



Retirement Fund Investments Decline with the Economy But Still Meet Several Performance Benchmarks; SBA Must Improve Communication with Its Stakeholders

at a glance

Nationwide, pension plan investment returns are falling, and Florida Retirement System (FRS) investment returns are consistent with this trend. Short-term losses will likely continue until the economy rebounds. However, in the context of the global economic downturn, the State Board of Administration's investment results have generally outperformed other public and private institutional pension funds. While both the pension and investment plans lost more than 4% of their value in Fiscal Year 2007-08, the most recent FRS actuarial valuation shows the pension plan was sufficiently funded to pay plan participant benefits.

Although the board has several procedures in place to help ensure appropriate oversight of FRS funds, independent consultants report that these procedures need to be strengthened. In particular, the board has lacked an independent compliance function and needs better internal controls that segregate its management and oversight functions. The board is working to correct these deficiencies. In addition, the board needs to improve its accountability to stakeholders through better communication of its investment results, activities, costs, and the pension plan's future funding needs.

Scope

Section 215.44(6), *Florida Statutes*, requires the Office of Program Policy Analysis and Government Accountability to perform a biennial evaluation of the State Board of Administration's (SBA) management of investments. This report examines the SBA's Florida Retirement System-related investment activities in Fiscal Years 2005-06, 2006-07, and 2007-08 and answers six questions.

1. Are funds contained within the FRS pension plan sufficient to pay retiree benefits?
2. How have economic events affected the performance of the FRS pension and investment plans?
3. How does the SBA oversee the pension and investment plans?
4. Are the fees the SBA pays external pension plan investment managers comparable to those paid by other states?
5. How well does the SBA communicate its investment results to stakeholders?
6. Has the SBA taken corrective action to address previous OPPAGA findings?

Background

Agency responsibilities

The State Board of Administration (SBA) is primarily an asset management organization charged by Article XII, Section 9 of the Florida Constitution and state law with investing on behalf of a variety of state and local

government entities. The board is composed of the Governor, the Chief Financial Officer, and the Attorney General who serve as trustees to the funds under board management. An executive director is appointed by the trustees and directs a staff that oversees the general management of the state's 35 investment funds.

State law provides detailed limitations on how the SBA is to invest these funds. For example, Florida statutes prohibit the board from investing more than

- 25% of any fund in bonds, foreign currency, notes, and notes secured by first mortgages, mortgage securities, group annuity contracts, real property, and U.S. government obligations;
- 80% of any common stock, preferred stock, and interest-bearing obligations of a corporation having an option to convert into common stock;
- 10% of the entire portfolio in alternative investments defined as investment in private equity, venture, hedge, or distress funds; and
- 1.5% of the entire portfolio in economically targeted investments designed to provide superior returns to the portfolio while also economically benefitting the state.¹

The Florida Retirement System (FRS) is the largest fund managed by the SBA. The board oversees investments in two FRS programs: the FRS Pension Plan and the FRS Investment Plan.

FRS Pension Plan. The pension plan is the nation's fourth largest public pension system, behind California Public Employees, California State Teachers, and New York State Common Funds. With assets of \$127 billion, on June 30, 2008, the fund comprises 82% of the funds managed by the board. Employees are able to vest with the plan after six years of employment. It is a defined benefit plan that bases pension payments on a formula that includes each employee's years of service, salary, and age at retirement. It is funded exclusively by the state; employees do not contribute to the fund or make decisions about how fund assets will be invested. The plan serves 590,194 participants and 274,708 retiree annuitants. Net asset values of this fund for Fiscal Years 2005-06, 2006-07, and 2007-08, were \$118 billion, \$136 billion, and \$127 billion, respectively. The fund is managed by 126 external

and 32 internal investment managers, with oversight from the board's executive director.

FRS Investment Plan. The Legislature established the investment plan in Fiscal Year 2002-03, allowing state employees to direct the board to invest their retirement funds in a pool of 20 approved investments. The plan allows employees to vest after one year of employment and currently serves 95,392 employees. Unlike the pension plan, benefit payments will be based on each employee's investment choices and market conditions. The investment plan is portable, as employees can roll plan funds into a qualified retirement plan with a new employer if they leave state employment after a year of service. Total assets for this plan have been \$2.3 billion, \$3.7 billion, and \$4.4 billion for Fiscal Years 2005-06, 2006-07, and 2007-08, respectively. Twenty-one external managers, with oversight from the board, manage the portfolios contained in the investment plan.

Agency resources

The State Board of Administration does not receive an annual legislative appropriation. Its operational and administrative expenses are funded through fees derived from its investment management services and employer contributions to the retirement system. In Fiscal Years 2005-06, 2006-07, and 2007-08, board fees were \$20 million, \$23 million, and \$27 million, respectively. The board's current budget is \$25.9 million and it has 163 authorized positions.

