

RETIRED Educator

WINTER 2008

CALIFORNIA STATE TEACHERS' RETIREMENT SYSTEM



Retired Educators Win Big in SBMA Ruling

California's longest-retired educators depend on quarterly inflation protection payments that are largely funded by the Supplemental Benefit Maintenance Account. Retirees and their survivors receive the payments when inflation erodes their monthly benefit to below 80 percent of its original consumer purchasing power. In 2006-07, CalSTRS paid \$230.3 million in supplemental benefits to nearly 55,000 recipients, including educators who retired in 1988 or earlier and survivors.

State fiscal crisis led to funding cut

The Supplemental Benefit Maintenance Account is funded primarily by annual contributions from the state General Fund. Cost-cutters targeted the contribution to that account during the state's fiscal crisis in the early part of the decade. In 2003, Governor Gray Davis signed Senate Bill 20, which withheld \$500 million of the \$558.9 million due for fiscal year 2003-04.

CalSTRS promptly filed suit to recover the funds for its retired members, claiming the state had a contractual obligation to pay the full amount. In May 2005, the Sacramento County Superior Court agreed and ordered the state to pay the past-due amount, plus interest. The state, in turn, appealed the decision.

Court of Appeal requires state to pay in full

On August 20, 2007, Sacramento's Third District Court of Appeal upheld the trial court ruling in a major victory for the state's retired educators. In addition to ordering the state to pay the \$500 million due plus interest, the appellate court increased the prejudgment simple interest rate from 7 percent to 10 percent. CalSTRS estimates that accrued interest could exceed \$200 million.

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CALSTRS
HOW WILL YOU SPEND YOUR FUTURE?

SEMIANNUAL NEWSLETTER FOR CALSTRS BENEFIT RECIPIENTS

Uncertain Health Coverage Spells an Uncertain Retirement



By Dana Dillon
Teachers' Retirement Board Chair

Over the course of more than two decades as an educator, activist, and

board member, I have seen the state of teachers' health care benefits erode. The issue has become especially worrisome for our retired members as fewer and fewer districts provide post-retirement health benefits.

Although CalSTRS' core business is to pay retirement benefits every month, our mission is much broader. It's not only our duty, but our desire to create a secure tomorrow for all educators. After all, most of you retire at age 61 or older after devoting at least 26 years to teaching. Once there, you deserve a little peace of mind.

That peace can be hard to find if you don't receive health care assistance from your employer. A 2006 CalSTRS survey of school districts revealed that 62 percent of our retired members age 65 and older fall into that category. It's a continuing trend—and it's getting worse.

While survey data and poll results provide us with numbers that help us understand this situation, you and your retired colleagues must actually cope with it day to day. That's why finding solutions is among the board's top priorities. And we've already taken action.

Throughout 2007, CalSTRS participated in the Governor's Public Employee Post-Employment Commission hearings (see story on page 8). We provided commission members with testimony and information about your pension system, with a focus on your health care issues.

At the July 2007 commission meeting, Board Vice-Chair Jerilyn Harris shared real stories of two retired members who struggle every day to pay for health care. One spent 35 years in the classroom and receives a \$2,500 monthly benefit. She picked up the cost of her health premium when she turned 65 because the insurance helps pay for prescription drugs she needs for a chronic pain condition and diabetes. Another retired in 2000, but continues to work full time as an online professor and insurance company sales representative to pay for his family's medical insurance and medical bills.

The board also convened a Public Education Health Benefit Task Force in 2006 to discuss this issue in more depth and make recommendations that will benefit school districts, school employees and their retired workers.

In addition, last summer the board voted to extend for five years the payment of Medicare Part A premiums (hospital) for eligible Defined Benefit Program members. We also continue to cooperate

CalSTRS Mission:

Securing the financial future and sustaining the trust of California's educators

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Katherine K. Evatt
Editor

Statements in this publication are general and the Teachers' Retirement Law is complex and specific. If a conflict arises between information contained in this publication and the law, any decisions will be based on the law.

