



**STATE OF NEW JERSEY
STATE POLICE RETIREMENT SYSTEM**

Financial Statements and Schedules

June 30, 2009 and 2008

(With Independent Auditors' Report Thereon)



KPMG LLP
Suite 402
301 Carnegie Center
Princeton, NJ 08540-6227

Independent Auditors' Report

The Board of Trustees
State of New Jersey
State Police Retirement System:

We have audited the accompanying statements of fiduciary net assets of the State of New Jersey State Police Retirement System (the System) as of June 30, 2009 and 2008, and the related statements of changes in fiduciary net assets for the years then ended. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control over financial reporting. Accordingly, we express no such opinion. 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 significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the State of New Jersey State Police Retirement System as of June 30, 2009 and 2008, and the changes in its financial position for the years then ended in conformity with U.S. generally accepted accounting principles.

As discussed in note 1 to the financial statements, the System adopted Governmental Accounting Standards Board (GASB) Statement No. 50, *Pension Disclosures* in 2008.

Management's Discussion and Analysis and the supplementary information included in the schedule of funding progress and schedule of employer contributions (schedules 1 and 2) are not a required part of the basic financial statements but are supplementary information required by U.S. generally accepted accounting principles. 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 audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the System's basic financial statements. The 2009 schedule of changes in fiduciary net assets by fund (schedule 3) is presented for purposes of additional analysis and is not a required part of the basic financial statements of the System. Such information has been subjected to the auditing procedures applied in the audit of the 2009 basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the 2009 basic financial statements taken as a whole.

KPMG LLP

February 26, 2010

**STATE OF NEW JERSEY
STATE POLICE RETIREMENT SYSTEM**

Management's Discussion and Analysis

June 30, 2009 and 2008

Our discussion and analysis of the financial performance of the State Police Retirement System (the System) provides an overview of the System's financial activities for the fiscal years ended June 30, 2009 and 2008. Please read it in conjunction with the basic financial statements and financial statement footnotes, which follow this discussion.

Financial Highlights

2009 – 2008

- Net assets held in trust for pension benefits decreased by \$406,897,582 as a result of fiscal year 2009's operations from \$1,967,797,990 to \$1,560,900,408.
- Additions for the year are negative \$274,178,989, which are comprised of member and employer pension contributions of \$24,296,108 and an investment loss of \$298,475,097.
- Deductions for the year are \$132,718,593, which are comprised of benefit and refund payments of \$132,132,908 and administrative expenses of \$585,685.

2008 – 2007

- Net assets held in trust for pension benefits decreased by \$101,462,924 as a result of fiscal year 2008's operations from \$2,069,260,914 to \$1,967,797,990.
- Additions for the year are \$20,703,275, which are comprised of member and employer pension contributions of \$54,813,028 and an investment loss of \$34,109,753.
- Deductions for the year are \$122,166,199, which are comprised of benefit and refund payments of \$121,634,216 and administrative expenses of \$531,983.

The Statements of Fiduciary Net Assets and the Statements of Changes in Fiduciary Net Assets

This annual report consists of two financial statements: *The Statements of Fiduciary Net Assets* and *The Statements of Changes in Fiduciary Net Assets*. These financial statements report information about the System and about its activities to help you assess whether the System, as a whole, has improved or declined as a result of the year's activities. The financial statements were prepared using the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized in the period they are earned, and expenses are recorded in the year they are incurred, regardless of when cash is received or paid.

The Statements of Fiduciary Net Assets show the balances in all of the assets and liabilities of the System at the end of the fiscal year. The difference between assets and liabilities represents the System's fiduciary net assets. Over time, increases or decreases in the System's fiduciary net assets provide one indication of whether the financial health of the System is improving or declining. *The Statements of Changes in Fiduciary Net Assets* show the results of financial operations for the year. The statements provide an explanation for the change in the System's fiduciary net assets since the prior year. These two financial statements should be reviewed along with the information contained in the financial statement footnotes, including the required supplementary schedules, to determine whether the System is becoming financially stronger or weaker.

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Management's Discussion and Analysis

June 30, 2009 and 2008

Financial Analysis

Summary of Fiduciary Net Assets

2009 – 2008

	<u>2009</u>	<u>2008</u>	<u>(Decrease)</u>
Assets	\$ 1,699,692,535	2,295,264,617	(595,572,082)
Liabilities	<u>138,792,127</u>	<u>327,466,627</u>	<u>(188,674,500)</u>
Net assets	<u>\$ 1,560,900,408</u>	<u>1,967,797,990</u>	<u>(406,897,582)</u>

The System's assets primarily consist of investments, securities lending collateral, accrued investment income and members' loans receivable. Between fiscal years 2008 and 2009, total assets decreased by \$595.6 million or 25.9% due to a decrease in the fair value of investments and the securities lending collateral.