Questions and Answers —

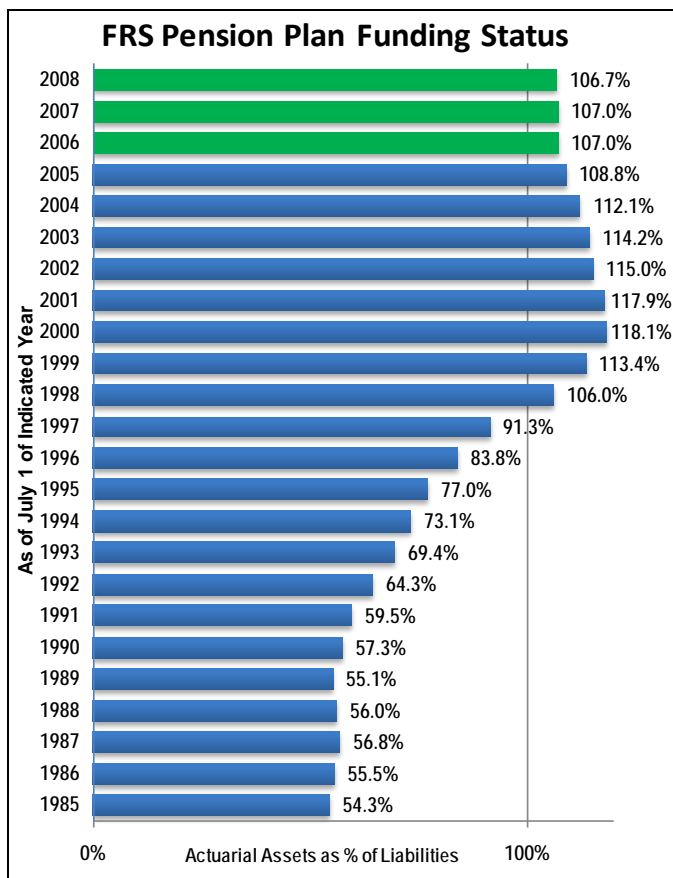
Are funds contained within the FRS pension plan sufficient to pay retiree benefits?

The FRS pension plan historically has shown strong financial health, particularly when compared to other public and private pension plans. Exhibit 1 shows that for the last three fiscal years, pension fund assets exceeded liabilities, i.e., the monies on hand have exceeded the monies needed to pay retirees. For the current review period (Fiscal Years 2005-06, 2006-07, and 2007-08), Florida's ratio of assets to liabilities was 107%, 107%, and 106.7%, respectively. During the same period, the fund operated at a surplus of \$7.6 billion, \$9.1 billion, and \$8.7 billion, respectively.

¹ See OPPAGA report *Economically Targeted Investment Program Under Development*, [Report No. 08-72](#), December 2008.

However, because of the downturn in the global economy, the board's executive staff—State Board of Administration managers—anticipate these surpluses may not carry forward into the next fiscal year.²

Exhibit 1 For the Past Decade, FRS Pension Plan Assets Have Exceeded Liabilities



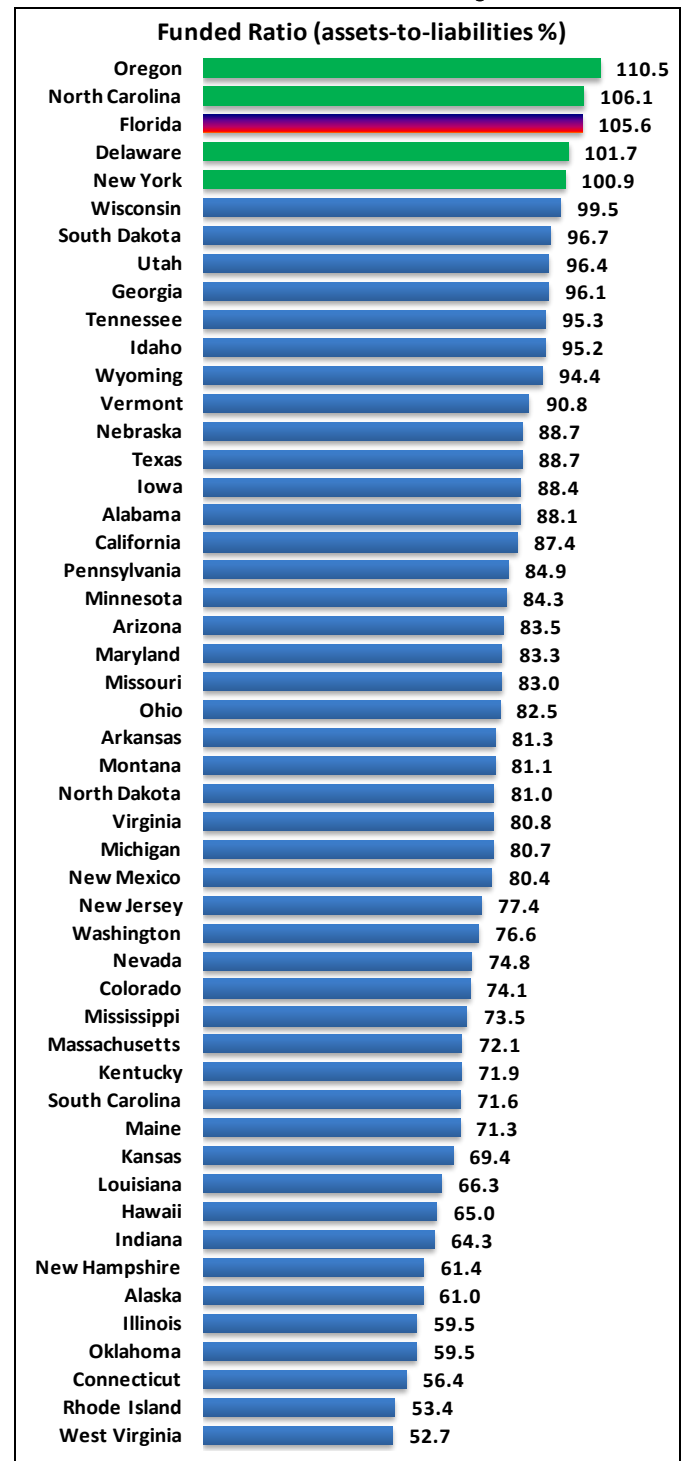
Source: State Board of Administration.