CalSTRS Retired Educator is published twice a year for retired members and benefit recipients of the California State Teachers' Retirement System. Send your comments or suggestions to:

Editor, Communications,
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P.O. Box 15275
Sacramento, CA 95851



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with the state Legislature in studying the possibility of an employer health benefit pool. It's critical for decision-makers to understand your health care realities.

Though CalSTRS doesn't provide health care for active or retired members, we must continue to show active leadership as we work to find solutions to this growing problem.



Legislation Affects Retirees

Consistent with our mission, CalSTRS advocates in the legislative arena to ensure continued security for the state's retired educators. Measures enacted in 2007 that affect retirees and bills pending for 2008 are described in brief on this page. Positions taken by the Teachers' Retirement Board are in italics at the end of each bill summary.

More Information

For the latest text of specific bills and bill analyses, visit www.CalSTRS.com/Legislation.

Bills signed by the Governor, which took effect January 1

Assembly Bill 1432 (Soto)	Confirms the Teachers' Retirement Law to federal law by allowing domestic partners of CalSTRS members and participants to roll certain benefit distributions over into qualified pension plans. Sponsor.
Assembly Joint Resolution 5 (Hernandez)	Requests that the President and the Congress enact the Social Security Fairness Act, which would repeal the Government Pension Offset and the Windfall Elimination Provision from the Social Security Act. Support.
Senate Bill 901 (Padilla)	Extends the current post-retirement earnings limit exemptions until June 30, 2009, and then repeals them on January 1, 2010. Sponsor.

Bills pending before the Legislature

Assembly Bill 36 (Niello)	Criminalizes making false material statements or representations in applying for CalSTRS benefits or knowingly accepting benefit payments to which one is not entitled. Support.
Senate Bill 11 (Migden)	Revises the criteria that apply to opposite-sex couples who wish to establish a registered domestic partnership by removing the requirement that at least one of the partners be at least age 62 and allowing partners age 18 and older to register. Support if amended.
Senate Bill 369 (Vincent)	Requires the Teachers' Retirement Board to file with the Legislature a one-year study of school districts that do not provide health benefits for retired teachers. Pending.
Senate Bill 879 (Calderon)	Allows retirees who serve as substitute teachers for their former employing district within five years of retirement to retain, rather than forfeit, their two-year service credit retirement incentive. Watch.

Portfolio Value Doubles in Five Years 21 Percent Return in 2007

Seventy-five cents of every CalSTRS benefit dollar comes from investment earnings. So when our investment portfolio has a strong year, that's good news for the Teachers' Retirement Fund. Investment earnings this last fiscal year were not only good—they were among the best in the nation.

"By any measure, 2006-07 will go down as one of our most spectacular years," said CalSTRS Chief Investment officer Christopher J. Ailman. "We played it smart when the opportunities arose and

it demonstrates a consistent flow of great investment decisions over the last five years. The CalSTRS board deserves credit for giving us the tools to attract and retain quality staff and set the right benchmarks and structure to succeed."

Thanks to smart management and favorable markets, the portfolio gained an amazing \$26 billion in value in fiscal year 2006-07, a one-year investment return of 21 percent. At year end, the fund was valued at \$170.4 billion.

These earnings put us in the top one percent of funds in our class, according to the Wilshire Trust Universe Comparison Service, and in the top five percent as measured by the State Street Universe of funds greater than \$10 billion.

Not only were last year's earnings stellar, they followed three straight years of double-digit investment returns. Over the last three years, the fund has earned an average of 14.9 percent per year. The total dollar value of CalSTRS investments has doubled since the U.S. stock market drop in October 2002.

CalSTRS on the Sidelines of the Sub-Prime Mortgage Crisis

As we celebrated one of our most profitable years (July 1, 2006—June 30, 2007), the market began a series of sharp ups and downs. On July 19, 2007, we hit an all-time high of \$175 billion, followed by a decline to \$169 billion by the end of August, 2007. But by the end of September, the fund had bounced back to a new high of \$176.9 billion.