Liabilities consist of retirement benefits payable to retirees and beneficiaries, securities lending collateral and rebates payable and, classified under accounts payable and accrued expenses, liabilities of SPRS for unclaimed member accounts and checks issued to members that have not been negotiated by the members but remain due and payable and Non Contributory Group Insurance Benefits (NCGI) payable. Total liabilities decreased by a net \$188.7 million or 57.6% due to a decrease in the securities lending collateral and rebates payable of \$189.5 million and an increase of \$0.8 million in retirement benefits payable and other payables.

Net assets held in trust for pension benefits decreased by \$406.9 million or 20.7%.

Summary of Fiduciary Net Assets

2008 – 2007

	<u>2008</u>	<u>2007</u>	<u>(Decrease)</u>
Assets	\$ 2,295,264,617	2,535,802,779	(240,538,162)
Liabilities	<u>327,466,627</u>	<u>466,541,865</u>	<u>(139,075,238)</u>
Net assets	<u>\$ 1,967,797,990</u>	<u>2,069,260,914</u>	<u>(101,462,924)</u>

The System's assets primarily consist of investments, securities lending collateral, accrued investment income and members' loans receivable. Between fiscal years 2007 and 2008, total assets decreased by \$240.5 million or 9.5% due to a decrease in the fair value of investments and the securities lending collateral.

Liabilities primarily consist of retirement benefits payable to retirees and beneficiaries, securities lending collateral and rebates payable and, classified under accounts payable and accrued expenses, liabilities of SPRS for unclaimed member accounts and checks issued to members that have not been negotiated by the members but remain due and payable. Total liabilities decreased by a net \$139.1 million or 29.8% due to a decrease in the securities lending collateral and rebates payable of \$146.7 million and an increase of \$7.6 million in retirement benefits payable due to full accrual of the July 1, 2008 payroll.

Net assets held in trust for pension benefits decreased by \$101.5 million or 4.9%.

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Summary of Changes to Fiduciary Net Assets

2009 – 2008

	<u>2009</u>	<u>2008</u>	<u>Increase (decrease)</u>
Additions:			
Member contributions	\$ 18,652,049	18,306,246	345,803
Employer contributions	5,644,059	36,506,782	(30,862,723)
Net investment loss	(298,475,097)	(34,109,753)	(264,365,344)
Total additions	<u>(274,178,989)</u>	<u>20,703,275</u>	<u>(294,882,264)</u>
Deductions:			
Benefits	131,974,745	121,438,077	10,536,668
Refunds of contributions	158,163	196,139	(37,976)
Administrative and miscellaneous expenses	585,685	531,983	53,702
Total deductions	<u>132,718,593</u>	<u>122,166,199</u>	<u>10,552,394</u>
Changes in net assets	<u>\$ (406,897,582)</u>	<u>(101,462,924)</u>	<u>(305,434,658)</u>

Additions consist of member and employer contributions and earnings from investment activities. Member contributions increased by \$0.3 million or 1.9% due to normal salary and membership increases.

There was a decrease in employer contributions by \$30.9 million or 84.5%. The State made a contribution of \$3.38 million for fiscal year 2009, which was received in September 2009 after the close of the fiscal year. The amount contributed for fiscal year 2009 is equal to 4.5% of the actuarially determined statutory amount.

Net investment income decreased by \$264.4 million or 775.0% due to depreciation of investments.

The total investment return for all pension funds was estimated to be 14.27% loss compared to 2.66% loss in the prior year.

Deductions are comprised of pension benefit payments to retirees and beneficiaries, refunds of contributions to former members, and administrative costs incurred by the System. Benefit payments increased by \$10.5 million or 8.7% primarily due to more retirees and beneficiaries receiving benefits. The amount of refunds processed decreased by 19.4%. Administrative expenses increased by 10.1%.

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Management's Discussion and Analysis

June 30, 2009 and 2008

Summary of Changes to Fiduciary Net Assets

2008 – 2007

	<u>2008</u>	<u>2007</u>	<u>Increase (decrease)</u>
Additions:			
Member contributions	\$ 18,306,246	17,861,043	445,203
Employer contributions	36,506,782	29,285,276	7,221,506
Net investment income (loss)	(34,109,753)	291,531,439	(325,641,192)
Total additions	<u>20,703,275</u>	<u>338,677,758</u>	<u>(317,974,483)</u>
Deductions:			
Benefits	121,438,077	110,912,899	10,525,178
Refunds of contributions	196,139	176,844	19,295
Administrative and miscellaneous expenses	531,983	531,130	853
Total deductions	<u>122,166,199</u>	<u>111,620,873</u>	<u>10,545,326</u>
Changes in net assets	<u>\$ (101,462,924)</u>	<u>227,056,885</u>	<u>(328,519,809)</u>

Additions consist of member and employer contributions and earnings from investment activities. Member contributions increased by \$0.4 million or 2.5% due to an increase in membership.

There was an increase in employer contributions by \$7.2 million or 24.7%. The State made a contribution of \$34.92 million in fiscal year 2008. The amount contributed in fiscal year 2008 is equal to 45.04% of the actuarially determined amount.

Net investment income decreased by \$325.6 million or 111.7% due to a decrease in the net appreciation in fair value of investments.