For the past three fiscal years, the majority of payments made to FRS retirees have been from investment earnings rather than the fund's principal. For Fiscal Years 2005-06, 2006-07, and 2007-08, about 70% of pension payments were made from the fund's earned interest. In contrast, states with pension funds that have no surplus have liabilities that exceed assets, or have insufficient interest earnings must generally make up for this shortfall through tax increases, bond issues, and higher employee and/or employer payroll contributions.

² The state does not contract for a mid-fiscal year funding ratio analyses. The Department of Management Services' Division of Retirement contracts with an actuary who annually calculates the funding ratio at the end of each fiscal year, which is June 30. Current funding ratios will be available at that time.

In its 2008 ranking of public pension plans, Standard & Poor's ranked Florida third in financial strength, as measured by assets exceeding liabilities (see Exhibit 2). Rankings are based on 2006 data, the most current data available for all 50 states.

Exhibit 2 Florida's Pension Plan Is One of Strongest in the U.S.



Source: Standard & Poor's February 20, 2008 Public Pension Ranking Report.

How have economic events affected the financial performance of the FRS pension and investment plans?

Despite the historical strength of the Florida Retirement System, investment returns for both the pension and investment plans have been affected by the U.S. recession and turmoil in the financial markets. It is in this context that investment returns of the more than 14,000 worldwide securities comprising the FRS pension and investment plans should be evaluated.

In December 2007, the U.S. economy entered into a recession, triggered by a decline in the value of mortgaged-backed securities.³ U.S. and foreign entities that had invested heavily in these securities suffered significant losses as housing prices and demand declined and mortgage defaults and foreclosures increased. This resulted in a credit crisis as financial institutions feared insolvency and virtually stopped making loans to consumers and businesses, thereby freezing worldwide credit markets. In this volatile environment, investors began reappraising the value of securities within a variety of asset classes. By December 2008, major financial markets and economies worldwide were in significant decline.

FRS Pension Plan performance was adversely affected by the downturn in the economy. To help counteract the impact of market declines on FRS pension plan investments, the State Board of Administration maintained diversified assets and continued its practice of daily monitoring the percentages of stocks, bonds, real estate, etc., in the pension fund and rebalancing these percentages if they fell outside those percentages authorized by law. Despite these efforts, the global downturn reduced pension plan returns. Specifically, as shown in Exhibit 3, the pension plan's one-year rate of return was a negative 4.42% and the overall fund balance dropped by \$9 billion in Fiscal Year 2007-08. In October 2008, as markets continued to fall, SBA managers suspended their rebalancing activities and accumulated cash as a hedge against further losses. Nonetheless, in the first six months of Fiscal Year 2008-09, the fund lost an additional \$28 billion, or 22%, and its losses exceeded its target return and

comparable benchmarks. Appendix A shows SBA's investment returns for the fund's asset classes.

Exhibit 3 FRS Pension Plan Returns Declined with the Economy but Frequently Exceeded Benchmarks

Florida Retirement System	FRS Pension Plan Returns			
	FY 2005-06	FY 2006-07	FY 2007-08	December 31, 2008 ¹
1-Year Return	10.56%	18.07%	-4.42%	-26.74%
Target Return Benchmark ²	10.03%	17.85%	-4.32%	-26.07%
Comparable Benchmark ³	10.70%	16.70%	-4.90%	-25.53%
Met or exceeded one or both benchmarks?	Yes	Yes	Yes	No
3-Year Return	12.42%	12.88%	7.66%	-2.88%
Target Return Benchmark ²	11.87%	12.32%	7.44%	-2.71%
Comparable Benchmark ³	12.40%	11.80%	6.60%	-2.78%
Met or exceeded one or both benchmarks?	Yes	Yes	Yes	No
5-Year Return	6.08%	11.52%	9.91%	2.03%
Target Return Benchmark ²	5.84%	11.30%	9.56%	1.96%
Comparable Benchmark ³	6.50%	10.90%	8.90%	1.83%
Met or exceeded one or both benchmarks?	Yes	Yes	Yes	Yes
10-Year Return	8.74%	8.46%	5.85%	2.67%
Target Return Benchmark ²	8.42%	7.98%	5.39%	2.31%
Comparable Benchmark ³	8.60%	8.20%	5.90%	3.07%
Met or exceeded one or both benchmarks?	Yes	Yes	Yes	Yes

¹ Reported returns are for the 1-, 3-, 5-, and 10-year periods ending December 31, 2008.

² The SBA's performance goal, called target benchmark, is based on actuarial projections and economic conditions. Over the long term, i.e., 15 to 30 years, the board strives for an overall fund benchmark of 5% above inflation.

