

State Board of Administration of Florida
Florida Retirement System (FRS) Investment Plan Trust Fund

Fiscal Years Ended June 30, 2019 and 2018

FINANCIAL STATEMENTS, NOTES TO THE FINANCIAL STATEMENTS,
AND MANAGEMENT'S DISCUSSION AND ANALYSIS

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INDEPENDENT AUDITOR'S REPORT

The Board of Trustees
State Board of Administration of Florida

Report on the Financial Statements

We have audited the accompanying financial statements of the Florida Retirement System ("FRS") Investment Plan Trust Fund (the "Trust") administered by the State Board of Administration ("SBA") of Florida, as of and for the years ended June 30, 2019 and 2018, and the related notes to the financial statements, which collectively comprise the Trust's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Trust administered by the SBA as of June 30, 2019 and 2018, and the changes in financial position for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the Trust and do not purport to, and do not, present fairly the financial position of the State of Florida, the State Board of Administration of Florida or the Florida Retirement System as of June 30, 2019 and 2018, their changes in financial position, or, where applicable, their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the *management's discussion and analysis* on pages 3 – 13 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 5, 2019 on our consideration of the Trust's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Trust's internal control over financial reporting and compliance.


Crowe LLP

Tampa, Florida
November 5, 2019

Management's Discussion and Analysis

Introduction

This section of the financial statements of the Florida Retirement System (FRS) Investment Plan Trust Fund (the Trust) presents management's discussion and analysis of the Trust's financial position for the fiscal years ended June 30, 2019 and 2018. Please read it in conjunction with the basic financial statements and the accompanying notes, which follow this section.

As further described in Note 1 to the financial statements, the FRS Investment Plan (the Plan) is a defined contribution plan for eligible members of the FRS who have not elected to participate in the FRS Pension Plan, a defined benefit plan, or who are mandated to participate in the Plan as a condition of renewed membership in the FRS.

The Plan is administered by the State Board of Administration of Florida (the SBA). The SBA has defined the roles and responsibilities of affected employers, the Division of Retirement within the Department of Management Services (DMS) and other service providers pertaining to the Plan. The Florida Legislature is responsible for setting contribution rates and providing statutory authority to the SBA for the administration of the Plan.

Contributions to the Plan are collected by DMS and transmitted to the SBA, which deposits them in the Trust. Alight Solutions, the Plan Administrator contracted by the SBA, is responsible for the placement of member-directed trades among investment options offered by the Plan and maintaining records of individual member accounts. Members choose from a diverse offering of low-cost investment options which include institutional and mutual funds selected by the SBA. In addition, a Self-Directed Brokerage Account (SDBA) investment option is also available (see Note 3 to the financial statements). Alight Solutions records in each member's account all relevant contributions, withdrawals, fees, and the investment performance of the funds selected by the member. The benefits each member receives from the Plan vary based on the member's individual account balance.

Management's Discussion and Analysis

Financial Statements

The financial reporting entity represented in the basic financial statements and accompanying notes is the Trust, which consists of the assets held in trust by the SBA for the payment of retirement benefits and reasonable administrative expenses of the Plan. The assets, liabilities, and net position of the Trust are reported in the comprehensive annual financial reports (CAFRs) published by the State of Florida and the DMS.

The Trust's basic financial statements include two-year comparative statements of net position and statements of changes in net position. The statements of net position provide information on the financial position of the Trust as of the end of each fiscal year. The statements of changes in net position present the results of Trust activities during the fiscal years presented in this report. The accompanying notes to the financial statements offer additional discussion that is essential for a full understanding of the data presented in the financial statements, and provide more detail about accounting policies, significant account balances and activities, material risks, obligations, contingencies, and subsequent events, if any.

Statements of Net Position

The statements of net position present the assets, liabilities, and net position (total assets in excess of total liabilities) of the Trust as of the end of the fiscal year and are point-in-time financial statements. The assets in the Trust are comprised of the members' investment accounts. The following table represents condensed financial information.

	As of June 30		
	2019	2018	2017
	(In Millions)		
Assets			
Investments	\$ 11,275	\$ 10,862	\$ 10,007
Receivables	51	45	40
Investments sold, but not settled	28	53	43
Total assets	11,354	10,960	10,090
Liabilities			
Payables	2	3	3
Investments purchased, but not settled	57	86	78
Total liabilities	59	89	81
Net position held in trust	<u>\$ 11,295</u>	<u>\$ 10,871</u>	<u>\$ 10,009</u>

Management's Discussion and Analysis

Statements of Changes in Net Position

The statements of changes in net position show the net investment income earned by the Trust, the contributions from employers and employees, and the withdrawals for members and beneficiaries that occurred during the fiscal year. The following table represents condensed financial information.

	Fiscal Years Ended June 30		
	2019	2018	2017
	<i>(In Millions)</i>		
Additions			
Net investment income	\$ 547	\$ 945	\$ 1,163
Contributions:			
Employer/employee contributions received from DMS	487	433	397
Member-directed benefits received from the FRS Trust Fund	565	597	569
Member-directed rollover deposits	65	62	69
Total contributions	1,117	1,092	1,035
Total additions	1,664	2,037	2,198
Deductions			
Benefit payments to members	1,151	1,097	1,070
Member-directed benefits sent to the FRS Trust Fund	84	71	71
Administrative expenses	5	7	8
Total deductions	1,240	1,175	1,149
Change in net position	424	862	1,049
Net position held in trust			
Beginning of year	10,871	10,009	8,960
End of year	\$ 11,295	\$ 10,871	\$ 10,009

Management's Discussion and Analysis

Analysis

The Trust's net position increased by \$424 million (3.9%) and increased by \$862 million (8.6%) during fiscal years 2019 and 2018, respectively. For both fiscal years 2018 and 2019, the growth in net position was due primarily to positive investment performance, with continued strength in the equity markets and lower yields generating increased fixed income appreciation. As well, a marginal increase in overall contributions provided some additional funds for investment in the Trust.

Trust investments generated net income of approximately \$547 million in fiscal year 2019 and \$945 million in fiscal year 2018. Equity investment performance contributed substantially to both fiscal years' net investment income. Domestic equities returned nearly 7% for fiscal year 2019 and just under 16% for fiscal year 2018. International equity performance was not as robust in fiscal year 2019 compared to 2018, but both years posted positive results. International equity returns were 1.6% and 9.2% for fiscal years 2019 and 2018, respectively. Fixed income returns improved in fiscal year 2019, exceeding 8%, versus 0.2% for fiscal year 2018. Lower yields provided for growth in these investments, producing continued growth in Trust net investment income and overall net position. Additional analysis of Trust investments can be found in the "Asset Allocation" and "Investment Returns" sections of Management's Discussion and Analysis.

