

***Comprehensive
Annual Financial
Report June 30, 1985***

SCHOOL EMPLOYEES RETIREMENT SYSTEM

**SCHOOL EMPLOYEES RETIREMENT SYSTEM
OF OHIO**

45 NORTH FOURTH STREET
COLUMBUS, OHIO 43215

**COMPREHENSIVE ANNUAL
FINANCIAL REPORT**

*For The
Fiscal Year Ended June 30, 1985*

*Prepared By SERS Staff
Thomas R. Anderson,
Executive Director*

THE SCHOOL EMPLOYEES RETIREMENT BOARD OF OHIO



MARY E. KASUNIC

*President
Wickliffe City School District
Wickliffe, Ohio
Term expires June 30, 1989*



ANTHONY J. CELEBREZZE, JR.

*Attorney General
Ex Officio Member*



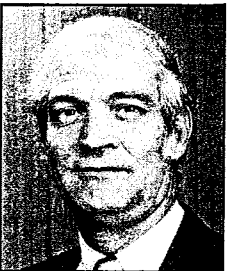
ORRIS E. FIELDS, JR.

*Vice President
Wilmington City School District
Wilmington, Ohio
Term expires June 30, 1987*



THOMAS E. FERGUSON

*Auditor of State
Ex Officio Member*



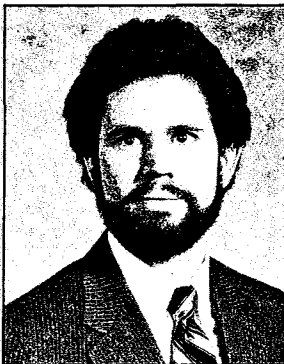
LOWELL B. DAVIS

*Employee-Member
Euclid City School District
Euclid, Ohio
Term expires June 30, 1989*



WILLIAM A. GUY

*Employee-Member
Columbus City School District
Columbus, Ohio
Term expires June 30, 1988*



THOMAS R. ANDERSON

Executive Director



AGNES F. O'KEEFE

*Retiree-Member
Westerville, Ohio
Term expires June 30, 1988*

ASSISTANT DIRECTORS

R. JACK COOPER

Investments

ROBERT E. HARTSOOK

Retirement Services

DALE D. McINTYRE

Information Services

THOMAS R. SKIPTON

Office Services

JOHN W. FRANK

Membership-Accounting

RITA M. VOLPI

Planning / Human Resources

C. DOUGLAS WILSON

Data Processing

ORGANIZATIONAL CHART

RETIREMENT BOARD
Mary E. Kasunic, President
Orris E. Fields, Jr., Vice President
Lowell B. Davis, Employee-Member
Agnes F. O'Keefe, Retiree-Member
William A. Guy, Employee-Member
Anthony J. Celebrezze, Jr., Attorney General
Thomas E. Ferguson, Auditor of State

EXECUTIVE DIRECTOR Thomas R. Anderson

Asst. Director Investments
R. Jack Cooper

Asst. Director Information Services
Dale D. McIntyre

Asst. Director Membership and Accounting
John W. Frank

Asst. Director Retirement Services
Robert E. Hartsook

Asst. Director Office Services
Thomas R. Skipton

Asst. Director Planning/Human Resources
Rita M. Volpi

Asst. Director Data Processing
C. Douglas Wilson

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SCHOOL EMPLOYEES RETIREMENT SYSTEM

45 North Fourth Street • Columbus, Ohio 43215 • Telephone (614) 221-5853

December 1, 1985

President and Members of the Retirement Board School Employees Retirement System

Dear President and Members:

The comprehensive annual financial report of the School Employees Retirement System (SERS) is submitted herewith. This report contains statements of financial condition, results of operation of the benefit programs administered by the SERS, schedules of significant data regarding the operation of the Retirement System, and the opinion of our certified public accountant, Peat, Marwick, Mitchell and Co. In addition, there is an Actuarial Section containing the opinion of our independent actuary, Gabriel, Roeder, Smith and Co., an Investment Section containing the investment report, schedules of portfolio activity, and a listing of our portfolio, and the Plan Summary.

Accounting System and Reports

This report was prepared in accordance with generally accepted accounting principles of governmental accounting and reporting as pronounced by the National Council of Governmental Accounting.