³ The comparable benchmark is the median rate of return achieved by 240 public and private institutional pension plans nationwide. Source: OPPAGA analysis of State Board of Administration data.

SBA officials report that investment results for the last 3½ years represent short-term results and that SBA's investing horizon is for 15 to 30 years and generally designed to withstand short-term market conditions. SBA managers routinely set investment performance goals, or benchmarks, with the goal being to achieve an overall fund rate of return of 5% above inflation averaged over a 15- to 30-year period.

³ A mortgage-backed security is a debt obligation (e.g., a bond) whose cash flows are backed by principal and interest payments from a pool of residential mortgage loans.

Benchmarks are based on economic conditions, actuarial projections, and market indices.⁴ Actuarial projections help the board determine how much money the plan needs to remain fully funded, given the life span of pension participants, their salaries, and workforce growth.

Despite the present economic downturn and the losses sustained, the overall fund for 2007-08, exceeded its 5- and 10-year internal benchmarks and its 5- and 10-year comparable benchmarks. The comparable benchmark measures the fund's performance against composite results of 240 other public and private institutional pension funds. These results indicate that nationwide pension plan investment returns are falling. Short-term losses will likely continue until the economy rebounds.

The SBA's 15- to 30-year time horizons have heretofore been designed to withstand these losses. Annually, the board commissions an external consultant to project the likelihood that different investment strategies (e.g., the percentage of stocks, bonds, etc., invested) will continue to earn rates of return sufficient to pay plan participants over the long term (15 to 30 years) under different economic scenarios and projections. The board will receive new projections in March 2009 and at that time will determine if it needs to revise its long-term investment strategy.

FRS Investment Plan performance was also negatively affected by the global economy. Similar to the FRS pension plan's performance, the investment plan's returns increased in Fiscal Year 2005-06 and 2006-07, but began declining in Fiscal Year 2007-08. Specifically, by the end of Fiscal Year 2007-08, the investment plan's one-year rate of return was a negative 4.69% (see Exhibit 4). By December 2008, the fund lost another 14.5%, or \$633 million in assets. These results mirror the worldwide economy's general decline.

Investment plan participants choose their investment strategies and the percentages of their assets that they want to invest in various asset classes such as stocks, bonds and cash. Since public employees, rather than the State Board of Administration, make these choices, the board has limited control over

performance results. Appendix B shows investment returns for the fund's different asset classes.

Exhibit 4 FRS Investment Plan Returns Declined with the Economy But Benchmarks Have Been Met

Primary Funds	Investment Plan Returns			
	FY 2005-06	FY 2006-07	FY 2007-08	December 31, 2008 ¹
Overall Portfolio Returns				
1-Year Return	10.18%	16.01%	-4.69%	-23.22%
Benchmark Return	9.35%	16.29%	-5.99%	-23.36%
Met or exceeded benchmark?	Yes	No	Yes	Yes
3-Year Return	10.98%	11.50%	6.80%	-2.37%
Benchmark Return	10.90%	11.38%	6.12%	-2.53%
Met or exceeded benchmark?	Yes	Yes	Yes	Yes
5-Year Return	NA²	NA²	8.61%	2.02%
Benchmark Return	NA ²	NA ²	8.32%	1.75%
Met or exceeded benchmark?	NA ²	NA ²	Yes	Yes

¹ Reported returns are for the 1-, 3-, 5-, and 10-year periods ending December 31, 2008.

² The Investment Plan was established in Fiscal Year 2002-03, so there are no five-year returns for these two fiscal years.

Source: OPPAGA analysis of State Board of Administration data.

How does the SBA oversee the pension and investment plans?

Although the State Board of Administration has several procedures in place to oversee the Florida Retirement System pension and investment plans, independent consultants report that these procedures need strengthening. Exhibit 5 describes the board's current oversight procedures for the pension plan. As shown, each month SBA managers monitor the funding status of the pension plan, evaluate the financial performance of both the pension and investment plans, conduct analyses to ensure investment managers' activities comply with law and policy, and monitor the investment performance of these managers. External managers who do not comply with investing requirements or who fail to meet their benchmarks are placed on a watch list and terminated if their performance does not improve or SBA's issues of concern are not addressed.⁵

⁴ A market index tracks and measures changes in the performance of a specific group of stocks, bonds, or other investments from a specific starting point—generally July 1 of each fiscal year for FRS investments. As an example, the SBA domestic equities portfolio is measured against the Russell 3000 index, which contains 98% of all U.S. stocks.

⁵ External managers are also terminated if there are changes in the investment firm, such as key employees leave or the firm is sold to a competitor. Board officials report that such terminations are not uncommon.

Similar oversight procedures are used for the FRS investment plan. For example, SBA managers have promulgated investment policies and guidelines to monitor the plan's 21 external investment managers and monthly analyzes the investment returns of these managers to help ensure that they comply with policy and law. Board officials also conduct analyses to verify that managers' reported investment results are accurate. As with the pension plan's investment managers, under-performing investment managers are placed on a watch list and terminated if their performance does not improve or SBA's issues of concern are not addressed.