Deductions from the Trust in both fiscal years consist mainly of benefit payments to members. Benefit payments increased by \$54 million (4.9%) and increased by \$27 million (2.5%) during fiscal years 2019 and 2018, respectively. Benefits payments from the Plan vary from year to year based on the number of retirees, their account balances, and the related benefits due during the fiscal year.

Additional Plan highlights and trends follow.

Management's Discussion and Analysis

Plan Participation and Membership

The number of employers participating in the Plan varied slightly over the last three fiscal years. Overall Plan membership increased significantly over that same time period, particularly in fiscal year 2019 due to the Plan default change (see the "Plan Choice" section of Management's Discussion and Analysis).

	As of June 30		
	2019	2018	2017
Participating employers	976	1,001	994
Plan membership:			
Active members ¹	148,161	130,466	121,205
Inactive members ²	65,052	60,198	56,013
Total Plan members	213,213	190,664	177,218

¹ Active members are those employees currently receiving contributions into their retirement account.

² Inactive accounts are held on behalf of members who are no longer employed by an eligible employer, so their accounts are not receiving contributions at this time. This includes retirees with a remaining balance, plan beneficiaries and alternate payees as a result of a Qualified Domestic Relations Order.

Active Plan Membership by Class

Over the last three fiscal years, active Plan membership has continued to increase across most of the membership classes, though some variation is expected from year to year.

	As of June 30						
	Regular	Senior Management	Special Risk Admin	Elected Officers	Special Risk	Other	Total
2019	131,035	2,228	22	534	12,057	2,285	148,161
2018	112,303	2,330	18	547	12,055	3,213	130,466
2017	105,060	2,256	25	517	10,915	2,432	121,205

Management's Discussion and Analysis

Plan Choice

Effective January 1, 2018, Chapter 2017-88, Laws of Florida was signed into law amending section 121.4501(4), Florida Statutes. The law provides that all new hires will have until the last business day of the 8th month after hire to make a choice between the FRS Pension Plan and FRS Investment Plan. If a new hire does not make an active election by the deadline date, the new hire will default into the FRS Investment Plan, except those who are enrolled in the Special Risk Class (who will still default to the FRS Pension Plan). The first group of new hires defaulted into the FRS Investment Plan effective October 1, 2018. For fiscal year ended June 30, 2019, 51% of all new hires defaulted to the FRS Investment Plan and 19% made an active election to enroll in the FRS Investment Plan. Based upon the limited data available, it is too soon to provide trend information or projections as to the effect the plan change amendment may have on the Trust's net position.

The number of new employees eligible to make an initial retirement plan choice continues to fluctuate from year to year. The percentage of employees making active elections to the Investment Plan showed some variation over the last three fiscal years as well. Most notably, the percentage of active elections in fiscal year 2019 decreased to 19% from the previous fiscal year rate of 24%, as employees begin entering the Investment Plan by default rather than by active election only. The number of employees joining the Investment Plan through a Second Election continues to decline.

	Fiscal Years Ended June 30		
	2019	2018	2017
New employees making initial plan choice	47,852	56,517	61,511
Number of new employees joining			
FRS Investment Plan:	33,418	13,537	13,866
Active election	19%	24%	23%
Plan default	51%	0%	0%
Employee Second Elections ¹ :			
To the FRS Investment Plan	3,270	3,871	4,019
To the FRS Pension Plan	1,067	766	792

¹ Florida Retirement System members are granted a one-time option to transfer from one retirement plan (Pension or Investment) to the other during their FRS-covered employment. This is considered a Second Election.

Management's Discussion and Analysis

Benefit Payments

Benefit payments reflect withdrawals from the Trust in the form of lump sum distributions, partial distributions, rollovers to other qualified retirement plans, and periodic payments to members. The number of members requesting benefit payments during the year increased by 4,155 (7.4%) and increased by 3,285 (6.2%) for fiscal years 2019 and 2018, respectively. The annual amount of benefits disbursed to Plan members varies from year to year due to the number of retirees and the benefit payment amounts due. Benefit payments increased by \$54 million (4.9%) in fiscal year 2019, compared to a \$27 million (2.5%) increase in fiscal year 2018.

	Fiscal Years Ended June 30		
	2019	2018	2017
Members requesting benefits	60,600	56,445	53,160
Benefit payments (<i>In Millions</i>)			
Rollovers	\$ 655	\$ 627	\$ 629
All other	496	470	441
Total benefit payments	<u>\$ 1,151</u>	<u>\$ 1,097</u>	<u>\$ 1,070</u>

Contribution Rates

Employer contribution rates, which are established by the Legislature and reflected in Section 121.72, *Florida Statutes*, vary by membership class but have remained stable as a percentage of compensation for the last three fiscal years.

Membership Class	Employee Rate	Employer Rate ¹
	FYs 2017-2019	FYs 2017-2019
Regular	3.00 %	3.30 %
Special risk	3.00	11.00
Special risk: administrative support	3.00	4.95
Legislators	3.00	6.38
Governor, Lt. Governor, and cabinet officers	3.00	6.38
State Attorney and public defenders	3.00	6.38
Justices and judges	3.00	10.23
County and local elected officers	3.00	8.34
Senior management service	3.00	4.67

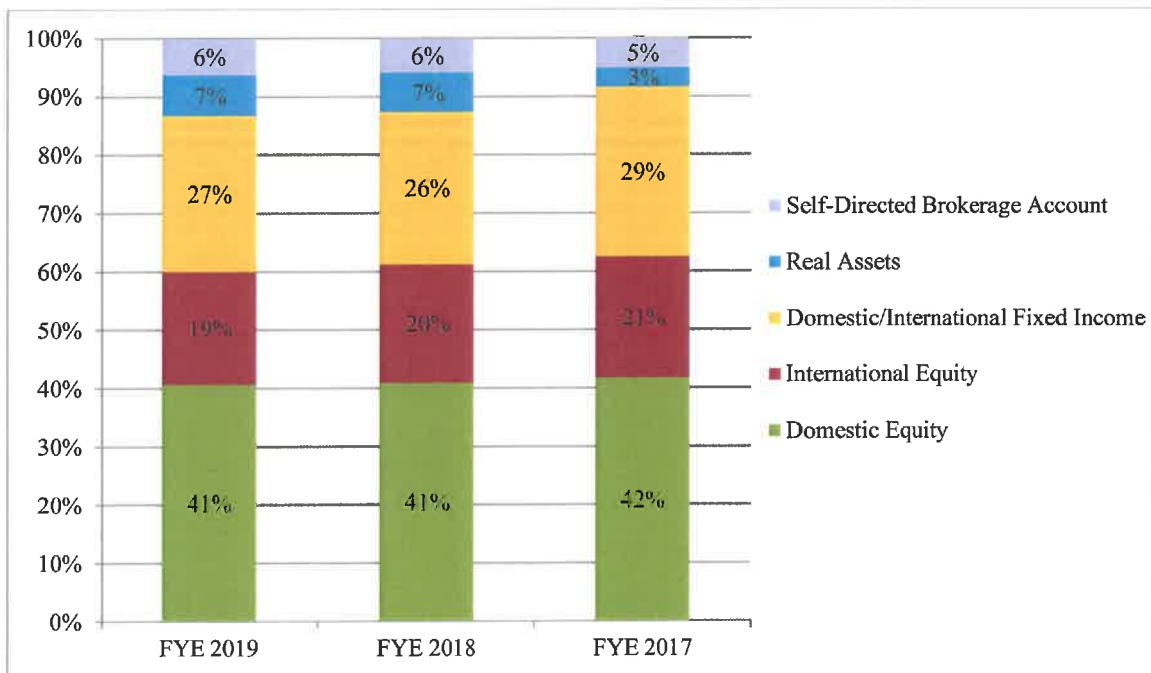
¹ Employer rates presented in this table do not include employer contributions for the Health Insurance Subsidy (1.66% for FYs 2017-2019), plan administrative/educational expense (.06% for FYs 2017-2019) or the disability and in line-of-duty death programs (varies by membership class) as these amounts are not deposited into the Trust.