Transactions of the SERS are reported on the accrual basis of accounting. Our internal accounting controls are designed to insure the safekeeping of member contributions and to provide a reasonable degree of reliability regarding all of our financial records. During the past year we made a significant modification to our cash management system which allows us to deposit and subsequently invest cash receipts on a more timely basis. These cash receipts are treated as undistributed deposits until such time as they are allocated to member contributions, employer contributions, or investment income.

Review of Operations

In early 1985, the SERS undertook to develop a Long-Term Business Plan. In accordance with our mission of "Providing the Best Possible Benefits and Service to the Members and Retirants of the School Employees Retirement System," a document was prepared which forecasted a number of challenges to the System which must be addressed in the next few years, analyzed our ability to meet those environmental forces, and proposed several key goals and objectives to be achieved by our actions during those years.

In March, Board President Mary Kasunic was re-elected to a four-year term expiring in 1989. During her previous six-year tenure, Mrs. Kasunic served as Vice President for one year and President for two years.

Continuing efforts at effective cost management of the SERS health care program for retirees led to several changes in the plan. The maximum lifetime benefit under the Aetna program was increased from \$500,000 to \$1 million; the annual deductible went from \$100 to \$150 per person; and the retiree cost for each drug prescription was raised from \$1.00 to \$2.00.

On the federal front, there were renewed efforts to require all public employees to join Social Security. Another proposal would institute a tax on school employees and employers to pay for Medicare coverage. Although mandatory Social Security coverage did not develop as a serious proposal, Congress was still considering mandatory Medicare coverage as of the date this report was prepared.

Financial Highlights

Revenues:

Revenues from employee and employer contributions were \$73.1 million and \$119.1 million, respectively, while income from investments totaled \$153.9 million. This represents an increase over 1984 of 8.3% for employee contributions, 11.5% for employer contributions, and 6.0% for investment income. Contribution rates for both employees and employers remained unchanged from the prior year.

Expenses:

Expenses are incurred primarily for the purpose for which the Retirement System was created; namely, the payment of benefits. Included in the total expenses for fiscal 1985 were benefit payments, refunds of contributions due to member termination or death, transfers of contributions to other Ohio Systems to provide benefits for those members who hold membership in more than one system, and administrative expenses. Expenses for fiscal 1985 totaled \$162.3 million, an increase of 10.9% over 1984 expenses. Increases in the number of benefit recipients, the average benefit paid, and health care expense combined to increase benefit expense by \$15 million, accounting for nearly all of the increase in total System expenses for the fiscal year.

Financial Highlights (Continued)

Funding and Reserves:

Funds are derived from the excess of revenues over expenses, and are accumulated by the Retirement System in order to meet current and future benefit obligations to retirees and beneficiaries. The higher the level of funding, the larger the accumulation of assets and the greater the investment income potential.

Net income for the fiscal year 1985 resulted in an increase in fund balances of \$186.9 million. This increase is \$10.7 million greater than the total increase in fund balances for the fiscal year 1984.

The actuarial valuation, for funding purposes, dated June 30, 1985 reflects an unfunded accrued liability of \$1,402 million. This liability represents the difference between the computed actuarial accrued liability for benefits to be paid members and retirants (\$3,086 million) and total of fund balances and expected value of future payments for state subsidies (\$1,684 million). The current employer contribution rate of 14% is sufficient to amortize this unfunded accrued liability over 36 years. A year ago, the funding period was 37 years.

Additional information regarding funding is provided within the Actuarial Section (pages 24 to 26 of this report).

Investments

The School Employees Retirement System invests the previously mentioned funds in order to maximize both current income yield and long-term appreciation. For the fiscal year ended June 30, 1985, investments provided 44.1% of the System's total revenues while employee and employer contributions provided 20.9% and 34.1%, respectively; and other sources accounted for the remaining 0.9%.

At June 30, 1985, our investment portfolio was structured as follows: 51.6% in debt securities; 24.4% in equity securities; 12.7% in short-term investments; and 11.3% in real estate.

Portfolio composition, rates of return, and analysis of significant economic conditions, and additional information concerning our investments are presented in the Investment Section (pages 27 to 49).