Both the Legislature and audit staff appointed by board trustees hired consulting firms to review board operations after local government officials were unable to withdraw funds from the Local Government Investment Pool.⁶ These independent consultants report that board oversight procedures need to be strengthened. The consultants faulted the board for not having an independent compliance

unit to help ensure that SBA managers follow and comply with the oversight procedures shown below. The consultants also concluded that the board needs to implement better internal controls by segregating its management and oversight functions. Board managers are currently in the process of evaluating the cost and feasibility of the consultants' recommendations and how it can best implement these recommendations. The board will make implementation decisions within the next 6 to 18 months.

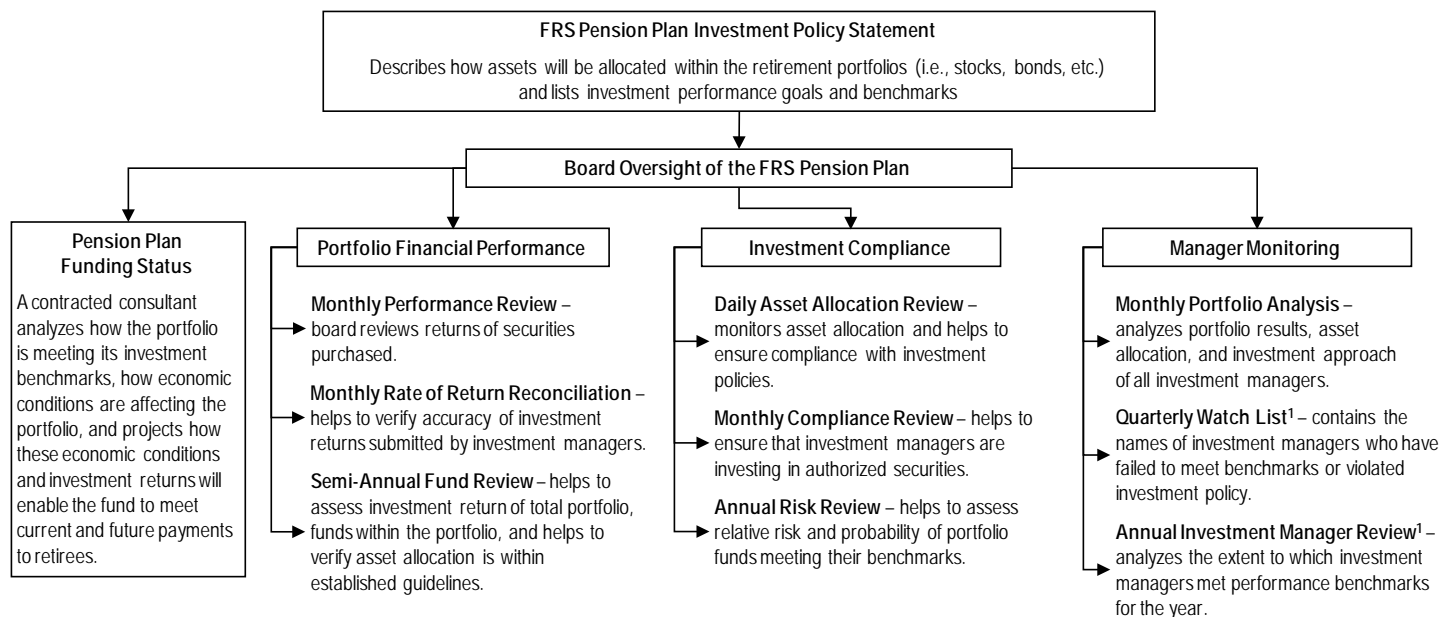
Are the fees the SBA pays external pension plan investment managers comparable to those paid by other states?

Florida falls within the mid-range of states regarding the fees and commissions that are paid to external investment management firms to select, purchase, and manage the securities comprising the Florida Retirement System Pension fund (see Exhibit 6).⁷

⁶ The fund was insufficiently liquid to allow local officials to withdraw needed funds, creating financial difficulties for some local governments. In response to the findings of both consulting firms, the board hired a national management consulting firm to help it implement corrective action procedures.

⁷ Comparison states were chosen based on the following factors: the asset value of the state's retirement portfolio was comparable to Florida—California and New York; the portfolio was fully funded with assets exceeding liabilities—Delaware, North Carolina, Oregon, and Wisconsin; states were in the southeastern region—Georgia and Tennessee; and states were specifically requested for our review—Texas and Washington.

Exhibit 5 SBA Has Various Monitoring Procedures to Oversee the FRS Pension Plan



¹ With the exception of Real Estate Investment Trust accounts, there is no watch list or annual review of investment managers for the real estate and private equity portfolios because these investments are not traded in the public markets, are generally held for the long term (10 years), and are generally illiquid in nature.

The SBA negotiates these fees and commissions with each management firm. Among the states we surveyed, fees as a percentage of net assets ranged from 0.092% to 0.411%, with Florida falling between New York and California, the nation's two other largest retirement funds. The board paid management fees of \$223 million, \$247 million, and \$299 million in Fiscal Years 2005-06, 2006-07, and 2007-08, respectively.