Management's Discussion and Analysis

Asset Allocation

The asset allocation of the Trust is a function of the members' investment decisions across the various investment options offered. Equity investments (domestic and international combined) remained the largest allocation, as members looked to capitalize on the long-term growth prospects of these assets. Allocations to fixed income investments have declined for a number of years due in part to performance expectations relative to other investment options, although fiscal year 2019 experienced some allocation growth with recent changes in yields and concerns over a possible equity market downturn. A new institutional real estate managed account was added to the Trust's real asset allocation in 2018. This managed account made-up the bulk of the fiscal year 2018 increase in real asset investments and the allocation to it remained relatively consistent for fiscal year 2019. The institutional real estate managed account is available only within the Retirement Date Funds. Members continued their allocations to the Self-Directed Brokerage Account, which allows for additional investment flexibility. Note 3 to the financial statements describes the Plan's Investment Policy Statement (IPS) and oversight of the Trust's investments.

By Percentage of Invested Assets¹



¹ International fixed income represents a small fraction (less than 1%) of the overall Trust investments and is combined with domestic fixed income for charting purposes.

Management's Discussion and Analysis

Investment Returns

The Trust's performance is a function of the members' decisions about their asset allocations and the investment options' performance. The SBA does not influence asset mix decisions; however, investment performance affects the Trust's net position.

The Trust's investment returns¹ were as follows:

Investment Type	Fiscal Years Ended June 30		
	2019	2018	2017
Retirement Date Funds ²	5.4 %	8.4 %	13.2 %
Short-term	2.5	1.7	0.9
Real assets	2.6	5.6	3.5
Fixed income	8.1	0.2	2.1
Domestic equity	6.8	15.9	20.1
International equity	1.6	9.2	21.0
Total Trust return	5.2 %	9.6 %	13.4 %
Total Trust aggregate benchmark	5.2	8.8	12.6
Over (under) benchmark	- %	0.8 %	0.8 %

¹ The investment performance information shown above for each fiscal year is the official investment return data supplied by the SBA's master custodian and performance measurement service provider, BNY Mellon Performance Reporting and Analytics Services.

² Retirement Date Funds consist of Plan fund investments in various proportions.

The Trust's total return for fiscal year 2019 was 5.2%. As of June 30, 2019, the Trust matched its trailing one-year and outperformed its trailing three-, five-, and ten-year period aggregate benchmark. The Trust's overall performance compared with its benchmark reflects the weighted performance for the underlying fund options in which members are investing. Performance for the Self-Directed Brokerage Account is not included since there is no comparable benchmark. Members assume the full risk and responsibility for the investments they have selected in the Self-Directed Brokerage Account and for monitoring the performance of these investments.

More detailed information and analysis of the Trust's performance can be obtained from the SBA's Annual Investment Report, which can be found at www.sbafla.com.

Management's Discussion and Analysis

Economic Factors

The 2019 fiscal year generated another year of positive capital market returns across most asset classes, despite some market volatility throughout the year. The year began by continuing the upward trend where the 2018 fiscal year left off. The U.S. stock market reached a new high and set the record for the longest bull market in U.S. history. Strong gross domestic product (GDP) growth, muted inflation, low unemployment and a positive outlook supported risk assets and the Federal Open Market Committee's (FOMC) monetary tightening cycle. September saw the eighth rate hike in this tightening phase, with another expected in December and more forecasted for 2019. While the U.S. equity market remained strong throughout third quarter 2018, European stocks improved only modestly on solid corporate earnings tempered by concerns over slowing economic growth. Emerging Market stocks were negatively impacted by a strong U.S. dollar, higher interest rates and global trade tension. During fourth quarter 2018, stocks around the world declined with tightening US monetary policy, increased fears of deteriorating US/China trade relations and signs of slowing economic growth.

The market reversed sharply in early 2019 and the fiscal year ended with a repeat of the up and down pattern experienced throughout the year. The S&P 500 Index returned to peak levels in April driven by a less aggressive FOMC. May saw a sell-off in risk assets, especially stocks and credit, as the rhetoric on trade and tariffs escalated once again and global economic growth slowed. Finally, June saw a positive rebound back to peak levels of the stock market after the Federal Reserve and European Central Bank provided reassurance that monetary policy intervention would be available if needed. Despite the resiliency of the stock market, bonds remained cautious on the outlook for growth and inflation, with the 10-year U.S. treasury yield continuing to fall, dipping below 2% at the end of the year.

Overall, most major capital markets generated positive investment results for the 2019 fiscal year. The global equity market generated positive returns, despite the sharp swings and underlying tensions experienced throughout the year. Global equity returns were primarily driven by the broad U.S. equity market, as represented by the Russell 3000® Index, which returned 9.0% over the year and significantly outpaced international equities. In U.S. dollar terms, developed international markets, represented by the MSCI World Ex USA Index, returned 1.3%, while emerging markets represented by the MSCI Emerging Markets Index posted a 1.2% return. As U.S. yields fell meaningfully throughout the year, the U.S. bond market, as represented by the Bloomberg Barclays Aggregate Bond Index, returned 7.9%. Generally propped up by renewed central bank support and absent any materially negative economic reports, capital markets continued to move higher for the 2019 fiscal year despite the concerns of trade wars, fears of recessionary signals and signs of fading fiscal support.

Management's Discussion and Analysis

Contacting the Trust's Financial Management

This financial report is designed to provide citizens, taxpayers, Plan members, and other interested parties with an overview of the Trust's finances and the prudent exercise of the SBA's oversight. If you have any questions regarding this report or need additional information, please contact the Chief of Defined Contribution Programs, State Board of Administration of Florida, P.O. Box 13300, Tallahassee, FL 32317.

