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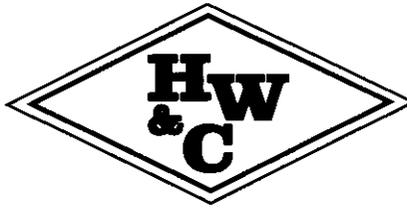
**Teachers' Retirement System of Louisiana
GASB 40 Note Disclosure
Years Ended June 30, 2004 and 2003**

Under provisions of state law, this report is a public document. A copy of the report has been submitted to the entity and other appropriate public officials. The report is available for public inspection at the Baton Rouge office of the Legislative Auditor and, where appropriate, at the office of the parish clerk of court.

Release Date 12-15-04

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CERTIFIED PUBLIC ACCOUNTANTS

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September 9, 2004

Independent Auditor's Report

Members of the Board of Trustees
Teachers' Retirement System of Louisiana
Baton Rouge, Louisiana

Members of the Board:

We have audited the financial statements of the

**Teachers' Retirement System of Louisiana
Baton Rouge, Louisiana**

a component unit of the State of Louisiana for the years ended June 30, 2004 and 2003 in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to the financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and issued our report thereon dated September 9, 2004. We have also audited the accompanying GASB 40 investment disclosure for the Teachers' Retirement System of Louisiana for the years ended June 30, 2004 and 2003. This schedule is the responsibility of the Teachers' Retirement System of Louisiana's management. Our responsibility is to express an opinion on this schedule based on our audit.

We conducted our audit of the GASB 40 investment disclosure in accordance with auditing standards generally accepted in the United States of America and the standards applicable to the 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 GASB 40 investment disclosure is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the GASB 40 investment disclosure. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall GASB 40 investment disclosure presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the GASB 40 investment disclosure referred to above presents fairly, in all material respects, the early implementation disclosure of GASB 40 of Teachers' Retirement System of Louisiana for the years ended June 30, 2004 and 2003, in conformity with accounting principles generally accepted in the United States of America.

This report is intended solely for the information and use of the Board of Trustees for the Teachers' Retirement System of Louisiana, the State of Louisiana Division of Administration, the Office of the Legislative Auditor of the State of Louisiana, and management and is not intended to be and should not be used by anyone other than these specified parties. Under Louisiana Statute 24:513, this report is distributed by the Legislative Auditor as a public document.

Yours truly,

Hawthorn, Weymouth, & Carroll L.L.P.

**TEACHERS' RETIREMENT SYSTEM OF LOUISIANA
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2004 AND 2003**

DEPOSIT AND RISK DISCLOSURES

The tables presented below include disclosures of custodial, interest rate, credit, and foreign currency risks in accordance with GASB 40 and are designed to inform financial statement users about investment risks that could affect the System's ability to meet its obligations. These tables classify investments by risk type, while the financial statements present investments by asset class; thus, the totals shown on the tables may not be comparable to the amounts shown for the individual asset classes on the financial statements.

CASH AND CASH EQUIVALENTS

Included in Teachers' Retirement System of Louisiana's Audited Financial Statements for June 30, 2004.

INVESTMENTS

Louisiana Revised Statutes 11:263 authorized the Board of Trustees to invest under the "Prudent-Man" rule. The Prudent-Man Rule establishes a standard that a fiduciary shall exercise the judgment and care under the circumstances, then prevailing, which an institutional investor of ordinary prudence, discretion, and intelligence exercises in the management of large investments entrusted to it, not in regard to speculation but in regard to the permanent disposition of funds considering probable safety of capital as well as probable income.

In accordance with Louisiana Revised Statutes 11:267, the System may invest up to 65% of its total assets in equities provided that the System invests an amount equal to at least 10% of total stock in equity indexing. The index portfolio(s) shall be invested in indices that seek either to replicate or to enhance a particular index. The index portfolio(s) may be invested in a variety of equity capitalization ranges and could be invested in either domestic or international equity.