Exhibit 6

As a Percentage of Fund Assets, Florida Falls in the Mid-Range of States for Fees and Commissions Paid to External Investment Managers

States ¹	Fees and Commissions (in thousands)	Total Net Assets (in thousands)	Fees and Commissions (% of Net Assets)
Tennessee	\$ 29,818	\$ 32,365,969	0.092%
Georgia	17,143	17,516,903	0.098%
Texas	24,609	24,463,828	0.101%
New York	203,730	156,625,243	0.130%
Florida	247,546	136,280,545	0.182%
California	516,376	252,612,943	0.204%
Wisconsin	170,854	80,466,980	0.212%
North Carolina	214,915	76,899,353	0.279%
Delaware	21,044	7,413,370	0.284%
Washington	232,434	64,077,004	0.363%
Oregon	258,692	62,891,942	0.411%

¹Not every state has a plan equivalent to Florida's defined contribution plan. The results shown are for each state's defined benefit pension plan. Additionally, not every state has calculated its fees for the 2007-08 Fiscal Year. These data are for the 2006-07 year, which was the year all the data were available for all the comparison states.

Source: Fees and commissions posted on official state websites, most current information available as of January 2009.

How well does the SBA communicate its investment results to stakeholders?

The State Board of Administration needs to strengthen its communication with stakeholders. Best practices for pension plan governance call for fund managers to issue annual reports to stakeholders in a manner that provides for openness, transparency, and accountability. Although the board annually publishes reports describing the status of the state's debt service, protocols for protecting funds in the case of disaster, and its proxy voting activity for securities it owns, the board's primary report to stakeholders remains its annual report. As such, the annual report should demonstrate to stakeholders, including the public employees whose retirement funds it invests,

what oversight the board took to protect the funds and how its various investments performed against associated financial markets and benchmarks.

The board's annual report provides useful information but needs to be improved. Specifically, the report generally does not inform stakeholders in plain terms what oversight steps the SBA took to protect the funds and provides little context for how well it invested the funds under SBA's stewardship. For example, the report includes tables of investment results but does not provide accompanying benchmarks against which to evaluate fund performance. In addition, the report does not adequately disclose investment outcomes for its more controversial alternative investments (now called private equity). The report does not provide one-year results for these investments with other summary investment results. Instead, the report discloses these results in text, along with performance benchmarks, which commonly require manual calculation before performance can be assessed. Moreover, the report provides little description of the types of investments comprising the various asset classes, and the descriptions that are provided are often unclear. Also, the report does not readily disclose how much stakeholders paid in total investment fees for internal and external investment management for the pension and investment plans.

Augmenting these results with clear descriptions of each asset class and the investing environment will better conform to best practices and improve board accountability to stakeholders. These improvements to the SBA's annual report would better inform all stakeholders—regardless of their financial sophistication—of what oversight the board provides to assets under its stewardship and how well it has invested those funds compared to broad financial markets and benchmarks.

Has the SBA taken corrective action to address previous OPPAGA findings?

Past OPPAGA reports have concluded that the State Board of Administration generally performed well in achieving its pension plan objectives but needed to improve reporting information to stakeholders. We determined that the board either addressed or has committed to address most prior OPPAGA recommendations. In 2004 and 2006, we recommended that the board provide an analysis of the Florida Retirement System's future funding

needs to the Legislature.⁸ The board commissions, on an annual basis, an external consultant to assess the likelihood that different investment strategies (the percentage of funds invested in stocks, bonds, and other assets) will earn rates of return sufficient to pay plan participants over a 15-year period under various economic scenarios. SBA officials indicated that after the board receives this information each year (typically in March), it will forward these analyses to the Legislature so that it is apprised of the results of the study.

Similarly, in 2002, we recommended that the board assess and report private equity investments against its short and long-term benchmarks.⁹ The board has implemented this recommendation for its 3-, 5-, and 10-year benchmarks. However, the board does not report its one-year investment performance in its summary table of all asset class performance results. Beginning with Fiscal Year 2008-09, officials report that in future reports, they also will include one-year investment returns in the performance table so stakeholders can see short and long-term investment performance for all asset classes.

Conclusions and Recommendations

Nationwide, pension plan investment returns are falling and returns for Florida Retirement System investments are consistent with this trend. Short-

term losses will likely continue until the economy rebounds. In context of the global economic downturn, the State Board of Administration continues to generally meet its investment objectives and outperforms many other public and private institutional pension funds.

However, the board needs to improve its accountability to stakeholders through better communication of its investment results, activities, and the pension plan's future funding needs. Such information should readily indicate what investment results the board achieved, how the board's investments compared to broader market indices and benchmarks, and how much investment services cost. The SBA's annual report should provide this information, written so that all stakeholders, regardless of financial sophistication, can readily comprehend the text. As such, we recommend that the board revise and simplify its annual investment report by addressing those criticisms detailed in text. We also recommend that results for all asset classes, including private equity, be posted in summary performance tables, rather than embedded in text. Lastly, we recommend that the board follow through on its stated intention of informing the Legislature about the pension plan's future funding needs by providing legislators copies of the FRS funding needs analysis, as was recommended in two previous OPPAGA reports.

Agency Response

In accordance with the provisions of s. 11.51(5), *Florida Statutes*, a draft of our report was submitted to the executive director of the State Board of Administration for review and response. The executive director's written response is included in Appendix C.