Statements of Net Position

	As of June 30	
	2019	2018
	<i>(In Thousands)</i>	
Assets		
Cash and cash equivalents	\$ 426	\$ 21
Investments:		
Fixed income	3,010,333	2,834,472
Equity	6,775,671	6,654,141
Real assets	787,711	740,128
Self-Directed Brokerage Account	700,874	633,004
Total investments	11,274,589	10,861,745
Receivables:		
Accounts receivable	-	13
Interest and dividends	4,225	3,491
Due from DMS	47,078	41,934
Investments sold, but not settled	28,138	53,214
Total receivables	79,441	98,652
Total assets	11,354,456	10,960,418
Liabilities		
Payables:		
Accounts payable and accrued liabilities	2,228	2,574
Due to DMS	34	14
Investments purchased, but not settled	57,197	86,267
Total liabilities	59,459	88,855
Net position held in trust	\$ 11,294,997	\$ 10,871,563

See accompanying notes to the financial statements.

Statements of Changes in Net Position

	Fiscal Years Ended June 30	
	2019	2018
	<i>(In Thousands)</i>	
Additions		
Investment income:		
Dividend income	\$ 49,709	\$ 38,790
Interest and other investment income	10,401	8,728
Net increase/(decrease) in fair value of investments	491,647	902,461
Total investment income	551,757	949,979
Investment expenses:		
Bank fees	(486)	(462)
Investment management fees	(4,428)	(4,383)
Total investment expenses	(4,914)	(4,845)
Net income from investments	546,843	945,134
Contributions:		
Employer/employee contributions received from DMS	486,942	433,372
Member-directed benefits received from the FRS Trust Fund	565,045	597,010
Member-directed rollover deposits	64,373	61,592
Total contributions	1,116,360	1,091,974
Total additions	1,663,203	2,037,108
Deductions		
Benefit payments to members	1,150,577	1,097,066
Member-directed benefits sent to the FRS Trust Fund	83,627	70,597
Administrative expenses	5,565	6,892
Total deductions	1,239,769	1,174,555
Change in net position	423,434	862,553
Net position held in trust		
Beginning of year	10,871,563	10,009,010
End of year	\$ 11,294,997	\$ 10,871,563

See accompanying notes to the financial statements.

Notes to the Financial Statements

1. Financial Reporting Entity

The Florida Retirement System (FRS) Investment Plan (the Plan), a defined contribution pension plan, qualified under IRC Section 401(a), was established pursuant to Section 121.4501, *Florida Statutes*, to provide for retirement benefits for eligible employees of the State and all participating county, district school board, community college and university employees as an alternative to the FRS Pension Plan or other optional retirement plans. Additionally, certain retirees of the FRS who return to employment with a participating employer are mandatory participants of the Plan. Under the Plan, employers and employees make contributions to an account, set up in the member's name, and the member directs the investments in the account, choosing from a number of diverse investment options selected and monitored by the State Board of Administration of Florida (the SBA). The Plan was first offered to public sector employees in fiscal year 2003, and was modeled after private sector 401(k) plans. The Plan's and the SBA's financial activities are reported in the Comprehensive Annual Financial Report (CAFR) of the State of Florida. The SBA is governed by a Board of Trustees, comprised of the Governor, as Chair, the Attorney General, and the Chief Financial Officer of the State of Florida.

The FRS Investment Plan Trust Fund (the Trust) was established pursuant to Section 121.4502, *Florida Statutes*, to hold the assets of the Plan in trust for the exclusive benefit of the Plan's members.

The Trust is a separate legal entity within the State of Florida. These financial statements and notes include only the net position and changes in net position of the Trust and do not purport to, and do not, present fairly the net financial position of the State of Florida, the SBA, or the Plan as of June 30, 2019 and 2018, and the changes in their net financial position for the years then ended, in conformity with accounting principles generally accepted in the United States (GAAP).

2. Summary of Significant Accounting Policies

Basis of Presentation

The financial statements of the Trust were prepared in accordance with GAAP as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and reporting principles. The Trust is accounted for as an investment trust fund pursuant to GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools* (GASB 31), GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* (GASB 34), and GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* (GASB 63). As such, the Trust's financial statements present statements of net position and statements of changes in net position.

Notes to the Financial Statements

2. Summary of Significant Accounting Policies (continued)

Measurement Focus and Basis of Accounting

The financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized when incurred, regardless of when the related cash flow takes place.

Cash and Cash Equivalents

The Trust reports all cash on hand and deposits in banks as cash and cash equivalents.

Investment Valuation

Investments are reported in accordance with GASB reporting standards as follows:

- Money market funds – at amortized cost
- Commingled funds – at the net asset value (NAV) of units held at the end of the period based upon the fair value of the underlying investments as reported by the external investment manager.
- Other investments – the most recent market price at the close of the markets on June 30, or the most recent market close of each fiscal year, if the markets are closed on June 30. If a market price is not readily determinable, alternative pricing methodologies may be used to determine fair value. Alternative pricing may include methodologies such as matrix-pricing, stale pricing, broker bids, or cost/book value.

Income Recognition

Investment transactions are accounted for on a trade (investment) date basis. Interest and dividend income is recorded on the accrual basis, with dividends accruing on the ex-dividend date.

Administrative Expenses

Pursuant to Section 121.4502, *Florida Statutes*, and in accordance with Internal Revenue Service Revenue Ruling 84-156, reasonable administrative expenses of the Plan may be paid from the Trust. These expenses may include the activities of the Plan administrator, Plan custodian, investment and administrative consulting, and other services rendered for the benefit of Plan members.

Notes to the Financial Statements

2. Summary of Significant Accounting Policies (continued)

Use of Estimates

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect reported amounts of assets and liabilities at the date of the financial statements and reported amounts of revenues (additions) and expenses (deductions) during the reporting period. Actual results could differ from those estimates.

Reclassifications

In the financial statements and notes, certain prior year amounts have been reclassified to conform to the current year presentation and provide more consistent reporting. These reclassifications had no effect on the Trust's net position or changes in net position.

New Accounting Standards

In November 2016, the GASB issued Statement No. 83, *Certain Asset Retirement Obligations (GASB 83)*. This Statement addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance in this Statement. This Statement will enhance comparability of financial statements among governments by establishing uniform criteria for governments to recognize and measure certain AROs, including obligations that may not have been previously reported. The requirements of GASB 83 are effective for reporting periods beginning after June 15, 2018. The statements of net position and the statements of changes in net position are not affected by the adoption of GASB 83, as the Trust does not hold tangible capital assets

In April 2017, the GASB issued Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements (GASB 88)*. The primary objective of this Statement is to improve the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements. It also clarifies which liabilities governments should include when disclosing information related to debt. For purposes of disclosures in notes to financial statements, debt is defined as a liability that arises from a contractual obligation to pay cash (or other assets that may be used in lieu of cash) in one or more payments to settle an amount that is fixed at the date the contractual obligation is established. Direct borrowings and direct placement have terms negotiated directly with the investor or lender and are not offered for public sale. For disclosure purposes, debt does not include leases, except for contracts reported as a financed purchase of the underlying asset, or accounts payable. This Statement amends Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, paragraph 119; Statement No. 38, *Certain Financial Statement Note Disclosures*, paragraphs 10 and 12; Interpretation No. 1, *Demand Bonds Issued by State and Local Governmental Entities*, paragraph 11; NCGA Interpretation 6, *Notes to*

Notes to the Financial Statements

2. Summary of Significant Accounting Policies (continued)

the Financial Statements Disclosure, paragraphs 4 and 5; and Implementation Guide No. 2015-1, Question 7.85.7. The requirements of this Statement are effective for reporting periods beginning after June 15, 2018. The statements of net position and the statements of changes in net position are not affected by the adoption of GASB 88, as the Trust does not enter into direct borrowing or direct placement agreements not offered for public sale.