Acknowledgments

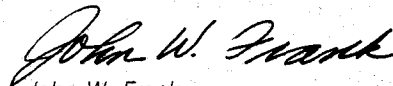
The preparation of this report is the result of the combined effort of the System's staff under the direction of the Retirement Board. It is intended to provide complete and reliable information as a basis for making management decisions, to disclose compliance with legal provisions, and as a means of determining responsible stewardship for the assets contributed by the members and their employers.

This report is being mailed to all employer members of the System and other interested parties.

Respectfully submitted,



*Thomas R. Anderson
Executive Director*



*John W. Frank
Assistant Director, Membership and Accounting*

**Financial
Statements**



Peat, Marwick, Mitchell & Co.
Certified Public Accountants
Two Nationwide Plaza
Columbus, Ohio 43215
614-221-3181

Honorable Thomas E. Ferguson
Auditor of State
State of Ohio

The Retirement Board
School Employees Retirement System of Ohio:

We have examined the balance sheets of the School Employees Retirement System of Ohio as of June 30, 1985 and 1984 and the related statements of revenues, expenses and changes in fund balance and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned financial statements present fairly the financial position of the School Employees Retirement System of Ohio at June 30, 1985 and 1984 and the results of its operations and the changes in its financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Our examinations were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information included in Schedules I through IV is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the examinations of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Peat, Marwick, Mitchell's Co.

November 11, 1985

BALANCE SHEET
Exhibit A

Financial Statements

Years ended June 30, 1985 and 1984

	1985	1984
Assets:		
Cash	\$ 428,419	\$ 683,162
Receivables:		
Contributions:		
Employers	60,576,671	51,586,334
Employees	6,866,775	7,094,695
State of Ohio subsidies	1,578,723	1,720,156
Accrued investment income	19,419,480	19,650,351
Investment sale proceeds	32,183,585	17,536,058
Total receivables	<u>\$ 120,625,234</u>	<u>\$ 97,587,594</u>
Investments, at cost (market \$1,697,945,355 and \$1,326,242,163, respectively)(notes 5 and 6)	<u>1,601,207,790</u>	<u>1,413,337,734</u>
Property and equipment, at cost (note7)	7,683,727	7,587,796
Less accumulated depreciation	<u>1,426,245</u>	<u>1,049,083</u>
Net property and equipment	<u>6,257,482</u>	<u>6,538,713</u>
Other assets	265,820	157,613
Total assets	<u>\$ 1,728,784,745</u>	<u>\$ 1,518,304,816</u>
Liabilities:		
Accounts payable and accrued expenses	\$ 451,179	\$ 358,690
Investment commitments payable	39,453,298	14,739,562
Accrued health care benefits payable	8,492,834	9,879,069
Notes payable	4,244,681	4,398,245
Other liabilities	<u>409,592</u>	<u>78,773</u>
Total liabilities	<u>\$ 53,051,584</u>	<u>\$ 29,454,339</u>
Net assets available for benefits	<u>\$ 1,675,733,161</u>	<u>\$ 1,488,850,477</u>
Fund balance (note 8):		
Actuarial present value of credited projected benefits for:		
Current retirants and beneficiaries	\$ 1,511,799,217	\$ 1,371,162,368
Present inactive members	111,168,934	101,847,922
Active members:		
Member contributions	432,528,863	396,230,502
Employer financed portion	<u>857,983,917</u>	<u>766,999,671</u>
Total actuarial present value of credited projected benefits	2,913,480,931	2,636,240,463
Unfunded actuarial present value of credited projected benefits payable	<u>(1,237,747,770)</u>	<u>(1,147,389,986)</u>
Total fund balance	<u>\$ 1,675,733,161</u>	<u>\$ 1,488,850,477</u>

See accompanying notes to financial statements.