⁸ *Use of Investment Returns Has Increased; Plan for Addressing Associated Risks Should Be Documented*, [Report No. 06-68](#), November 2006 and *Multi-Year Projections of Retirement System Funding Should Be Provided to the Legislature*, [Report No. 04-70](#), October 2004.

⁹ *While State Board of Administration Investments Perform Relatively Well, the SBA Should Reassess Planned Expansion of Alternative Investments*, [Report No. 02-37](#), June 2002. *Multi-Year Projections of Retirement System Funding Should Be Provided to the Legislature*, [Report No. 04-70](#), October 2004.

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Appendix A

Asset Classes Comprising the Pension Plan Incurred Losses During the Past Fiscal Year

Just as overall fund returns for the Florida Retirement System Pension Plan showed recent losses, the various asset classes comprising the overall fund also sustained losses, as did the market indices associated with each asset class.¹⁰ These indices served as benchmarks against which the board measured its investment performance in each asset class. As can be seen in Table A-1, stock investments comprised the largest portion of the fund for the three fiscal years and exhibited characteristic short-term volatility. Domestic and foreign equities, combined, represented the strongest financial gains for the fund in the first two fiscal years and the biggest losses during the last fiscal year.

The short-term volatility of stocks is balanced by fixed income securities, like bonds, which generally tend to be more stable in the short term. Although bond returns had virtually no effect on the fund in Fiscal Year 2005-06, they improved in the succeeding fiscal years, and offset some of the domestic and foreign equity losses in Fiscal Year 2007-08.¹¹ Real estate returns declined steadily over the three-year period. Investment returns for cash and short-term securities also declined, from mid-single digit returns to less than 1%, as demand for securities backed by mortgages decreased during Fiscal Year 2007-08. These results generally reflect the current economic downturn.

¹⁰ A market index tracks and measures changes in the performance of a specific group of stocks, bonds, or other investments from a specific starting point—generally July 1 of each fiscal year for FRS investments. As an example, the SBA domestic equities portfolio is measured against the Russell 3000 index, which contains 98% of all U.S. stocks.

¹¹ Although exhibiting short-term volatility, stocks typically provide the highest rates of return over time and, since 1929, have averaged a return of 10% a year.

Table A-1
Pension Plan Returns Declined with the Economy, Meeting Only Half the Benchmarks

Asset Class	FRS Pension Plan Returns by Asset Class			
	FY 2005-06	FY 2006-07 ¹	FY 2007-08 ¹	December 31, 2008 ²
Domestic Equities – Stocks exclusively from U.S. companies	9.04%	19.60%	-12.70%	-37.41%
Benchmark return	9.55%	20.07%	-12.68%	-37.31%
Met or exceeded benchmark?	No	No	No	No
Percentage of fund	50.40%	42.9%	35.50%	33.76%
Foreign Equities – Stocks exclusively from countries outside of the U.S.	26.43%	29.82%	-6.68%	-44.35%
Benchmark return	27.90%	29.62%	-7.62%	-46.14%
Met or exceeded benchmark?	No	Yes	Yes	Yes
Percentage of fund	15.20%	16.4%	18.70%	17.65%
Fixed Income – Investments that yield a regular (or fixed) return, e.g., bonds	0.02%	6.39%	5.42%	-3.96%
Benchmark return	-0.50%	6.53%	7.12%	5.24%
Met or exceeded benchmark?	Yes	No	No	No
Percentage of fund	21.30%	22.9%	27.6%	27.77%
Real Estate – office, retail, industrial, and apartment buildings as well as real estate investment trusts, which are publicly traded real estate securities	23.48%	16.11%	8.69%	-1.50%
Benchmark return	9.09%	6.41%	10.12%	-1.06%
Met or exceeded benchmark?	Yes	Yes	No	No
Percentage of fund	4.90%	6.0%	7.70%	9.45%
Cash Equivalents - cash and high quality securities that that can be sold in less than one year with little loss of value	4.31%	5.43%	0.86%	-5.80%
Benchmark return	4.35%	5.30%	4.44%	2.99%
Met or exceeded benchmark?	No	Yes	No	No
Percentage of fund	0.80%	2.9%	0.90%	1.13%
Private Equity – stocks in companies that are not publicly traded on a stock exchange	13.15%	12.90%	7.52%	-4.30%
Benchmark return	14.06%	24.60%	-8.19%	-32.81%
Met or exceeded benchmark?	No	No	Yes	Yes
Percentage of fund	3.10%	3.20%	3.40%	4.45%
High Yield – bonds that have a high potential of return to compensate for their higher risk	NA ³	NA ³	0.99%	-18.37%
Benchmark return	NA ³	NA ³	0.09%	-22.05%
Met or exceeded benchmark?	NA ³	NA ³	Yes	Yes
Percentage of fund	NA ³	NA ³	2.20%	2.31%
Strategic Investments – real estate debt, city, county, and state infrastructure projects, timberland, and corporate governance activist funds designed to improve returns on undervalued companies	NA ⁴	NA ⁴	-8.86%	-37.36%
Benchmark Return	NA ⁴	NA ⁴	-8.51%	-33.59%
Met or exceeded benchmark?	NA ⁴	NA ⁴	No	No
Percentage of fund	NA ⁴	NA ⁴	4.10%	3.47%

¹The SBA's 2006-07 and 2007-08 Investment Report lists returns that are both higher and lower than reported here, stating in footnotes that certain trades were included and others excluded from their calculations. The numbers presented here reflect all trades executed by the SBA.