The financial market decline was fueled by the sub-prime mortgage crisis. Thanks to the careful policies guiding our portfolio management, our exposure to this investment vehicle is extremely low—less than $\frac{1}{10}$ of one percent of the total portfolio. Therefore, we avoided chasing yields and buying many of the unrated risky securities. Our strength comes from being well diversified across several different investment categories and by not overreaching for a high return beyond a prudent level of risk.

CalSTRS investment professionals believe the ups and downs in the marketplace aren't over yet, and we expect further weakness in the mortgage market and residential real estate market. However, you can rest assured that our portfolio is built on a solid foundation capable of weathering this latest financial storm.



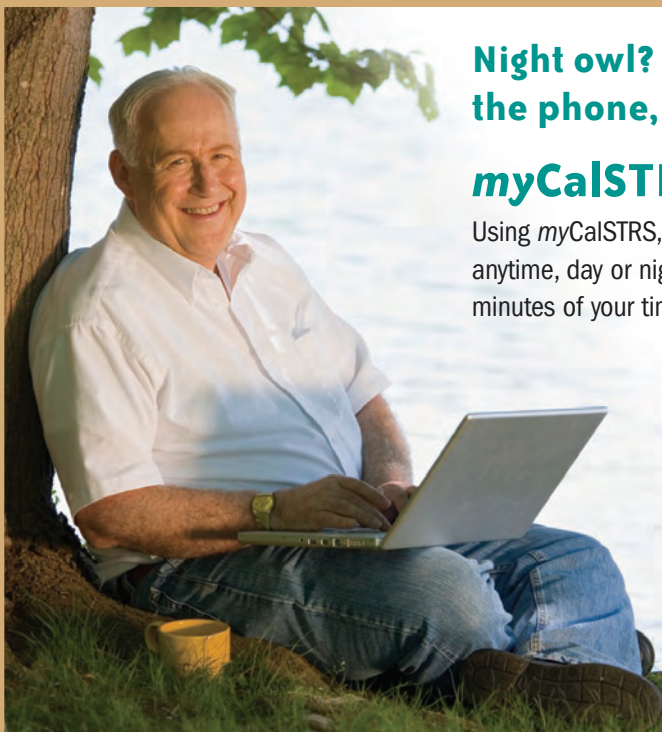
In addition, our 10-year average annual return is 9 percent, greater than the 8 percent average necessary to help meet projected long-term benefit liabilities.

Not long after our 2006-07 earnings were announced, the market created some ups and downs in our portfolio (see previous page). And despite excellent money management, the pension system still has a projected long-term funding shortfall. For more information on how the CalSTRS board is working to address this issue, see “CalSTRS Funding Gap Narrows” on page 7.

New Process Will Reduce CalSTRS Costs

Effective April 1, 2008, we will begin to handle small retroactive benefit adjustments differently than we have in the past. CalSTRS will no longer pay or collect adjustment amounts at or under \$10. If future adjustments to your account total more than \$10, we will then collect or pay you the full adjustment amount. This change will improve our cost effectiveness and efficiency by reducing the need to pay or collect very small amounts of money.

myCalSTRS: Your Information, When You Need It



Night owl? Busy during the week? Hate to talk on the phone, but still need your CalSTRS information?

myCalSTRS is the answer!

Using myCalSTRS, you can obtain specific information about your CalSTRS account anytime, day or night. All it takes is a computer with Internet access and a few minutes of your time.

A simple click of the mouse allows you to:

- View your 1099-R and other benefit payment information
- Update your mailing address and telephone number (with Level II access)
- Review your tax withholding and beneficiary choices
- Ask questions about your account and receive prompt, confidential answers

To register, go to www.CalSTRS.com and follow the step-by-step directions. If you're already registered, you can log in right away.

TRB Approves Campaign Contribution Limits

“This sends a strong message to our business partners and membership that protecting the system’s integrity is paramount.”
– CalSTRS CEO
Jack Ehnes

The Teachers’ Retirement Board has fiduciary responsibility for the considerable assets of the Teachers’ Retirement Fund—the second-largest public pension fund in the country. In that role, the board sets investment policy and makes other decisions related to the fund’s investments.