3. Deposits and Investments

Deposits

The reported carrying amount of deposits totaled \$426 thousand and \$21 thousand at June 30, 2019 and 2018, respectively. All deposits were held in U.S. dollars.

Investments

The Plan has an Investment Policy Statement (IPS) that includes, among other items, the investment objectives of the Plan, manager selection, monitoring guidelines and performance measurement criteria. The IPS is reviewed no less than annually to ensure the structure and guidelines are appropriate, taking into consideration the Plan's goals and objectives.

The primary investment objectives of the Plan are to: (1) offer a diversified mix of low-cost investment options that span the risk-return spectrum and give members the opportunity to accumulate retirement benefits; (2) offer investment options that avoid excessive risk, have a prudent degree of diversification relative to broad market indices, and provide a long-term rate of return, net of all expenses and fees that seek to achieve or exceed the returns on comparable market benchmark indices; and (3) offer members meaningful, independent control over the assets in their account.

The SBA's Executive Director & Chief Investment Officer is responsible for selecting, evaluating, and monitoring performance of the investment options, with a focus on maximizing return within appropriate risk constraints outlined in the Plan's IPS. The Plan offers a number of low-cost institutional investment funds that invest in various short-term, fixed income and equity securities.

The Plan offers eleven customized Retirement Date Funds that consist of mixtures of various asset classes. At the end of fiscal year 2019, 84% of the Plan's members had allocated at least some of their assets to one or more of the available Retirement Date Funds. Approximately 45% of total Trust assets were held in the Retirement Date Funds, which are constructed using the various investment funds offered in the Plan.

The SBA follows the *Florida Statutes'* fiduciary standards of care in managing the Plan's investment options. The SBA Trustees appoint members to serve on the Investment Advisory Council, which makes recommendations on the Trust's investment policy, strategy and procedures.

Notes to the Financial Statements

3. Deposits and Investments (continued)

Self-Directed Brokerage Account

Beginning in January 2014, a Self-Directed Brokerage Account (SDBA) was added as an option available to Plan members. The SDBA allows Plan members to invest in thousands of different investments in addition to the Plan's primary investment funds. It is offered through Alight Financial Solutions (AFS), a subsidiary of Alight Solutions, the Plan Administrator.

The SDBA is for experienced investors who want the flexibility to invest in a variety of options beyond those available in the Plan's primary investment funds. It is not suitable for all members.

The SDBA provides access to the following investment instruments:

- Stocks listed on a Securities Exchange Commission (SEC) regulated national exchange;
- Exchange Traded Funds (except for leveraged Exchange Traded Funds);
- Mutual Funds (except for any of the Plan's primary investment funds); and
- Fixed Income products.

The SDBA accessibility does not include any of the following as investment alternatives:

- Illiquid investments;
- Over the Counter Bulletin Board (OTCBB) securities;
- Pink Sheet® (PS) securities;
- Leveraged Exchange Traded Funds;
- Direct Ownership of Foreign Securities;
- Derivatives, including, but not limited to futures and options contracts on securities, market indexes, and commodities;
- Buying/Trading on Margin;
- Limited Partnership Interests;
- Investment Plan products; or
- Any investment that would jeopardize the investment plan's tax qualified status.

A Plan member may participate in the SDBA if the member:

- Maintains a minimum balance of \$5,000 in the primary investment options offered under the Plan;
- Makes a minimum initial transfer of funds into the SDBA of \$1,000;
- Makes subsequent transfers of funds into the SDBA in amounts of \$1,000 or greater;
- Pays all trading fees, commissions, administrative fees and any other expenses associated with participating in the SDBA; and
- Does not violate any trading restrictions established by the provider, the Investment Plan, or state or federal law.

Notes to the Financial Statements

3. Deposits and Investments (continued)

The SBA is not responsible for managing the SDBA beyond administrative requirements as established between the SBA and AFS. As such, investments available through the SDBA have not been subjected to any selection process, are not monitored by the SBA, require the member's investment expertise to prudently buy, manage and/or dispose of, and have a risk of substantial loss.

Fund Lineup Changes

There were no fund lineup changes during fiscal year 2019. During fiscal year 2018, one institutional commercial real estate separate account was added to the manager allocations in the Retirement Date Funds.

Investment Performance

The SBA staff, consultants and Trustees review the Trust's performance quarterly. The long-term performance of each actively managed investment option is expected to exceed the returns on its performance benchmark, net of all fees and charges, while avoiding large year-to-year deviations from the returns of the performance benchmark. The long-term performance of each passively managed investment option is expected to closely approximate returns of the performance benchmark, net of all fees and charges. At the total Trust level, performance is evaluated by asset class and is measured on an absolute basis and relative to appropriate market benchmarks for each investment option. Performance data is aggregated for the total Trust and for each product type or asset class, using member allocations as the weighting factors. Performance for the SDBA is not included since there is no comparable benchmark. The member assumes the full risk and responsibility for the investments selected in the SDBA and for monitoring the performance of these investments. More detailed information can be obtained by visiting the Florida Retirement System website at MyFRS.com.

Notes to the Financial Statements

3. Deposits and Investments (continued)

The following schedule discloses the Trust's investments, by type, at June 30, 2019 and 2018.

Investment Type ¹	As of June 30	
	2019	2018
	<i>(In Thousands)</i>	
Fixed income		
Money market funds	\$ 974,262	\$ 903,511
Domestic	318,051	297,356
International	12,621	15,734
Domestic commingled funds	1,705,399	1,617,871
Total fixed income	3,010,333	2,834,472
Equity		
Domestic	572,941	575,542
International	20,601	21,873
Domestic commingled/mutual funds	4,005,603	3,871,793
International commingled/mutual funds	2,176,526	2,184,933
Total equity	6,775,671	6,654,141
Commingled real asset funds	787,711	740,128
Self-Directed Brokerage Account	700,874	633,004
Total investments	\$ 11,274,589	\$ 10,861,745

¹ Retirement Date Funds consist of Trust investments, shown in this table, in various proportions.