The System has no investments of any single organization (other than those issued or guaranteed by the U.S. Government) that represents 5% or more of the System's net plan assets, nor does the System hold more than 5% of any corporation's stock. In addition, the Board of Trustees has adopted certain investment policies, objectives, rules and guidelines that are intended to protect the System's assets in real terms such that assets are preserved to provide benefits to participants and their beneficiaries; achieve investment returns sufficient to meet the actuarial assumption necessary to improve the future soundness of the System; and maximize the total rate of return on investments within prudent parameters of risk for a retirement system of similar size and type.

The Board of Trustee's desired investment objective is a long-term compound rate of return on the System's assets of 3.9% above the CPI-U seasonally adjusted or the actuarial rate (currently 8.25%), which ever is higher.

During Fiscal Year 2004, the System's investments (including investments bought, sold, and held during the year) appreciated in value by \$1,488,052,719 compared to depreciation of \$13,188,622 in 2003.

TEACHERS' RETIREMENT SYSTEM OF LOUISIANA
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	<u>2004</u>	<u>2003</u>
Increase/(decrease) in fair value of investments held at year end:	\$561,550,408	\$503,225,833
Realized gains/(losses) on investments including currency sold during the year:	<u>926,502,311</u>	<u>(516,414,455)</u>
Total	<u>\$1,488,052,719</u>	<u>\$ (13,188,622)</u>

The following table presents the fair value of investments by type at June 30, 2004 and 2003, respectively:

	<u>2004 Fair Value</u>	<u>2003 Fair Value</u>
Investments - Type		
Bonds		
Domestic not on securities loan	\$1,125,737,871	\$1,164,640,472
International not on securities loan	403,221,476	37,623,969
Common and preferred stocks		
Domestic not on securities loan	3,824,171,679	1,955,098,625
Domestic on securities loan for securities collateral or letters of credit	73,737,867	80,246,255
International not on securities loan	1,267,218,161	940,674,133
Investments held by broker-dealers under securities loans with cash collateral		
Bonds		
Domestic	533,822,121	539,894,429
International	157,430,363	378,808,699
Common stocks		
Domestic	1,028,836,000	2,433,595,000
International	186,918,142	92,981,064
Domestic money market funds	910,719,505	434,080,034
Real estate investment	494,342,545	451,697,324
Mezzanine financing investments	335,701,043	325,414,623
Private equity investments	<u>1,433,141,536</u>	<u>1,541,367,296</u>
Total	<u>\$11,774,998,309</u>	<u>\$10,376,121,923</u>

Note: Used information in annual report note disclosures (GASB Stmt 3) due to change in investment custodian & information not being readily available for comparison.

CUSTODIAL CREDIT RISK

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the pension trust fund will not be able to recover the value of its investment or

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JUNE 30, 2004 AND 2003

collateral securities that are in possession of an outside party. Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the government, and are held by either the counterparty or the counterparty's trust department or agent but not in the System's name.

Teachers' Retirement System of Louisiana has no custodial credit risk at June 30, 2004 and 2003 since all investments were registered in the name of the System and held in the possession of the System's custodial bank, Mellon Bank, and securities lending advisor, Custodial Trust Company.

CREDIT RISKS

The System expects the domestic and international securities investment managers to maintain diversified portfolios by sector and by issuer using the following guidelines:

- A. Investments in fixed income securities shall be high quality marketable securities meeting one or more of the following criteria for domestic managers:
- (1) All U.S. Treasury, federal agencies, and U.S. Government guaranteed obligations.
 - (2) Corporate bonds, debentures, notes, asset-backed securities, and equipment trust certificates rated Baa3 or BBB- or higher (investment grade) by Moody's or Standard & Poor's (includes split-rated bonds).
 - (3) Mortgage securities will be limited to pass-throughs, collateralized mortgage obligations, adjustable rate mortgages, commercial mortgage-backed securities, and other mortgage securities deemed prudent by the investment manager. The use of interest-only strips and principal-only strips may not exceed 10% of the portfolio.
 - (4) Municipal bonds rated Baa3 or BBB- or higher may not exceed 20% of the market value of the bond portfolio.
 - (5) Positions in any one issuer of corporate or municipal securities are not to exceed 5% of the market value of the bond portfolio, measured at the time of purchase.
 - (6) Holdings of individual issues are to be of sufficient size to accommodate easy liquidation.
 - (7) Private placements (including Rule 144As) may be held, provided that holdings do not exceed 25% of the market value of the bond portfolio. High-yield portfolios and Mezzanine Limited Partnerships are excluded from this restriction.
 - (8) Debt obligations of foreign governments, corporations, and supranationals issued outside of the U.S. (Eurobonds and non-U.S. dollar bonds) may be held by investment managers.
 - (9) High yield portfolios are to be invested in debt securities (including convertibles) rated from Ba1 to Caa (Moody's rating) or BB+ to CCC (Standard & Poor's rating)