At its meeting September 6, 2007, the board approved regulations restricting campaign contributions to board members and the Governor. The restrictions apply to individuals and businesses who are seeking an investment relationship with CalSTRS. They are the first of their kind for California public pension plans.

“We’re proud of the work we’ve done as a board toward eliminating ‘pay to play’ opportunities,” said Board Chair Dana

Dillon. “We currently operate at the highest ethical level. Moving forward with these regulations underscores our commitment to conflict-free investment decisions.”

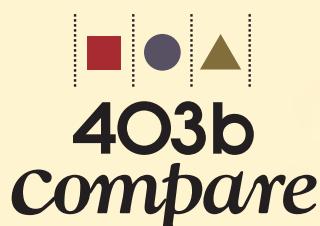
The regulations:

- Restrict campaign contributions to board members and the Governor in a 12-month period to no more than \$1,000 per donation or \$5,000 total.
- Require board members to recuse themselves from decisions involving any of their donors who make a campaign contribution greater than the contribution limits.
- Disqualify a party who violates the regulations from engaging in future or additional business with CalSTRS for two years.

“As pension fiduciaries and strong advocates of good governance practices, we felt these regulations were an important step,” said Jack Ehnes, CalSTRS chief executive officer. “It sends a strong message to our business partners and membership that protecting the system’s integrity is paramount.”

The board action was part of a rule-making process that began in December 2006 when the board approved proposed regulatory language. That action was followed by public hearings and review of written comments from the public, including members of the business and investment communities.

The regulations were approved by the Office of Administrative Law and filed with the Secretary of State on October 29, 2007. They went into effect on November 28, 2007.


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CalSTRS Funding Gap Narrows

There's good news about the CalSTRS funding gap. It's narrowing, thanks in part to unprecedented investment returns in 2006-07 (see story on page 4). We are currently funded at 87 percent as of June 30, 2006.

The gap, or unfunded actuarial obligation, is the amount we will need in the future to pay benefits due to current members for service already performed. The shortfall numbers are derived from an actuarial valuation, a snapshot of the fund's assets and liabilities as of June 30, 2006.

Regardless of the funding gap, current members' benefits are guaranteed.

Must CalSTRS be funded at 100 percent? It's certainly our goal. But a valuation is somewhat like a home mortgage: There isn't a need to have all the money today, but we should have a plan in place to handle the debt.

There are two major reasons for the improved financial status of the Defined Benefit Program: the fund had an excellent investment return in the last fiscal year, earning \$2.1 billion more than expected, and overall, statewide teacher salaries did not increase as much as anticipated.

Despite these improvements, the DB Program's funding gap can't be paid off with the current contributions to the program, and it's unlikely to be eliminated by investment returns. The Teachers' Retirement Board has adopted a strategy to address the unfunded actuarial

Defined Benefit Program	June 30, 2006	June 30, 2005
Projected shortfall	\$19.6 billion	\$20.3 billion
Funding level	87 percent	86 percent
Percent of annual teacher payroll needed to reduce obligation to zero in 30 years	4.168 percent	4.491 percent

obligation and is in the process of educating the Legislature and stakeholders.

We'll keep you posted on progress toward closing the funding gap in future newsletters, on CalSTRS.com—and for those of you who have chosen to receive them, with periodic e-news updates. If you'd like to sign on to receive CalSTRS e-news, see the preference settings on your myCalSTRS account (see related story on page 9). You may unsubscribe at any time.

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Talk to a CalSTRS customer service
representative at 800-228-5453

Governor's Commission to Submit Final Report

The Governor... stated that promised pension and retiree health benefits "are obligations that must—and will—be paid by government."

As we go to press, we're awaiting the final report from Governor Arnold Schwarzenegger's Public Employee Post-Employment Benefits Commission. The commission should issue its report before you receive this newsletter.

Regardless of the commission's recommendations, we'd like to assure you that your pension benefits are safe. Your basic defined benefit pension is a contractual obligation guaranteed by law. The Governor acknowledged this when he established the commission in December 2006, stating that promised pension and retiree health benefits "are obligations that must—and will—be paid by government."

