# Omaha School Employees' Retirement System

Financial Statements
August 31, 2008

Together with Independent Auditor's Report

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SEIM JOHNSON

## Independent Auditor's Report

To the Board of Education
Omaha School Employees' Retirement System:

We have audited the accompanying financial statements of the Omaha School Employees' Retirement System (OSERS), a fiduciary fund of Douglas County School District #0001 (District), as of and for the year ended August 31, 2008, as listed in the table of contents. These financial statements are the responsibility of District's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the activity of OSERS and do not purport to, and do not, present fairly the financial position of the District as of August 31, 2008, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of OSERS as of August 31, 2008, and the changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 7, 2008, on our consideration of OSERS' internal control over financial reporting and 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the Untied States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was performed for the purposes of forming an opinion on the financial statements taken as a whole. The accompanying schedules of funding progress and employer contributions are not a required part of the basic financial statements, but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and do not express an opinion on it.

Seim, Johnson, Sestak & Quist, LLP

Omaha, Nebraska,
November 7, 2008.



Seim Johnson Sestak & Quist, LLP > 8807 Indian Hills Drive, Suite 300 > Omaha, NE 68114-4123 > Tel: 402.330.2660 > Fax: 402.330.5108 > SeimJohnson.com

### Overview

The following overview is a discussion and analysis of the financial activities of the School Employees' Retirement System of Douglas County School District 0001, more commonly known as the Omaha School Employees' Retirement System (OSERS), for the fiscal year ended August 31, 2008. Its purpose is to provide explanation and insights into the information presented in the financial statements, notes to the financial statements, and required supplementary information.

### Financial Highlights

Net assets in the plan, which represent funds available to pay current and future pension benefits, decreased by $67.3 million during the fiscal year to $1,050 million. This 6% decrease in net assets was due to adverse investment performance during a very challenging economic period.

The plan experienced total additions of only $6.5 million. This amount was significantly less than the previous fiscal year due to decreased investment income and appreciation as a result of the poor economic period. Deductions from the plan of $73.9 million were higher than last year due to increased numbers of retirees who are receiving greater retirement benefits.

### Overview of the Financial Statements

The discussion and analysis below is intended to assist the reader in better understanding the purpose and meaning of each of the key components of the financial statements, which are comprised of the following:

1. The Statement of Fiduciary Net Assets presents information about assets and liabilities, with the difference between the two reported as net assets held in trust for pension benefits. The level of net assets reflects the resources available to pay benefits to members when due. Over time, increases and decreases in net assets measure whether the financial position of OSERS is improving or deteriorating.
2. The Statement of Changes in Fiduciary Net Assets presents the results of fund operations during the year and discloses the additions and deductions from plan net assets. It supports the net change that has occurred to the prior year's net asset value on the statement of plan net assets.
3. The Notes to the Financial Statements provide additional information that is essential to gain a full understanding of the data provided in the basic financial statements. The notes provide important and detailed information about OSERS, the pension trust fund, and the statements themselves.
4. The Supplementary Information consists of data on the funded status of the plan and the status of contributions from the employer and the State of Nebraska.

### Financial Analysis

The following table shows condensed information from the Statement of Fiduciary Net Assets:

*Plan Net Assets (Thousands of Dollars)*

| | 2008 | 2007 | Change | Percent |
|---|---|---|---|---|
| Total assets | $ 1,056,690 | 1,117,834 | (61,144) | (5.47) |
| Total liabilities | 6,409 | 206 | 6,203 | 3011.17 |
| Net assets | $ 1,050,281 | 1,117,628 | (67,347) | (6.03) |

The following table shows condensed information from the Statement of Changes in Fiduciary Net Assets:

*Additions to Plan Net Assets - (Thousands of Dollars)*

| | | 2008 | 2007 | Change | Percent |
|---|---|---|---|---|---|
| Employer contributions | $ | 23,279 | 22,267 | 1,012 | 4.54 |
| Member contributions and transfers | | 20,756 | 17,737 | 3,019 | 17.02 |
| State contributions | | 5,064 | 4,033 | 1,031 | 25.56 |
| Total contributions and transfers | $ | 49,099 | 44,037 | 5,062 | 11.49 |
| Investment income and appreciation | $ | (43,497) | 164,101 | (207,598) | (126.51) |
| Other income | | 936 | 134 | 802 | 598.51 |
| Total investment and other income | $ | (42,561) | 164,235 | (206,796) | (125.91) |
| Total additions | $ | 6,538 | 208,272 | (201,734) | (96.86) |