**STATEMENTS OF REVENUES, EXPENSES
AND CHANGES IN FUND BALANCE**
Exhibit B

Financial Statements

Years ended June 30, 1985 and 1984

	1985	1984
Revenues:		
Contributions:		
Employers (note 4)	\$ 119,145,737	\$ 106,886,556
Employees	73,117,682	67,503,890
State of Ohio subsidies	1,578,723	1,720,155
Transfer from other Ohio systems	1,425,653	1,224,116
	<u>\$ 195,267,795</u>	<u>\$ 177,334,717</u>
Investment income (loss):		
Interest and dividends	\$ 126,576,303	\$ 117,932,778
Real estate income, net of depreciation expense of \$2,336,846 in 1985 and \$1,752,462 in 1984	12,500,660	10,401,237
Net realized gain on sale of investments	14,960,421	14,076,319
Gain (loss) on options traded net of option expense of \$3,586,244 in 1985 and \$2,212,774 in 1984	(103,355)	2,805,129
	<u>\$ 153,934,029</u>	<u>\$ 145,215,463</u>
Total revenues	<u>\$ 349,201,824</u>	<u>\$ 322,550,180</u>
Expenses:		
Benefits:		
Retirement	\$ 96,910,985	\$ 85,444,144
Disability	10,527,898	9,270,155
Survivor	8,004,136	7,389,851
Health care	30,778,698	29,153,910
Death	563,433	590,375
	<u>146,785,150</u>	<u>131,848,435</u>
Refund of employee contributions	8,373,795	7,827,632
Administrative expenses	5,673,205	4,658,760
Transfer to other Ohio systems	1,486,990	1,181,012
Loss on disposal of fixed assets	—	879,498
Total expenses	<u>\$ 162,319,140</u>	<u>\$ 146,395,337</u>
Net income	\$ 186,882,684	\$ 176,154,843
Fund balance, beginning of year	1,488,850,477	1,312,695,634
Fund balance, end of year	<u>\$ 1,675,733,161</u>	<u>\$ 1,488,850,477</u>

See accompanying notes to financial statements.

**STATEMENT OF CHANGES
IN FINANCIAL POSITION**
Exhibit C

Financial Statements

Years ended June 30, 1985 and 1984

	1985	1984
Resources provided by:		
<i>From operations:</i>		
Net income	\$ 186,882,684	\$ 176,154,843
<i>Items which do not use working capital:</i>		
Depreciation	381,002	382,692
Loss on disposal of property and equipment	—	879,498
Total resources provided from operations	<u>187,263,686</u>	<u>177,417,033</u>
Proceeds from disposal of property and equipment	1,219	90,804
Proceeds from notes payable	—	3,391,913
Other	80,631	—
Total resources provided	<u>\$ 187,345,536</u>	<u>\$ 180,899,750</u>
 Resources used by:		
Additions to property and equipment	100,990	1,049,069
Increase in other assets	108,207	43,054
Repayment of notes payable	234,195	194,846
Net increase in working capital	<u>186,902,144</u>	<u>179,612,781</u>
Total resources used	<u>\$ 187,345,536</u>	<u>\$ 180,899,750</u>
 Changes in components of working capital:		
<i>Increase (decrease) in current assets:</i>		
Cash	(254,743)	433,913
Receivables	23,037,640	32,019,676
Investments	187,870,056	139,711,385
	<u>\$ 210,652,953</u>	<u>\$ 172,164,974</u>
<i>Increase (decrease) in current liabilities:</i>		
Accounts payable and accrued expenses	92,489	126,540
Investment commitments payable	24,713,736	(8,234,979)
Accrued health care benefits payable	(1,386,235)	922,972
Other liabilities	330,819	(262,340)
	<u>\$ 23,750,809</u>	<u>\$ (7,447,807)</u>
Net increase in working capital	<u>\$ 186,902,144</u>	<u>\$ 179,612,781</u>

See accompanying notes to financial statements.