The commission was charged with proposing ways to address pension and

retiree health care obligations to ensure that local governments and the state can provide guaranteed benefits to retired public servants. Over the past year, the 12-member panel met monthly to hear public testimony and expert opinion on everything from accounting standards to abusive pension practices.

Last July, a CalSTRS team testified at the commission meeting in La Jolla. Teachers' Retirement Board Vice-Chair Jerilyn Harris, CEO Jack Ehnes, Deputy CEO Ed Derman and CalSTRS Consulting Actuary Mark Johnson presented information about the CalSTRS benefit structure, investments and members. Harris, a CalSTRS retiree, gave moving testimony about retired educators burdened by high



health care costs (see article page 2).

The Governor and commission have made it clear that retiree health care currently provided by local governments, including school districts, is a guaranteed obligation and will be met. Nevertheless, health care was thrust to the forefront of the discussion by a new accounting rule that requires governments to disclose retiree health care liabilities. The disclosure has highlighted the unfunded status of retiree health care programs across the state. Unlike pensions, which are funded as they are earned, most governments that provide retiree health benefits pay for those benefits as they are provided.

The final report is expected to:

- Identify the full amount of California governments' retiree health care liabilities
- Evaluate and compare various approaches for addressing governments' unfunded retiree health care and pension obligations
- Propose a plan to address those unfunded obligations

For more information about the commission and its report, please visit the Public Employee Post-Employment Benefits Commission Web site at www.pebc.ca.gov.



Save Time and Get Results with *myCalSTRS*

Want to view information about your account, update your CalSTRS contact information, and ask benefit questions anytime day or night? *myCalSTRS*, our secure online member Web site, is here for you.

With basic, Level 1 access to *myCalSTRS*, you can:

- Send us secure online messages with questions about your account and receive secure online replies
- View your Form 1099-R documents
- See your benefit payment stubs and beneficiary information

Already have Level 1 access? Consider moving up to Level 2. With Level 2, a quick click of the mouse allows you to update your personal information, including your phone number, e-mail address and mailing addresses.

Here's how:

- Make sure we have your current mailing address
- Go to the CalSTRS Web site, www.CalSTRS.com
- Log on to *myCalSTRS*
- See the Settings menu
- Click on Level 2 access
- Follow the simple directions on the page

And you're done.

We'll send a letter to your current address of record within a few weeks containing your Personal Identification Number. Once you have your PIN, you can update your personal information at your convenience. No forms, no stamps, no waiting.

With either level of access, you can also choose to receive this newsletter and other CalSTRS news by e-mail instead of through the U.S. Postal Service. It's a green choice that saves paper—and it reduces CalSTRS postage and printing costs, too.

We'll be adding new features to *myCalSTRS* in the future. Go to www.CalSTRS.com and register today so you won't miss out!



Vote Your Proxy

By Jack Ehnes, Chief Executive Officer

Whether you are an individual investor with a handful of shares or an institutional investor with millions at stake, voting your proxy is a powerful tool you can use to influence corporate governance and social and environmental policies at the companies in your portfolio.

And in this age of the Internet, when you can discreetly buy and sell stocks online, all it takes is a few mouse clicks through the proxy process to be a shareholder activist.

What is proxy voting? Owning stock in a company gives you the right to vote on important matters concerning corporate policies and governance, including the election of directors who sit on the company's board. A U.S. public company is required by law to send shareholders a proxy statement and proxy card, or ballot, before holding its annual meeting. The proxy statement discusses the company's management, operations and financial performance along with descriptions of proposals on which shareholders can vote. While shareholders can vote in person at annual meetings, most vote by marking and signing the proxy card and returning it by mail or electronically via a proxy voting service.

Social and environmental issues are popping up on proxy ballots with

increasing frequency, livening up the once-staid proxy season by spotlighting labor practices and climate change risk. These proposals deserve the attention of shareholders large and small. Their growing popularity has been fueled in part by former Vice President Al Gore's 2006 Academy Award-winning hit documentary, *An Inconvenient Truth*, which elevated global warming as a national issue.