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and in unrated securities determined to be of comparable quality by the manager. Unrated securities and securities rated Caa, CCC, or below shall not exceed 20% of the market value of the portfolio.

- (10) High yield portfolios are subject to the criteria in paragraphs (5) and (6) with bond rating modified according to paragraph (9).
 - (11) Investment grade fixed income portfolios are to be invested in fixed income securities pursuant to paragraphs (1), (2), (3), (4), (5) and (6) above, except that all securities, at the time of purchase, shall be investment grade. If a security is downgraded below investment grade, the investment manager will work to seek the best resolution over time to such downgrade.
 - (12) Investment grade fixed income portfolios shall not invest in mortgage-backed inverse floaters, interest-only, principal-only strips or highly volatile less liquid tranches.
 - (13) Investment grade fixed income portfolios may invest in debt obligations of foreign governments, corporations, and supranationals issued in the United States and are dollar denominated (Yankee) securities. Aggregate weighting of these securities shall be limited to 10% of the market value of the portfolio.
- B. Investments in fixed income securities shall be high quality marketable securities meeting one or more of the following criteria for global fixed income managers:

Items (1) through (7) of the fixed income guidelines for domestic managers will apply with the following additional guidelines.

- (1) The debt of countries, foreign and domestic agencies, foreign and domestic corporations, and supranational entities are acceptable for investment. The manager should consider the creditworthiness and the liquidity of a potential security before making an investment. The manager should also review whether the custodian has a subcustodian within a particular country before considering an investment.
- (2) Portfolio weightings in countries represented in the Citibank World Government Bond Index, including cash, may range from 0% to 100% of the portfolio.
- (3) Portfolio weightings in countries not represented in the Citibank World Government Bond Index, including cash, may not, in aggregate, exceed 40% of the portfolio market value without Board approval. However, practical consideration should be given to liquidity and marketability of issues, particularly within nonmajor and emerging markets.
- (4) Quality ratings for corporate debt shall be consistent with those stated in item (2) of the Fixed Income Guidelines for Domestic Managers.

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- (5) Permitted hedge vehicles for currency exposure management are as follows:
- (a) Forward Foreign Exchange Contracts
 - (b) Currency Futures Contracts
 - (c) Options on Currency Futures Contracts
 - (d) Options on Spot Currencies
- (6) Net short foreign currency positions may not be taken in this portfolio.
- C. Investments in common stock securities, including ADRs, shall be high quality, readily marketable securities offering potential for above-average growth. Common stock investments are limited to those meeting all of the following criteria:
- (1) Stocks must be listed or traded on a national securities exchange, including the NASDAQ. ADR securities may be traded over the counter. U.S. stocks must be registered with the Securities and Exchange Commission. The use of derivatives (such as Exchange Traded Funds (ETFs), options, warrants, and futures to establish unleveraged long positions in equity markets) is permissible.
 - (2) No more than 5% of the total outstanding shares of common stock for any one corporation may be held in the System's equity portfolio.
 - (3) No more than 5% of the cost or market value of the System's equity portfolio (whichever is more) or 15% of the market value of each manager's portfolio may be invested in the common stock of any one corporation.
 - (4) No more than 20% of stock valued at market of the System's equity portfolio may be held in any one industry category as defined by the custodian.
 - (5) Convertible securities and covered-option writing, if any, shall be considered as part of the equity portfolio.
 - (6) Equity managers (growth or value) hired for the small cap investment category are expected to maintain a weighted average market capitalization of the portfolio within minus 50% and plus 100% of the weighted average market capitalization of the Russell 2000 Index (growth or value, respectively).
 - (7) Equity managers (growth or value) hired for the mid cap investment category are expected to maintain a weighted average market capitalization of the portfolio within plus or minus 50% of the weighted average market capitalization of the Russell Mid Cap Index (growth or value, respectively).
- D. Investments in common stock securities of Developed Markets (EAFE Countries and Canada), shall be high quality, readily marketable securities offering potential for above-average growth. Items (2), (4), and (5) of the Stock Guidelines for Domestic Managers will apply with the following additional guidelines.