NOTES TO FINANCIAL STATEMENTS
June 30, 1985 and 1984

(1) Description of the System

(A) Organization - The School Employees Retirement System of Ohio (SERS) was established by the Ohio General Assembly in 1937 to provide retirement benefits to employees of Ohio public schools who are not required to possess a certificate in order to perform their duties. Responsibility for the organization and administration of SERS is vested in the Retirement Board. Employer and employee membership data follow:

Employer Members	June 30,	
	1985	1984
Local.....	376	376
City.....	192	192
County.....	86	87
Village.....	49	49
Vocational.....	49	49
Technical.....	13	13
College.....	2	2
Other.....	1	1
	<u>768</u>	<u>769</u>
Employee Members		
Current retirants and beneficiaries.....	<u>38,708</u>	<u>36,838</u>
Inactive vested members.....	<u>7,597</u>	<u>7,467</u>
Active plan members:		
Vested.....	54,159	51,743
Nonvested.....	<u>32,679</u>	<u>33,018</u>
Total active plan participants.....	<u>86,838</u>	<u>84,761</u>

(B) Benefits - Members are eligible for normal retirement benefits upon reaching age 65 and earning 30 years of service credit. The benefit is equal to 2% of the member's final average salary, as defined, multiplied by the number of years of credited service. Early retirement with reduced benefits is available upon reaching (a) age 55 and 25 years of service credit or (b) age 60 and 5 years of service credit.

In addition to retirement benefits, SERS also provides for disability benefits, survivor benefits, death benefits and health care benefits. Members are eligible for disability benefits after completion of 5 years of eligible service. Qualified dependents of a deceased member are eligible for monthly survivor benefits. Death benefits of \$500 are payable upon the death of a retirant to a designated beneficiary. All members receiving a benefit from SERS are eligible to receive medical insurance. Members who retire after June 1, 1986 must have at least 10 or more years of service credit to qualify for the health care benefits.

Members with credited service in the State Teachers Retirement System (STRS) or Public Employees Retirement System (PERS) are eligible to receive transferred credit

from either or both of those systems. Any service which is not concurrent with service within SERS will be included in the determination of retirement benefits. Similarly, a member with credited service in SERS may transfer such service to STRS or PERS upon retirement.

Upon termination of a member's school employment, the member's accumulated contribution, without interest, is refundable.

(C) Contributions - The Ohio Revised Code requires contributions by active members and their employers. Contribution rates are established by the Retirement Board within the allowable rates established by the Ohio Revised Code. Active members and their employers are required to contribute 8.75% and 14%, respectively, of active member payroll. An Employees' Saving Fund (Account) is established for member contributions. Contributions may be refunded to a member who withdraws from SERS or to the member's beneficiary following the member's death.

(2) Summary of Significant Accounting Policies

The following are the significant accounting policies followed by SERS.

(A) Investments - Income on all investments is recognized on the accrual basis.

Corporate and government bonds and obligations with fixed maturities are reported at cost (as of the trade date) adjusted for amortization of premiums and accretion of discounts.

Investments in residential mortgage-backed securities are carried at the amount of unpaid principal balance of the securities, adjusted for accretion of discounts.

Investments in first mortgage loans are carried at the amount of unpaid principal balance of the loan.

Investments in common stocks are carried at cost. Gains and losses on stock sales are recognized on the basis of the average cost of the stocks sold.

Net option income is earned on premiums received from selling covered call stock options. Premiums received are earned ratably over the term of the option or until the option is exercised, closed, or expired.

Investments in short-term obligations, principally certificates of deposit, commercial paper, U.S. Treasury bills and bank repurchase agreements are carried at cost, which approximates market value.

Investments in real estate are carried at cost. Depreciation on buildings is provided using the straight-line method over the estimated useful lives of the property (40 to 45 years).

(B) Depreciation (Non-Investment) - Depreciation is provided using the straight-line method over the estimated useful lives of the related assets.

(C) Federal Income Tax Status - During the years ended June 30, 1985 and 1984 SERS qualified under the

NOTES TO FINANCIAL STATEMENTS (Continued)
June 30, 1985 and 1984

provision of the Internal Revenue Code and was exempt from Federal income taxes.

(D) Accrued Health Care Benefits Payable - Amounts accrued for health care benefits payable are based upon estimates furnished by the claims administrator. Such estimates have been developed from prior claims experience.

(3) Actuarial Cost Method and Assumptions

Employer contribution rates are determined using the entry age normal actuarial cost method. This method produces an employer contribution rate consisting of (1) an amount for normal cost (the estimated amount necessary to finance benefits earned by employees during the current service year), and (2) the amount for amortization of the unfunded actuarial accrued liability as of June 30, 1985 over 36 years.