So how can ordinary shareholders use the proxy process to make their votes count at corporations? It's easy. You can do your own due diligence at home on your computer. Companies now routinely post their proxy statements online, either on their Web sites or on proxy-dedicated Web sites hosted by the companies or a proxy voting agent. The companies will provide you with a "Notice Regarding the Availability of Proxy Materials" and detailed instructions on how to cast votes electronically.

You will be directed to a Web site where complete meeting materials and instructions on how to use the voting platform are available. Your confidentiality will be preserved with a control or identification number that you will use only to vote proxies or provide proxy voting instructions.

In the time it takes to program your TiVo, you can weigh in on critical corporate issues that can affect your investment portfolio. We usually associate voting with the political world, but voting your proxy is a key legal right in business that deserves the attention of all investors.

Where can I get answers to questions about my Form 1099-R?

Answers to frequently asked questions about CalSTRS Form 1099-Rs are on our Web site at www.calstrs.com/help/faqs/1099faqs.aspx. If you can't find your answer there or don't have Internet access, please call us toll-free at 800-228-5453 (TTY: 916-229-3541).

I have 403(b) and 457 accounts with CalSTRS. Am I required to withdraw funds from those accounts at any specific time?

Yes. Federal law requires that most of the benefits in your 403(b) or 457 retirement plan be paid to you during your lifetime rather than to your beneficiaries after your death. Consequently, you must begin to take certain distributions from your account after a specific date. If you don't take out the required minimum, you will owe additional federal income tax.

Your first required distribution must take place by April 1 of whichever comes later:

- The year following the calendar year in which you turn 70½
- The year following the calendar year in which you retire

The required amount of the distribution will vary depending on the specifics of your account and your age.

The federal tax on an unpaid minimum distribution is 50 percent. If you're turning age 70 before July 1, 2008, be sure to talk with your tax advisor about the required distributions so you don't face an unwelcome surprise at tax time next year.

Ask CalSTRS

Why is CalSTRS building a new headquarters instead of using the money for teacher pensions?

The formula for CalSTRS defined benefit pensions and annual benefit adjustment are set by the Legislature, not CalSTRS. As a result, CalSTRS cannot increase educators' benefits without a change in state law.

The income from CalSTRS investments, including income from real estate investments, provides about 70 cents of every benefit dollar. The new headquarters is part of our real estate investment portfolio—an investment in better service to our members and improvement to the West Sacramento community. Lease payments on the new building will provide a reasonable rate of return to the Teachers' Retirement Fund while its energy-efficient features will save over \$145,000 a year in energy costs. Consolidating operations now located in three older buildings will create an efficient, productive work environment. And most important, we'll be able to serve you better with a member service center, workshop rooms and improved board meeting facility just a few short blocks from the State Capitol.

CalSTRS' smart choices in the construction process will save approximately \$13.2 million and ensure the project is completed on schedule. The new headquarters is a good investment for California educators.

Retired Educators Win Big in SBMA Ruling *continued from page 1*

"The court spoke loud and clear today," said Teachers' Retirement Board Chair Dana Dillon, responding to the decision. "The state cannot interfere with promised benefits to teachers. Our most vulnerable members are the true winners in this ruling."

The state made a \$500 million payment on September 10.

Supreme Court rejects state appeal

On October 9, 2007, the Department of Finance appealed the Court of Appeal's interest ruling to the California Supreme Court, disputing the increase in the prejudgment interest rate. On November 14, the Supreme Court declined to review the appellate court decision, leaving it to stand as issued.

The \$200 million interest payment will require a legislative appropriation.



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Call Us Early, Call Us Late!

Phone center hours extended

Last year's CalSTRS member survey showed that 75 percent of those contacted preferred to call our phone service center outside our usual hours. To serve you better and help you get fast answers to your questions, we're now open 11 hours a day.

Call us at 800-228-5453

7 a.m. to 6 p.m., Pacific time
Monday through Friday, except state holidays