² Reported returns are for the 1-, 3-, 5-, and 10-year periods ending December 31, 2008.

³In June 2007, High Yield was removed from Fixed Income and placed into its own asset class. High Yield represented 1.3% of the total asset allocation as of June 30, 2007.

⁴This is a new asset class that received initial funding in June 2007, which represented 4.4% of the total asset allocation as of June 30, 2007.

Source: OPPAGA analysis of State Board of Administration data.

Appendix B

Most Asset Classes in the Investment Plan Incurred Losses During the Past Fiscal Year

Similar to the pension plan, asset classes within the Florida Retirement System Investment Plan experienced investment losses, as did many of their associated market indices. As shown in Table B-1, the biggest losses for Fiscal Year 2007-08 were in domestic equities and foreign/global equities. The biggest gains during the past fiscal year were in U.S. treasury inflation-protected securities and fixed income. With the exception of treasury inflation-protected securities and fixed income, all asset classes performed more poorly in the last fiscal year than in preceding years, again reflecting the market's overall decline.

Table B-1
Investment Plan Returns Have Declined with the Economy

Returns by Asset Class	Investment Plan Returns			
	FY 2005-06	FY 2006-07	FY 2007-08	December 31, 2008 ¹
Domestic Equities - Stocks exclusively from U.S. companies	12.06%	18.84%	-11.91%	-36.52%
Benchmark Return	10.83%	19.57%	-13.24%	-36.46%
Met or exceeded benchmark?	Yes	No	Yes	No
Percentage of Fund	35.50%	31.90%	26.10%	21.01%
Foreign/Global Equities - Stocks from both the U.S. and foreign countries	25.2%	26.67%	-6.46%	-40.88%
Benchmark Return	23.78%	26.16%	-9.59%	-42.78%
Met or exceeded benchmark?	Yes	Yes	Yes	Yes
Percentage of Fund	8.80%	12.10%	11.20%	8.26%
Fixed Income - Investments that yield a regular (or fixed) return, e.g., bonds	-0.31%	6.41%	6.98%	1.39%
Benchmark Return	-0.32%	6.61%	6.21%	1.95%
Met or exceeded benchmark?	Yes	No	Yes	No
Percentage of Fund	9.10%	8.10%	9.00%	9.85%
Treasury Inflation-Protected Securities - Inflation-indexed bonds issued by the U.S. Treasury whose interest rate is linked to inflation	-1.63%	3.94%	15.30%	-2.03%
Benchmark Return	-1.64%	3.99%	15.09%	-2.35%
Met or exceeded benchmark?	Yes	No	Yes	Yes
Percentage of Fund	3.00%	2.10%	4.00%	4.35%
Cash Equivalents - cash and high quality securities that that can be sold in less than one year with little loss of value	4.42%	5.49%	4.13%	2.42%
Benchmark Return	4.34%	5.48%	4.45%	2.99%
Met or exceeded benchmark?	Yes	Yes	No	No
Percentage of Fund	9.60%	8.80%	11.80%	19.55%
Balanced Fund - stocks, bonds, and money market funds	10.35%	16.68%	-4.68%	-22.76%
Benchmark Return	9.81%	16.84%	-4.98%	-23.34%
Met or exceeded benchmark?	Yes	No	Yes	Yes
Percentage of Fund	34.10%	37.00%	37.90%	36.98%

¹ Reported returns are for the 1-, 3-, 5-, and 10-year periods ending December 31, 2008.

Source: OPPAGA analysis of State Board of Administration data.

Appendix C



STATE BOARD OF ADMINISTRATION
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CHIEF FINANCIAL OFFICER
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BILL MCCOLLUM
ATTORNEY GENERAL
AS SECRETARY
ASH WILLIAMS
EXECUTIVE DIRECTOR & CIO

March 5, 2009

Gary R. VanLandingham, Ph.D., Director
Office of Program Policy Analysis and
Government Accountability
Room 312 Claude Pepper Building
111 West Madison Street
Tallahassee, FL 32399-1475

Dear Dr. VanLandingham:

We reviewed the Office of Program Policy Analysis and Government Accountability's (OPPAGA) preliminary findings and recommendations contained in the report titled: *Retirement Fund Investments Decline with the Economy But Still Meet Several Performance Benchmarks; SBA Must Improve Communication with Its Stakeholders*. We offer the following responses in regard to the information presented in the report.

1. The State Board of Administration agrees to revise and simplify its Annual Investment Report, starting with the Fiscal Year 2008-09 edition, as necessary to:
 - a. Readily indicate what investment results the board achieved, how the board's investments compared to broader market indices and benchmarks, and how much investment services cost;
 - b. Provide information, written so that all stakeholders, regardless of financial sophistication, can readily comprehend the text; and
 - c. Post results for all asset classes, including private equity, in summary performance tables, rather than embedded in text.
2. The State Board of Administration agrees to annually communicate the results of its Florida Retirement System funding needs analysis to the Legislature.

We welcome OPPAGA's efforts and, as always, we appreciate your diligence and professionalism.

Sincerely,

Ashbel C. Williams
Executive Director & CIO