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- (1) Investment managers may invest up to 20% of the market value of the portfolio in the emerging market countries contained in the IFC Investable Index, including up to 5% (of the 20% limit) in emerging market countries not contained in the IFC Investable index. Managers should consider liquidity and marketability of issues, particularly within non-major and emerging markets, and should also be sensitive to the weight of individual economic sectors of the market within the portfolio. The manager should also review whether the custodian has a subcustodian within a particular country before considering an investment.
- (2) Investment managers may invest up to 10% of the portfolio's market value in domestic equity securities. This flexibility should be viewed by the manager as an opportunistic or defensive mechanism rather than a normal position.
- (3) No single industry group shall constitute more than 25% of the portfolio's market value or its equivalent representation in the EAFE Index; whichever is more, without prior Board approval.
- (4) No individual security shall constitute more than 10% of the portfolio's market value.
- (5) Cash held by the manager may be in U.S. dollars or foreign currencies of the manager's choice.
- (6) Residual currency exposures of the underlying international equity portfolio may be actively managed by the investment manager. If actively managed, the objectives of the foreign exchange exposure management, within the international equity portfolio, are to:
 - (a) Add value by increasing total returns and reducing volatility of returns through hedging and cross-hedging activities.
 - (b) Avoid currency losses in periods of an appreciating U.S. dollar.
- (7) Permitted Equity Investments
 - (a) Equity managers are to confine investments to common stocks and securities that are directly convertible or exercisable into common stocks, including ADRs and GDRs.
 - (b) Use of derivatives such as options, warrants, and futures to establish unleveraged long positions in equity markets is permissible.
 - (c) Currency options contracts may be exchange traded or over-the-counter (OTC) traded in the interbank market. Additional instruments, such as swaps, or other derivatives, may be used if the risk/return trade-off is perceived by the manager to be suitable and competitive with the above-stated hedge vehicles.

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- (d) International equity managers may invest up to 10% of the portfolio in Rule 144A securities.
- (8) Permitted hedge vehicles for currency exposure management are as follows:
- (a) Forward Foreign Exchange Contracts
 - (b) Currency Futures Contracts
 - (c) Options on Currency Futures Contracts
 - (d) Options on Spot Currencies
- (9) Net short foreign currency positions may not be taken in this portfolio

Credit Risk is defined as the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The System's exposure to credit risk at June 30, 2004, was as follows:

<u>Moody's Rating</u>	<u>Total</u>	<u>Domestic</u>	<u>International</u>
Not Rated	\$1,014,327,741	\$969,086,083	\$45,241,658
A1	13,791,639	13,684,220	107,419
A2	35,940,641	3,774,975	32,165,666
A3	22,673,159	22,499,230	173,929
AA1	26,992,544	3,392,030	23,600,514
AA2	32,532,365	5,189,295	27,343,070
AA3	11,939,593	11,939,593	
AAA	445,517,213	73,477,475	372,039,738
AGY	568,098,160	568,098,160	
B1	111,438,772	102,357,941	9,080,831
B2	197,810,091	193,369,529	4,440,562
B3	181,942,911	166,805,395	15,137,516
BA1	35,717,654	34,130,629	1,587,025
BA2	44,221,589	40,037,778	4,183,811
BA3	131,218,789	121,597,839	9,620,950
BAA1	23,498,014	10,571,739	12,926,275
BAA2	11,071,253	10,260,080	811,173
BAA3	13,331,273	12,661,470	669,803
CA	1,908,252	1,908,252	
CAA1	42,183,486	42,183,486	
CAA2	6,047,138	6,047,138	
CAA3	2,017,000	2,017,000	
N/A	9,888,139	8,688,172	1,199,967