*Deductions from Plan Net Assets - (Thousands of Dollars)*

| | | 2008 | 2007 | Change | Percent |
|---|---|---|---|---|---|
| Retirement benefits | $ | 70,368 | 66,000 | 4,368 | 6.62 |
| Refunds to members | | 2,544 | 2,286 | 258 | 11.29 |
| Administrative expense | | 973 | 790 | 183 | 23.16 |
| Total deductions | $ | 73,885 | 69,076 | 4,809 | 6.96 |

## Omaha School Employees' Retirement System

### Statement of Fiduciary Net Assets
### August 31, 2008 (Thousands of Dollars)

| | |
|---|---|
| ASSETS | |
| Cash and cash equivalents | $ 7,838 |
| Contributions receivable | |
| Employer | 1,379 |
| Employee | 1,006 |
| Total contributions receivable | 2,385 |
| Investments, at fair value | |
| Cash equivalents held in investment portfolios | 51,102 |
| US Government Securities | 4,925 |
| Domestic corporate bonds | 185,558 |
| International bonds | 7,267 |
| Domestic preferred stocks | 850 |
| Domestic common stocks | 411,432 |
| International common stocks | 173,989 |
| Limited partnerships | 48,177 |
| Real estate investments | 158,453 |
| Total investments | 1,041,753 |
| Accrued investment income | 4,714 |
| Total assets | 1,056,690 |
| LIABILITIES | |
| Accounts payable | 258 |
| Accrued payroll and benefits payable | 6,151 |
| Total liabilities | 6,409 |
| NET ASSETS | |
| Held in trust for pension benefits (A schedule of funding progress for the Plan is presented on page 11) | $ 1,050,281 |

## Omaha School Employees' Retirement System

### Statement of Changes in Fiduciary Net Assets
### For the Year Ended August 31, 2008 (Thousands of Dollars)

| | | |
|---|---|---|
| ADDITIONS | | |
| Contributions | | |
| Employee contributions | $ | 19,909 |
| Employer contributions | | 23,279 |
| State contributions | | 5,064 |
| Total contributions | | 48,252 |
| Investment income | | |
| Interest and dividends | | 30,704 |
| Net depreciation in fair value of investments | | (69,144) |
| | | (38,440) |
| Less investment expense | | (5,057) |
| Net investment income | | (43,497) |
| Purchases of service | | 847 |
| Other | | 936 |
| Total additions | | 6,538 |
| DEDUCTIONS | | |
| Retirement benefits | | 70,368 |
| Refunds to employees, including interest | | 2,544 |
| Administrative expenses - | | |
| Personnel costs | | 368 |
| Professional fees | | 530 |
| Other | | 75 |
| Total deductions | | 73,885 |
| NET DECREASE | | (67,347) |
| NET ASSETS HELD IN TRUST FOR PENSION BENEFITS | | |
| Beginning of year | | 1,117,628 |
| End of year | $ | 1,050,281 |

## (1) Summary of Significant Accounting Policies

The following is a summary of the significant accounting policies of the Omaha School Employees Retirement System (OSERS).

### A. *Reporting Entity*

In 1909, the Douglas County School District #0001 (the District) began maintaining a retirement system for its teachers. Subsequently, the District added two more retirement systems, one covering non-teaching school employees and one covering school cafeteria employees. In 1951, the Nebraska State Legislature consolidated the three systems into one new system. The new system, OSERS, is a defined-benefit plan.

OSERS is included as a fiduciary fund of the District. The financial statements present only the activity of the Omaha School Employees' Retirement System and do not purport to, and do not present fairly the financial position of the District, as of August 31, 2008, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

### B. *Basic Financial Statements*

The financial transactions of OSERS are included in the fiduciary funds of the District. The fund is accounted for by providing a separate set of self-balancing accounts that comprises its assets, liabilities, net assets, additions, and deductions. This fund is used to report assets held in a trustee or agency capacity for others and therefore are not available to support the Districts programs.

### C. *Basis of Accounting/Measurement Focus*

OSERS activity is accounted for on an economic resources measurement focus using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions to the plan are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the Plan.