Notes to the Financial Statements

3. Deposits and Investments (continued)

Fair Value Hierarchy

The Trust's investments are measured and reported at fair value and classified according to the following hierarchy:

Level 1 - Investments reflect unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2 - Investments reflect prices based on significant observable inputs (including, but not limited to, quoted prices for similar investments, interest rates, foreign exchange rates, volatility and credit spreads), either directly or indirectly. These inputs may be derived principally from, or corroborated by, observable market data through correlation or by other means.

Level 3 - Investments reflect prices based upon unobservable inputs, including situations where there is little market activity, if any, for assets or liabilities.

The categorization of investments within the hierarchy is based upon the pricing transparency of the instrument and should not be perceived as the particular investment's risk.

Fixed income and equity securities classified in Level 1 of the fair value hierarchy are valued using quoted prices at June 30 (or the most recent market close date if the markets are closed on June 30) in active markets from the custodian bank's primary external pricing vendors, which utilize primary exchanges.

Fixed income securities classified as Level 2 are valued using evaluated prices from the custodian bank's external pricing vendors. The pricing methodology involves the use of evaluation models such as matrix pricing, which is based on the securities' relationship to benchmark quoted prices. Other evaluation models use actual trade data, collateral attributes, broker bids, new issue pricings and other observable market information.

Fixed income securities classified as Level 3 are valued using prices from the custodian bank's external pricing vendors or an alternative pricing source, utilizing inputs such as stale prices, cash flow models, or broker bids.

The SDBA is classified as level 2, since the individual, underlying assets are priced by observable inputs. The SDBA Administrator uses an external pricing source to value the underlying investments and aggregates the overall investment values into a total account fair value for reporting purposes.

Certain investments, such as money market funds, are carried at cost, and not priced at fair value. Mutual funds are valued at the quoted price traded on the exchanges. Commingled investments are measured at the net asset value (NAV) per share (or its equivalent) as provided by the investment manager.

Notes to the Financial Statements

3. Deposits and Investments (continued)

The Trust has the following fair value measurements as of June 30, 2019 and June 30, 2018.

		As of June 30, 2019		
		Fair Value Measurements Using		
Investments by Fair Value Level	Total	(Level 1)	(Level 2)	(Level 3)
		(In Thousands)		
Mutual funds and Self-Directed Brokerage Account				
Domestic equity mutual funds	\$ 548,520	\$ 548,520	\$ -	\$ -
International equity mutual funds	446,403	446,403	-	-
Self-Directed Brokerage Account	700,874	-	700,874	-
Total mutual funds and Self-Directed Brokerage Account	1,695,797	994,923	700,874	-
Fixed income				
U.S. government guaranteed obligations	115,778	-	115,564	214
Federal agencies	88,850	-	87,956	894
Domestic bonds and notes	113,423	-	113,247	176
International bonds and notes	12,621	-	12,621	-
Total fixed income	330,672	-	329,388	1,284
Equity				
Domestic	572,941	572,941	-	-
International	20,601	20,601	-	-
Total equity	593,542	593,542	-	-
Total investments by fair value level	\$ 2,620,011	\$ 1,588,465	\$ 1,030,262	\$ 1,284
		Redemption Frequency (If Currently Eligible)	Redemption Notice Period	
Investments measured at the net asset value (NAV)				
Commingled fixed income funds ¹	\$ 1,705,399	Daily	2 - 15 Days	
Commingled domestic equity funds ²	3,457,083	Daily	2 - 5 Days	
Commingled international equity funds ³	1,730,123	Daily	2 Days	
Commingled real asset funds ⁴	787,711	Daily	1 - 15 Days	
Total investments measured at the NAV	7,680,316			
Other investments carried at amortized cost				
Money market funds	974,262			
Total investments	\$ 11,274,589			

¹ *Commingled Fixed Income Funds:* One TIPS fund and five fixed income funds are considered to be commingled in nature. The TIPS fund seeks long-term real total return and is designed to keep pace with inflation. The five commingled fixed income funds utilize various investment strategies such as short/intermediate duration, index/benchmark tracking, high-yield, and corporate/government investment grade debt. Each fund is valued at the net asset value of units held at the end of the period based upon the fair value of the underlying investments.

² *Commingled Domestic Equity Funds:* Six domestic equity funds are considered to be commingled in nature. These commingled domestic equity funds utilize various investment strategies such as index/benchmark tracking, small/mid cap, and large cap growth/value seeking appreciation and income. Each fund is valued at the net asset value of units held at the end of the period based upon the fair value of the underlying investments.

³ *Commingled International Equity Funds:* One international equity fund is considered to be commingled in nature. This fund invests in a portfolio of international equity securities whose total rates of return will approximate as closely practicable the capitalization weighted total rates of return of the markets in certain countries for equity securities traded outside the United States. The fund is valued at the net asset value of units held at the end of the period based upon the fair value of the underlying investments.

⁴ *Commingled Real Asset Funds:* These two funds consist of various investments such as real estate, commodities, floating rate loans, energy industry Master Limited Partnerships, global infrastructure, and agriculture. The funds are valued at the net asset value of units held at the end of the period based upon the fair value of the underlying investments.

Notes to the Financial Statements

3. Deposits and Investments (continued)

		As of June 30, 2018		
		Fair Value Measurements Using		
Investments by Fair Value Level	Total	(Level 1)	(Level 2)	(Level 3)
		(In Thousands)		
Mutual funds and Self-Directed Brokerage Account				
Domestic equity mutual funds	\$ 545,704	\$ 545,704	\$ -	\$ -
International equity mutual funds	492,076	492,076	-	-
Self-Directed Brokerage Account	633,004	-	633,004	-
Total mutual funds and Self-Directed Brokerage Account	1,670,784	1,037,780	633,004	-
Fixed income				
U.S. government guaranteed obligations	115,261	-	115,261	-
Federal agencies	71,278	-	71,278	-
Domestic bonds and notes	110,817	-	110,661	156
International bonds and notes	15,734	-	15,734	-
Total fixed income	313,090	-	312,934	156
Equity				
Domestic	575,542	575,542	-	-
International	21,873	21,873	-	-
Total equity	597,415	597,415	-	-
Total investments by fair value level	\$ 2,581,289	\$ 1,635,195	\$ 945,938	\$ 156
		Redemption Frequency (If Currently Eligible)	Redemption Notice Period	
Investments measured at the net asset value (NAV)				
Commingled fixed income funds ¹	\$ 1,617,871	Daily	2 - 15 Days	
Commingled domestic equity funds ²	3,326,089	Daily	2 - 5 Days	
Commingled international equity funds ³	1,692,857	Daily	2 Days	
Commingled real asset funds ⁴	740,128	Daily	1 - 15 Days	
Total investments measured at the NAV	7,376,945			
Other investments carried at amortized cost				
Money market funds	903,511			
Total investments	\$ 10,861,745			

¹ *Commingled Fixed Income Funds:* One TIPS fund and five fixed income funds are considered to be commingled in nature. The TIPS fund seeks long-term real total return and is designed to keep pace with inflation. The five commingled fixed income funds utilize various investment strategies such as short/intermediate duration, index/benchmark tracking, high-yield, and corporate/government investment grade debt. Each fund is valued at the net asset value of units held at the end of the period based upon the fair value of the underlying investments.