The following significant assumptions were used in the actuarial valuations as of June 30, 1985 and 1984: (1) a rate of return on the investments of 7.5% compounded annually; (2) projected salary increases of 4.5%, compounded annually, attributable to inflation; (3) additional projected salary increases ranging from .5% to 3% per year attributable to seniority and merit; (4) post-retirement mortality life expectancies of participants based on the 1955 American Annuity Table set ahead 1 year for men and set back 5 years of women; (5) rates of withdrawal from active

service before retirement for reasons other than death, rates of disability and expected retirement ages developed on the basis of actual plan experience; (6) health care premium increases of 4.5% annually with 25% of eligible retirants electing a joint survivor form of payment and 25% of eligible retirants electing to cover spouses for health care; and (7) eligibility of all health care benefit recipients for Medicare on attainment of age 65, or immediately if retired for disability.

(4) Funding Requirement Determinations and Actual Contributions

Included in employer contributions were \$112,592,000 and \$103,229,000 for 1985 and 1984, respectively, equivalent to 14 percent of active member payroll for 1985 and 1984 of \$804,230,000 and \$737,348,000, respectively. Amounts contributed by employers were in accordance with actuarially computed funding requirement determinations.

The components of employer contributions are as follows: (1) \$50,666,000 and \$46,453,000 (6.3 percent of active member payroll) for normal costs in 1985 and 1984, respectively, and (2) \$61,926,000 and \$56,776,000 (7.7 percent of active member payroll) for amortization of the unfunded actuarial accrued liability in 1985 and 1984, respectively.

(5) Investments

A summary of investments as of each June 30 follows:

	1985		1984	
	Carrying Value	Market Value	Carrying Value	Market Value
Corporate and government bonds and obligations:				
Corporate bonds	\$ 74,661,252	\$ 72,241,271	\$ 102,030,849	\$ 80,087,456
Utility bonds	169,737,107	167,011,577	218,140,982	162,788,324
United States Government and Agency obligations	181,862,785	193,020,218	125,142,359	118,347,977
Canadian Government obligations	8,985,292	8,786,797	9,889,773	8,870,658
	<u>\$ 435,246,436</u>	<u>\$ 441,059,863</u>	<u>\$ 455,203,963</u>	<u>\$ 370,094,415</u>
First mortgage loans:				
GNMA modified pass-through mortgage-backed securities	197,325,440	199,737,808	171,428,594	143,160,754
FHLMC mortgage-backed participation certificates	98,913,409	101,176,498	109,455,487	97,529,578
FHA/VA guaranteed single-family mortgages	539,863	443,805	598,747	412,711
HUD guaranteed mortgages	1,887,513	1,768,748	2,954,659	2,436,912
FHA guaranteed project mortgage	3,509,325	2,228,423	3,573,395	1,733,097
Commercial and industrial mortgages	89,240,709	97,502,763	49,393,882	53,090,982
	<u>\$ 391,416,259</u>	<u>\$ 402,858,045</u>	<u>\$ 337,404,764</u>	<u>\$ 298,364,034</u>
Common Stocks	<u>\$ 389,537,785</u>	<u>\$ 438,176,482</u>	<u>\$ 353,050,885</u>	<u>\$ 364,788,446</u>
Short-term investments:				
Commercial paper	194,792,556	195,262,788	106,287,996	106,790,665
Bankers acceptances	9,195,301	9,210,006	19,761,495	19,840,519
Certificates of deposit	—	—	5,000,000	5,000,000
	<u>\$ 203,987,857</u>	<u>\$ 204,472,794</u>	<u>\$ 131,049,491</u>	<u>\$ 131,631,184</u>
Real estate, land and buildings	101,039,956	121,071,000	101,125,666	118,094,000
Commingled real estate funds	71,079,497	81,453,847	32,002,965	39,773,209
Capital development fund — limited partnership	8,900,000	8,853,324	3,500,000	3,496,875
Total investments	<u>\$ 1,601,207,790</u>	<u>\$ 1,697,945,355</u>	<u>\$ 1,413,337,734</u>	<u>\$ 1,326,242,163</u>

Market values of securities are based primarily on quotations from national security exchanges. Market value of real estate is based upon appraisals. Market values of the commingled real estate funds are based on information provided by the fund managers.