### D. *Method Used to Value Investments*

OSERS invests in both short-term and long-term securities. Investment managers are utilized to advise the Board of Trustees regarding investments. The market value of the investments will fluctuate as a result of interest rate changes and general economic conditions. Investments are valued at fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. The fair value of real estate investments is based on independent appraisals. Investments that do not have an established market are reported at estimated fair value.

### E. *Net Realized Gains and Losses on Investments and Other*

Market value fluctuations and changes in yields make it beneficial to periodically trade securities. These trades are recommended by the investment managers and are intended to maximize growth and earnings. When a trade is executed, the market value is compared to the cost and any difference is recorded as net realized gain or loss. No adjustments are recognized for the anticipated change in growth or yield.

(2) **Cash and Investments**

A. *Legal and Contractual*

The Retirement investments are governed by State statute 79-9,108 and 79-9,111. These statutes state that the Trustees of the Retirement System, with approval of the Board of Education, shall invest and reinvest funds of the retirement system. The Board of Education shall approve or deny the investments each month. The trustees shall invest the funds of the retirement system in investments of the nature which individuals of prudence, discretion, and intelligence acquire or retain in dealing with property of another. Such investments shall not be made for speculation but for investments, considering the probable safety of their capital as the probable income derived.

The trustee shall not purchase investments on margin or enter futures contracts or other contract obligations which requires the payment of margin or enter into any similar contractual arrangement which may result in losses in excess of the amount paid or deposited with respect to investment contracts, unless such transaction constitutes a hedging transaction or is incurred for the purpose of portfolio or risk management for the funds and investments of the system. The Trustee may write covered call options or put options. The trustee may lend any security if cash, United States Obligations or United States government agency obligations with a market equal to or exceeding the market value of the security lent or received as collateral.

B. *Credit Risk*

The credit quality of the bonds held in the portfolio is listed below. Each bond investment manager is required to invest according to investment guidelines, including credit quality, established for them by the Board of Trustees.

Credit Quality Distribution of Securities
with Credit Exposures as a Percentage of Each Bond Account

| | | Atlantic Asset Management | Fountain Capital Management | Halbis Capital Management |
|---|---|---|---|---|
| Treasury | | 6.13% | | |
| Agency | | 29.85% | | |
| AAA | | 31.58% | | |
| AA | | 6.59% | | |
| A | | 12.05% | | 0.15% |
| BBB | | 13.80% | 2.70% | 2.67% |
| BB | | | 42.70% | 36.58% |
| B | | | 52.55% | 54.07% |
| CCC | | | 0.22% | 5.73% |
| CC | | | | 0.22% |
| C/D | | | | 0.03% |
| NR | | | 1.83% | 0.55% |
| Total Value | $ | 13,106 | 92,879 | 94,795 |

C. *Interest Rate Risk*

The retirement funds do not have a formal policy limiting investment maturities that would help manage its exposure to fair value losses that may result from increasing interest rates.

| Maturity (Years) | As a Percentage of Market Value |
|---|---|
| 0 to 5 | 68.85% |
| 6 to 10 | 30.01 |
| Over 10 | 1.14 |

D. *Individual Debt Investment*

The Retirement funds at August 31, 2008 contained no individual highly sensitive debt investments with exposure to interest rate changes.

E. *Foreign Currency Risk*

The exposure to foreign currency is outlined below on a portfolio wide basis:

| Currency | Market Value | Percentage of Portfolio |
|---|---|---|
| Australian Dollar | $ 10,178,681 | 0.97 |
| British Sterling Pound | 16,124,310 | 1.54 |
| Canadian Dollar | 6,769,260 | 0.65 |
| EMU (Euro) | 12,998,710 | 1.24 |
| Hong Kong Dollar | 23,908,889 | 2.28 |
| Japanese Yen | 51,760,958 | 4.95 |
| Singapore Dollar | 4,163,337 | 0.40 |
| Swedish Krona | 6,105,479 | 0.58 |
| Swiss Franc (Chf) | 9,408,228 | 0.90 |
| United States Dollar | 905,049,870 | 86.49 |
| Total | $ 1,046,467,722 | 100.00 |

The retirement system's foreign currency-denominated investments include both corporate bonds and stocks.