² *Commingled Domestic Equity Funds:* Six domestic equity funds are considered to be commingled in nature. These commingled domestic equity funds utilize various investment strategies such as index/benchmark tracking, small/mid cap, and large cap growth/value seeking appreciation and income. Each fund is valued at the net asset value of units held at the end of the period based upon the fair value of the underlying investments.

³ *Commingled International Equity Funds:* One international equity fund is considered to be commingled in nature. This fund invests in a portfolio of international equity securities whose total rates of return will approximate as closely practicable the capitalization weighted total rates of return of the markets in certain countries for equity securities traded outside the United States. The fund is valued at the net asset value of units held at the end of the period based upon the fair value of the underlying investments.

⁴ *Commingled Real Asset Funds:* These two funds consist of various investments such as real estate, commodities, floating rate loans, energy industry Master Limited Partnerships, global infrastructure, and agriculture. The funds are valued at the net asset value of units held at the end of the period based upon the fair value of the underlying investments.

Notes to the Financial Statements

3. Deposits and Investments (continued)

Deposit and Investment Risk

The Trust has deposits and a broad range of financial investments exposed to various risks, including overall market volatility. Due to the level of risk associated with certain financial investments, it is reasonably possible that changes in the values of financial investments will occur in the near term and that such changes could materially affect the amounts reported in the financial statements.

The Plan's IPS provides a statement of objectives for the Plan, general guidelines for each asset class and the Retirement Date Funds, as well as educational services to help members manage the level of risk associated with the choices they make with their individual investment accounts.

Investments available through the Plan's SDBA are not selected or monitored by the SBA. The SDBA investments are subject to Alight Financial Solutions' Self-Directed Brokerage Account guidelines and the risks inherent in the types of investments selected by participating Plan members.

GASB Statement No. 40, *Deposit and Investment Risk Disclosures*, requires that certain risks be discussed in the financial statements. These risks include credit risk, custodial credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. Each of these risks is managed by the Trust's investment advisors, subject to guidelines set forth in prospectuses, Statements of Additional Information and other governing documents.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Credit quality ratings are used as an assessment of creditworthiness and are assigned by Nationally Recognized Statistical Rating Organizations (NRSROs). These ratings are disclosed in aggregate by investment type for the securities held as of the financial statement date.

The mutual funds and commingled trust funds in the Trust are institutional funds and, as such, are not rated by the NSRSOs.

Notes to the Financial Statements

3. Deposits and Investments (continued)

The following tables disclose credit quality ratings related to credit risk on investments held in the Trust at June 30, 2019 and 2018.

Credit Quality Ratings		As of June 30, 2019					
		Total	Money Market Funds	Federal Agencies ¹	Domestic Bonds and Notes	Commingled Fixed Income	International Bonds and Notes
S&P ¹	Moody's ¹	(In Thousands)					
AAA		\$ 17,892	\$ -	\$ -	\$ 17,892	\$ -	\$ -
AA		13,558	-	-	13,319	-	239
A		23,143	-	-	19,429	-	3,714
BBB		38,744	-	-	31,293	-	7,451
BB		749	-	-	468	-	281
B		1,712	-	-	1,712	-	-
	Aaa	17,629	-	-	17,629	-	-
	Aa	72	-	-	72	-	-
	A	2,218	-	-	1,690	-	528
	Baa	7,697	-	-	7,697	-	-
	Ba	2,318	-	-	1,910	-	408
NR	NR	2,768,823	974,262	88,850	312	1,705,399	-
		<u>\$ 2,894,555</u>	<u>\$ 974,262</u>	<u>\$ 88,850</u>	<u>\$ 113,423</u>	<u>\$ 1,705,399</u>	<u>\$ 12,621</u>

Ratings not applicable:

U.S. guaranteed obligations² \$ 115,778

Total fixed income investments \$ 3,010,333

¹ S&P ratings were primarily used. If S&P did not provide a rating or did not provide the rating with the greatest degree of risk, then Moody's ratings were used. If neither rating agency issued a rating, the security was listed as "NR" (not rated). Long-term ratings are presented.

² U.S. guaranteed obligations do not require disclosure of credit quality.

³ Federal Agency TBAs and mortgage-backed securities are classified as "NR" because they do not have explicit credit ratings on individual securities.

Notes to the Financial Statements

3. Deposits and Investments (continued)

		As of June 30, 2018					
Credit Quality Ratings		Total	Money Market Funds	Federal Agencies ³	Domestic Bonds and Notes	Commingled Fixed Income	International Bonds and Notes
S&P ¹	Moody's ¹						
(In Thousands)							
AAA		\$ 18,942	\$ -	\$ -	\$ 18,942	\$ -	\$ -
AA		78,089	-	64,413	12,966	-	710
A		17,277	-	-	13,083	-	4,194
BBB		35,659	-	-	30,095	-	5,564
BB		1,438	-	-	1,223	-	215
	Aaa	24,092	-	-	24,092	-	-
	Aa	642	-	-	642	-	-
	A	2,357	-	-	584	-	1,773
	Baa	8,504	-	-	5,956	-	2,548
	Ba	3,553	-	-	2,954	-	599
NR	NR	2,528,658	903,511	6,865	280	1,617,871	131
		\$ 2,719,211	\$ 903,511	\$ 71,278	\$ 110,817	\$ 1,617,871	\$ 15,734

Ratings not applicable:

U.S. guaranteed obligations² \$ 115,261

Total fixed income investments \$ 2,834,472

¹ S&P ratings were primarily used. If S&P did not provide a rating or did not provide the rating with the greatest degree of risk, then Moody's ratings were used. If neither rating agency issued a rating, the security was listed as "NR" (not rated). Long-term ratings are presented.

² U.S. guaranteed obligations do not require disclosure of credit quality.

³ Federal Agency TBAs and mortgage-backed securities are classified as "NR" because they do not have explicit credit ratings on individual securities.

Notes to the Financial Statements

3. Deposits and Investments (continued)

Custodial Credit Risk

Custodial credit risk is the risk that if a depository institution or counterparty fails, the Trust will not be able to recover the value of its deposits, investments or collateral securities in the possession of an outside party.

As stated in SBA's custodial credit policy, the SBA seeks to minimize custodial credit risk through the use of trust accounts maintained at top tier third-party custodian banks, whose creditworthiness is monitored by the SBA. To the extent possible, the SBA's negotiated custody contract requires that deposits and investments be held in accounts in the SBA's name, separate and apart from the assets of the custodian bank. In addition, un-invested cash for all portfolios/funds under SBA management is generally swept nightly into overnight investments, thereby reducing the Trust's exposure to custodial credit risk. On occasion, however, the Trust's cash balances can exceed federally-insured limits.