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<u>Moody's Rating</u>	<u>Total</u>	<u>Domestic</u>	<u>International</u>
NR	2,210,000	2,210,000	
UST	132,643,657	132,643,657	
VMIG1	1,511,250	1,511,250	
WR	<u>10,459,013</u>	<u>10,137,081</u>	<u>321,932</u>
Total credit risk debt securities	<u>\$3,130,931,336</u>	<u>\$2,570,279,497</u>	<u>\$560,651,839</u>

INTEREST RATE RISK

Interest rate risk is defined as the risk that changes in interest rates will adversely affect the fair value of an investment. As of June 30, 2004, the System had the following investments and maturities:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Investment Maturities (in years)</u>			
		<u>< 1</u>	<u>1 - 5</u>	<u>5 - 10</u>	<u>> 10</u>
U S Treasury & Government Agency	\$614,396,445	\$49,637,987	\$213,455,137	\$26,998,452	\$324,304,869
Collateralized Mortgage Obligations	101,439,901	0	13,616,407	22,955,584	64,867,910
Corporate Bonds	678,633,501	6,486,058	170,544,067	445,365,495	56,237,881
Foreign Corporate Bonds	63,490,237	321,931	15,954,501	43,408,061	3,805,744
Foreign Government Bonds	467,851,017	48,914,560	212,579,396	161,427,528	44,929,533
Foreign Treasuries	29,310,585	0	0	29,310,585	0
Other	1,175,809,650	912,545,717	31,730,347	155,670,763	75,862,823
TOTAL	<u>\$3,130,931,336</u>	<u>\$1,017,906,253</u>	<u>\$657,879,855</u>	<u>\$885,136,468</u>	<u>\$570,008,760</u>

Teachers' Retirement System of Louisiana, as expressed in its Investment Policy Statement, expects its fixed income managers to approximate the portfolio's duration (a measure of a debt investment's exposure to fair value changes arising from changing interest rates) to its respective benchmarks, i.e. the Lehman Brothers Aggregate for domestic fixed income investments and CITI World Government Bond Index for international fixed income investments.

FOREIGN CURRENCY RISK

Foreign currency risk is defined as the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The System's exposure to foreign currency risk is limited to its investment in foreign marketable securities at June 30, 2004, as follows:

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Currency	Percent	Total	Bonds	Stocks
Australian Dollar	1.54%	\$27,684,224	\$25,218,467	\$2,465,757
British Pound Sterling	18.09%	325,195,804	62,301,253	262,894,551
Brazil Real	0.10%	1,756,430		1,756,430
Canadian Dollar	1.48%	26,670,445	14,760,069	11,910,376
Danish Krone	1.11%	20,042,310		20,042,310
Euro Currency Unit	35.66%	640,993,383	195,070,703	445,922,680
Hong Kong Dollar	2.23%	40,073,247		40,073,247
Indonesian Rupian	0.13%	2,392,988		2,392,988
Japanese Yen	18.67%	335,548,601	64,952,235	270,596,366
Malaysian Ringgit	0.14%	2,542,593		2,542,593
Mexican New Peso	0.91%	16,286,897	12,264,030	4,022,867
New Zealand Dollar	1.71%	30,743,729	30,743,729	
Norwegian Krone	1.72%	30,910,358	21,105,381	9,804,977
Polish Zloty	1.79%	32,165,666	32,165,666	
Singapore Dollar	1.67%	30,101,130		30,101,130
South Korean Won	0.77%	13,792,930		13,792,930
Swedish Krona	4.08%	73,312,731	39,492,146	33,820,585
Swiss Franc	7.57%	135,992,776		135,992,776
Thailand Baht	0.64%	11,420,833		11,420,833
Total	100.00%	\$1,797,627,075	\$498,073,679	\$1,299,553,396