## (3) Plan Description and Contribution Information

A. *Membership Information*

Membership consisted of the following as of September 1, 2007, the date of the latest actuarial valuation:

| | |
|---|---|
| Retirees and beneficiaries receiving benefits | 3,245 |
| Deferred vested plan members | 483 |
| Active and leave of absence plan members | 7,041 |
| Total | 10,769 |

B. *Background of the Plan*

In 1909, the District began maintaining a retirement system for its teachers. Subsequently, the District added two more retirement systems, one covering non-teaching school employees and one covering school cafeteria employees. In 1951, the Nebraska State Legislature consolidated the three systems into one new system. The new system, OSERS, is a defined-benefit plan.

C. *Plan Description*

The employees of the District, OSERS and Educational Service Unit #19 are covered by OSERS. OSERS is a single-employer retirement plan.

In accordance with Nebraska statutes, OSERS is governed by the Board of Education, which is advised by a Board of Trustees composed of three employees, one annuitant, three Board of Education members, two business people, and the Superintendent of the District. OSERS is administered by the Executive Director of the System.

D. *Contributions*

Employees of the District, OSERS and Educational Service Unit #19 are required to contribute 7.30% of their annual salary to OSERS. The District, OSERS and Educational Service Unit #19 contribute 7.373% of member salaries or such amount above 7.373% necessary to maintain the solvency of OSERS. The State of Nebraska contributes 7/10ths of 1% of the employees' compensation and an additional sum in accordance with State Statute 79-988.01. Administrative costs of OSERS are financed through investment earnings.

E. *Payment of Benefits and Refunds*

Each employee who has completed five or more years of creditable service is eligible to elect a deferred vested service annuity in lieu of a refund of accumulated contributions. OSERS provides for various benefits including normal retirement benefits, early retirement benefits, disability benefits, and pre-retirement and post retirement survivor benefits. These benefits are paid monthly from OSERS. The benefits under OSERS are based on an average of the highest three years of salary earned by employees during their employment with the District, up to their normal retirement dates. Employees who terminate employment with less than five years of creditable service can elect to receive a refund or a rollover of the employee's contributions plus accrued interest.

## (4) Funded Status and Funding Progress

The funded status of the Plan as of September 1, 2007, the most recent actuarial valuation date, is as follows:

| Actuarial Value of Assets (a) | Actuarial Accrued Liability (AAL) (b) | Unfunded AAL (UAAL) (b-a) | Funded Ratio (a/b) | Covered Payroll (c) | UAAL as a Percentage of Covered Payroll ((b-a)/c) |
|---|---|---|---|---|---|
| $1,117,628,000 | $1,255,527,000 | $137,899,000 | 89.00% | $272,844,149 | 50.54% |

The schedule of funding progress, presented as required supplementary information (RSI) following the notes to the financial statements, present multiyear trend information about whether the actuarial values of Plan assets are increasing or decreasing over time relative to the AALs for benefits.

Additional information as of the latest actuarial valuation is as follows:

- Actuarial valuation date is September 1, 2007.
- The actuarial cost method used to determine the ARC is the Entry Age Normal Cost Method.
- The assets are shown at actuarial value which is a market-related smoothed value.
- Economic assumptions are:

  Inflation: 3.5%
  Investment Return: 8.0%
  Salary increases: 4.0% plus merit of 0% to 2.6%
  Post-retirement benefit increases: 1.5%

- The amortization period is a closed 30 year period.

## (5) Commitments and Contingencies

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The District carries commercial insurance for risks of loss including workers' compensation. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years. The District contracts with reputable carriers and utilizes deductibles ranging from $1,000 to $350,000 per claim, and $250,000 to $2,600,000 in the aggregate, depending on the type of insurance. The District has established three separate funds to address the payment of claims which are less than the deductible amounts. Actual claims paid from these funds did not exceed the District's expectations during the fiscal year ended August 31, 2008. Also, the District has a line of credit up to $1,300,000 with a financial institution for purposes of payment of premiums for general liability and automobile liability.

## (6) Subsequent Events

Subsequent to year-end, the credit and liquidity crisis in the United States and throughout the global financial system has resulted in substantial volatility in financial markets and the banking system. These and other economic events have had a significant adverse impact on investment portfolios. As a result, the Plan's investments have likely incurred a significant decline in fair value since August 31, 2008.

