Corporate Governance</p> <p style="text-align: center;">Senator Browne, Chair Representative Markosek Mr. SantaMaria Ambassador Silverstein Treasurer Torsella Ms. Wiessmann</p>	<p style="text-align: center;">Elections</p> <p style="text-align: center;">Ambassador Silverstein, Chair Ms. Beck Senator Browne Mr. Davis Mr. Rivera Treasurer Torsella</p>
<p style="text-align: center;">Health Care</p> <p style="text-align: center;">Ms. Lemmo, Chair Ms. Beck Senator Blake Representative Bloom Mr. Davis Ms. Lastner</p>	<p style="text-align: center;">Investment</p> <p style="text-align: center;">Mr. Mains, Chair Ms. Lemmo</p> <p style="text-align: center;">Committee is comprised of all Board Members</p>	<p style="text-align: center;">Personnel</p> <p style="text-align: center;">Ms. Lastner, Chair Senator Blake Ms. Lemmo Mr. Mains Representative Markosek Treasurer Torsella</p>

NOTE: The chair of the Board of Trustees is a voting ex officio member of all Committees.

Organizational Chart of the Public School Employees' Retirement System

As of June 30, 2017



For Schedules of Fees and Commissions please refer to the Financial and Investment sections.

Administrative Staff



James H. Grossman Jr.
Chief Investment Officer



Glen R. Grell
Executive Director



Terrill J. Sanchez
Deputy Executive Director



Charles K. Serine
Chief Counsel



Brian S. Carl
Chief Financial Officer



Joseph E. Wasiak
Assistant Executive Director



Richard R. Spinks
Chief Technology Officer



Edward G. Rohrbaugh
Director of Administration



Franca M. D'Agostino
Director of Health
Insurance



Eugene W. Robison
Director of Communications
and Counseling



Steven C. Goldstein
Director of Information
Technology



Tammy L. Meshey
Director of Human
Resources



Marla Cattermole
Director of Benefits
Administration



Alicia James
Internal Auditor



Tony Parisi
Director of Government
Relations



Evelyn M. Williams
Press Secretary

PSERS REGIONAL OFFICES

Public School Employees' Retirement System of Pennsylvania

PSERS FIELD SERVICES DIVISION



Northwest

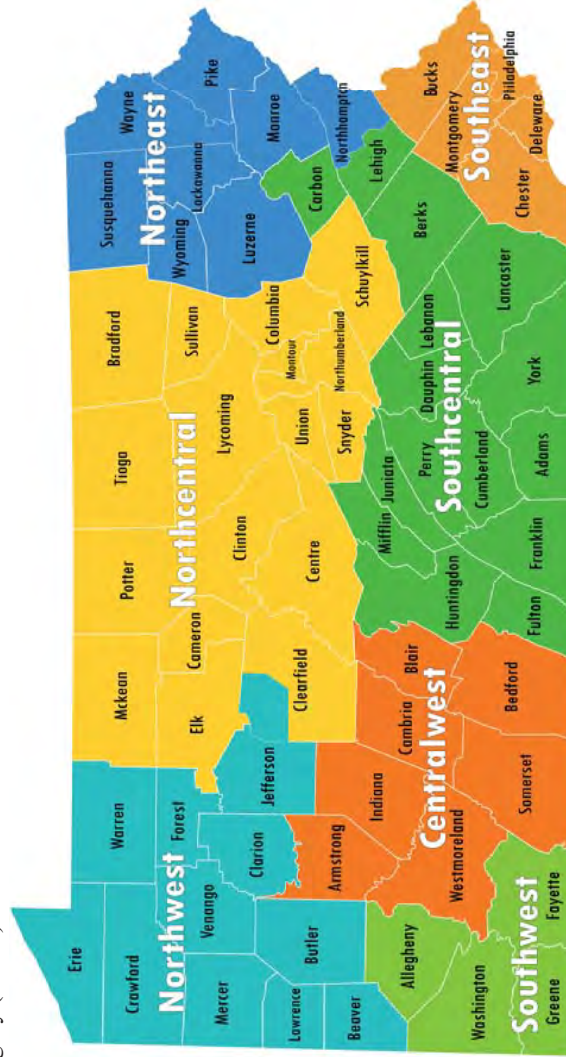
Pennwood Center
464 Allegheny Boulevard, Suite C
Franklin, PA 16323-6210
 Local: 1.814.437.9845
 FAX: 1.814.437.5826
Toll-Free: 1.888.773.7748 ext. 5175
 Donald Gregory (x5150)

Northcentral

300 Bellefonte Avenue, Suite 201
Lock Haven, PA 17745-1903
 Local: 1.570.893.4410
 FAX: 1.570.893.4414
Toll-Free: 1.888.773.7748 ext. 5275
 Jeremy Wible (x5252)

Northeast

417 Lackawanna Avenue, Suite 201
Scranton, PA 18503-2013
 Local: 1.570.614.0269
 FAX: 1.570.614.0278
Toll-Free: 1.888.773.7748 ext. 5375
 Sherry Sibio (x5350)



Southwest

300 Cedar Ridge Drive, Suite 301
Pittsburgh, PA 15205-9778
 Local: 1.412.920.2014
 FAX: 1.412.920.2015
Toll-Free: 1.888.773.7748 ext. 5775
 Russell Miller (x5751)

Centralwest

219 W. High Street
Ebensburg, PA 15931-1540
 Local: 1.814.419.1180
 FAX: 1.814.419.1189
Toll-Free: 1.888.773.7748 ext. 5875
 Brian Farester (x5850)

Southcentral

5 N 5th Street
Harrisburg, PA 17101-1905
 Local: 1.717.720.6335
 FAX: 1.717.783.9606
Toll-Free: 1.888.773.7748 ext. 6335
 John Tucker (x6330)

Southeast

605 Louis Drive, Suite 500
Warminster, PA 18974-2825
 Local: 1.215.443.3495
 FAX: 1.215.443.3487
Toll-Free: 1.888.773.7748 ext. 5575
 Joshua Catalifu (x5551)
 Linda Visco (x5560)

Effective June 30, 2017

PSERS Headquarters Building



The administrative headquarters of the Public School Employees' Retirement System (PSERS) is located at 5 North Fifth Street in downtown Harrisburg, Pennsylvania within the State Capitol complex. Regional field offices are also maintained in Ebensburg, Franklin, Lock Haven, Harrisburg, Pittsburgh, Warminster, and Scranton.

The headquarters building was constructed and first occupied by the Retirement System in 1987. It is the first time a building was constructed for PSERS use. It is owned by the Five North Fifth Street Corporation, a holding entity formed by PSERS, and is managed by Property Management, Inc.