U.S. dollar deposits held at SBA's custodian bank are covered by the Federal Deposit Insurance Corporation (FDIC) up to the maximum available limits. Cash deposits totaling \$426 thousand were held at June 30, 2019, of which no more than \$250 thousand was insured by the FDIC. The remaining uninsured and uncollateralized deposits totaled \$176 thousand. There were no uninsured or uncollateralized deposits at June 30, 2018.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The Trust did not hold any investments with a single issuer representing 5% or more of the Trust's fair value at June 30, 2019 or 2018.

Notes to the Financial Statements

3. Deposits and Investments (continued)

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of fixed income instruments.

The Plan's IPS provides that the money market funds will offer high-quality, liquid, short-term instruments to control interest rate sensitivity. The other fixed income funds may be passively or actively managed. In both cases, the funds' sensitivity to interest rate changes generally will closely approximate that of the performance benchmark.

The interest rate risk tables for the Trust as of June 30, 2019 and 2018, are presented below. Investment types, related to fixed come portfolios, are presented using effective weighted duration.

Investment Type	As of June 30, 2019	
	Total	Effective Weighted Duration
	<i>(In Thousands)</i>	<i>(In Years)</i>
Money market funds	\$ 974,262	0.08
Fixed income funds/trusts	1,705,399	5.33
U.S. guaranteed obligations:		
Treasury bonds and notes	89,179	7.28
Bonds and notes	657	4.76
GNMA mortgage-backed	22,089	1.22
GNMA commitments to purchase (TBAs)	2,070	2.35
Mortgage-backed CMOs and CMBS	1,783	4.44
Federal agencies:		
Mortgage-backed	50,448	1.41
FNMA, FHLMC commitments to purchase (TBAs)	18,650	1.69
Mortgage-backed CMOs and CMBS	19,752	2.51
Domestic:		
Corporate bonds and notes	64,204	8.33
Asset and mortgage-backed	35,103	1.66
Mortgage-backed CMOs and CMBS	12,436	4.07
Municipal/provincial	1,680	15.99
International:		
Corporate bonds and notes	10,604	6.47
Government and agency obligations	2,017	10.82
Total fixed income investments	\$ 3,010,333	

Notes to the Financial Statements

3. Deposits and Investments (continued)

<u>Investment Type</u>	As of June 30, 2018	
	Total	Effective Weighted Duration
	<i>(In Thousands)</i>	<i>(In Years)</i>
Money market funds	\$ 903,511	0.08
Fixed income funds/trusts	1,617,871	5.75
U.S. guaranteed obligations:		
Treasury bonds and notes	85,572	7.11
Bonds and notes	547	3.66
GNMA mortgage-backed	17,589	3.61
GNMA commitments to purchase (TBAs)	11,446	3.34
Mortgage-backed CMOs and CMBS	107	5.49
Federal agencies:		
Unsecured bonds and notes	663	1.26
Mortgage-backed	41,297	4.30
FNMA, FHLMC commitments to purchase (TBAs)	6,865	3.78
Mortgage-backed CMOs and CMBS	22,453	4.91
Domestic:		
Corporate bonds and notes	53,364	7.98
Asset and mortgage-backed	43,796	1.32
Mortgage backed CMOs and CMBS	12,051	4.86
Municipal/provincial	1,606	15.79
International:		
Corporate bonds and notes	12,161	7.29
Government and agency obligations	3,573	7.79
Total fixed income investments	\$ 2,834,472	

Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The Trust's actively managed fixed income and equity portfolios are prohibited from holding any non-U.S. dollar denominated securities.

Although the Trust's commingled funds are denominated in U.S. dollars, the international equity and real asset funds may have underlying investments exposed to foreign currency risk in various currencies. The fair value of the commingled international equity funds was \$2.18 billion for both fiscal years 2019 and 2018. For fiscal years 2019 and 2018, the commingled real asset funds' fair values were \$788 million and \$740 million, respectively.

Notes to the Financial Statements

4. Contingencies and Litigation

In the ordinary course of its operations, the SBA, on behalf of the Trust, may be party to various claims, legal actions, and class action lawsuits. The SBA's General Counsel Office handles these matters either directly or with assistance of outside legal counsel. In the opinion of the SBA's management and legal counsel, these matters are not anticipated to have a material financial impact on the Trust.

5. Related-Party Transactions

The Trust considers the State of Florida and its Department of Management Services (DMS), Division of Retirement, and the Florida Retirement System Trust Fund (FRS Trust Fund) to be related parties for the purpose of the financial statements.

The DMS is responsible for the receipt of member demographic data and for collecting employer and employee contributions and remitting those contributions to the SBA for deposit into the Trust for the benefit of the Plan members. In addition, the DMS provides administrative services to the Trust and charges an administrative fee based on membership in the investment plan each quarter-end. The FRS Trust Fund is the source of funding for a member's accumulated benefit obligation (ABO) when a member in the FRS Pension Plan elects to join the FRS Investment Plan. The FRS Trust Fund is also a recipient of certain benefits returned to the Trust.

The table below discloses significant transactions between the Trust, the DMS, and the FRS Trust Fund.

	Fiscal Years Ended	
	2019	2018
	<i>(In Thousands)</i>	
Receivables:		
Due from DMS	\$ 47,078	\$ 41,934
Payables:		
Due to DMS	\$ 34	\$ 14
Additions:		
Employer/employee contributions received from DMS	486,942	433,372
Member-directed benefits received from the FRS Trust Fund	565,045	597,010
Total additions	<u>\$ 1,051,987</u>	<u>\$ 1,030,382</u>
Deductions:		
Member-directed benefits sent to the FRS Trust Fund	83,627	70,597
Administrative fees to DMS	125	84
Total deductions	<u>\$ 83,752</u>	<u>\$ 70,681</u>

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

The Board of Trustees
State Board of Administration of Florida

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the Florida Retirement System Investment Plan Trust Fund (the "Trust") administered by the State Board of Administration ("SBA") of Florida, as of and for the year ended June 30, 2019, and the related notes to the financial statements, and have issued our report thereon dated November 5, 2019. As discussed in Note 1, the financial statements present only the Trust and do not purport to, and do not, present fairly the financial position of the State of Florida, the SBA of Florida or the Florida Retirement System, their changes in financial position, or, where applicable, their cash flows, in conformity with accounting principles generally accepted in the United States of America.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Trust's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control. Accordingly, we do not express an opinion on the effectiveness of the Trust's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Trust's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

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

A handwritten signature in black ink that reads "Crowe LLP". The signature is stylized, with the "C" being large and looping, and the "LLP" being written in a more straightforward, blocky style.

Crowe LLP

Tampa, Florida
November 5, 2019