# Omaha School Employees' Retirement System

## Schedule of Funding Progress
## For the Year Ended August 31, 2008

| Actuarial Valuation Date | Actuarial Value of Assets (a) | Actuarial Accrued Liability (AAL) (b) | Unfunded AAL (UAAL) (b-a) | Funded Ratio (a/b) | Covered Payroll (c) | UAAL as a Percentage of Covered Payroll ((b-a)/c) |
|---|---|---|---|---|---|---|
| 9/1/1997 | 552,614,545 | 629,006,550 | 76,392,005 | 87.86% | 159,480,000 | 47.90% |
| 9/1/1998 | 593,850,065 | 674,707,945 | 80,857,880 | 88.02% | 163,389,532 | 49.49% |
| 9/1/1999 | 660,763,772 | 745,189,416 | 84,425,644 | 88.67% | 172,950,471 | 48.81% |
| 9/1/2000 | 764,436,759 | 842,915,774 | 78,479,015 | 90.69% | 184,179,640 | 42.61% |
| 9/1/2001 | 800,544,438 | 897,398,640 | 96,854,202 | 89.21% | 199,851,531 | 48.46% |
| 9/1/2002 | 800,819,106 | 963,802,083 | 162,982,977 | 83.09% | 212,241,690 | 76.79% |
| 9/1/2003 | 817,966,471 | 1,009,062,603 | 191,096,132 | 81.10% | 211,692,872 | 90.27% |
| 9/1/2004 | 843,486,000 | 1,006,324,000 | 222,838,000 | 79.10% | 222,667,000 | 100.08% |
| 9/1/2005 | 887,165,000 | 1,126,967,000 | 239,802,000 | 78.70% | 231,708,783 | 103.49% |
| 9/1/2006 | 948,938,000 | 1,195,354,000 | 246,416,000 | 79.40% | 248,759,070 | 99.06% |
| 9/1/2007 | 1,117,628,000 | 1,255,527,000 | 137,899,000 | 89.00% | 272,844,149 | 50.54% |

## Schedule of Employer Contributions
## For the Year Ended August 31, 2008

| Year Ending | Annual Required Contribution (a) | Total Employer Contribution (b) | Percentage of ARC Contribution (b/a) |
|---|---|---|---|
| 8/31/1998 | 12,816,177 | 12,816,177 | 100.00% |
| 8/31/1999 | 14,703,164 | 14,703,164 | 100.00% |
| 8/31/2000 | 14,750,128 | 14,750,128 | 100.00% |
| 8/31/2001 | 15,435,941 | 15,435,941 | 100.00% |
| 8/31/2002 | 15,287,495 | 15,160,351 | 99.20% |
| 8/31/2003 | 17,927,131 | 18,328,875 | 102.20% |
| 8/31/2004 | 20,046,306 | 19,630,300 | 97.90% |
| 8/31/2005 | 22,459,221 | 20,210,403 | 90.00% |
| 8/31/2006 | 24,311,628 | 26,766,000 | 110.10% |
| 8/31/2007 | 28,143,388 | 24,981,000 | 88.80% |

SEIM JOHNSON

# 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

To the Board of Education
Omaha School Employees' Retirement System:

We have audited the financial statements of the Omaha School Employees' Retirement System (OSERS) as of and for the year ended August 31, 2008, and have issued our report thereon dated November 7, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

## *Internal Control Over Financial Reporting*

In planning and performing our audit, we considered OSERS' internal control over financial reporting as a basis for designing our auditing procedures 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 internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of OSERS' internal control over financial reporting.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with accounting principles generally accepted in the United States of America such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

## *Compliance and Other Matters*

As part of obtaining reasonable assurance about whether OSERS' financial statements are free of 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.

This report is intended solely for the information and use of the Board of Education, Board of Trustees, management, and the appropriate Federal and state regulatory agencies, and is not intended to be and should not be used by anyone other than these specified parties.

Seim, Johnson, Sestak & Quist, LLP

Omaha, Nebraska,
November 7, 2008.



Seim Johnson Sestak & Quist, LLP > 8807 Indian Hills Drive, Suite 300 > Omaha, NE 68114-4123 > Tel: 402.330.2660 > Fax: 402.330.5108 > SeimJohnson.com