The total investment return for all pension funds was estimated to be 2.66% loss compared to 17.1% gain in the prior year.

Deductions are comprised of pension benefit payments to retirees and beneficiaries, refunds of contributions to former members, and administrative costs incurred by the System. Benefit payments increased by \$10.5 million or 9.5% primarily due to more retirees and beneficiaries receiving benefits. The amount of refunds processed increased by 10.9%. Administrative expenses increased slightly.

Retirement System as a Whole

The overall funded ratios are 81.5% for fiscal year 2009 and 83.1% for fiscal year 2008.

Contacting System Financial Management

The financial report is designed to provide our members, beneficiaries, investors and other interested parties with a general overview of the System's finances and to show the System's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact the Division of Pensions and Benefits, P.O. Box 295, Trenton, NJ 08625 – 0295.

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Statements of Fiduciary Net Assets

June 30, 2009 and 2008

Assets	2009	2008
Cash	\$ 426,116	221,398
Securities lending collateral	126,864,795	316,979,452
Investments, at fair value:		
Cash Management Fund	57,312,372	86,633,696
Common Pension Fund A	417,349,016	555,724,322
Common Pension Fund B	590,959,683	528,351,151
Common Pension Fund D	309,144,638	453,379,769
Common Pension Fund E	151,626,857	304,366,616
Mortgages	2,646,327	3,103,415
Total investments	1,529,038,893	1,931,558,969
Receivables:		
Contributions:		
Members	776	1,175,562
Employer	3,886,652	72,876
Accrued interest and dividends	19,663,115	19,013,452
Members' loans	19,745,900	26,187,472
Other	66,288	55,436
Total receivables	43,362,731	46,504,798
Total assets	1,699,692,535	2,295,264,617
Liabilities and Net Assets		
Liabilities:		
Accounts payable and accrued expenses	118,685	94,045
Retirement benefits payable	11,190,533	10,393,130
Securities lending collateral and rebates payable	127,482,909	316,979,452
Total liabilities	138,792,127	327,466,627
Net assets:		
Held in trust for pension benefits	\$ 1,560,900,408	1,967,797,990

See accompanying notes to financial statements.

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Statements of Changes in Fiduciary Net Assets

Years ended June 30, 2009 and 2008

	2009	2008
Additions:		
Contributions:		
Members	\$ 18,652,049	18,306,246
Employers	5,644,059	36,506,782
Total contributions	24,296,108	54,813,028
Investment income:		
Net depreciation in fair value of investments	(349,862,626)	(108,474,420)
Interest	38,560,416	57,172,808
Dividends	12,915,421	17,269,049
	(298,386,789)	(34,032,563)
Less investment expense	88,308	77,190
Net investment loss	(298,475,097)	(34,109,753)
Total additions	(274,178,989)	20,703,275
Deductions:		
Benefits	131,974,745	121,438,077
Refunds of contributions	158,163	196,139
Administrative and miscellaneous expenses	585,685	531,983
Total deductions	132,718,593	122,166,199
Change in net assets	(406,897,582)	(101,462,924)
Net assets – Beginning of year	1,967,797,990	2,069,260,914
Net assets – End of year	\$ 1,560,900,408	1,967,797,990

See accompanying notes to financial statements.

STATE OF NEW JERSEY
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Notes to Financial Statements

June 30, 2009 and 2008

(1) Description of the System

The State of New Jersey State Police Retirement System (the System; SPRS) is a single-employer contributory defined benefit plan which was established as of July 1, 1965, under the provisions of N.J.S.A. 53:5A. The System is included along with other state-administered pension trust and agency funds in the basic financial statements of the State of New Jersey.

The System's designated purpose is to provide retirement, death and disability benefits to its members. Membership in the System is mandatory for all uniformed officers and troopers of the Division of State Police of the State of New Jersey. The System's Board of Trustees is primarily responsible for its administration.

According to State of New Jersey Administrative Code, all obligations of the System will be assumed by the State of New Jersey should the System terminate.

In 2008, the System adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 50, *Pension Disclosures*.

Vesting and Benefit Provisions

The vesting and benefit provisions are set by N.J.S.A. 53:5A. The SPRS provides retirement as well as death and disability benefits. All benefits vest after ten years of service (as defined). Retirement benefits are available after 20 years of service (as defined) at any age with mandatory retirement at age 55. The retirement benefit is based upon final compensation, which is defined as salary (as defined) plus maintenance allowance (as defined) during the last 12 months prior to retirement, and is a life annuity equal to the greater of the following: (a) 50% of final compensation; (b) for members retiring due to mandatory retirement, 50% of final compensation, plus 2% for each year of service in excess of 20 years to a maximum of 60% of final compensation; or (c) for members retiring with 25 or more years of service, 65% of final compensation, plus 1% for each year of service in excess of 25 years, to a maximum of 70% of final compensation. Members may elect deferred retirement after ten years of service in which case benefits in the form of life annuity would begin at age 55 equal to 2% of final compensation for each year of service up to 20 years.

Members are always fully vested for their own contributions.

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Notes to Financial Statements

June 30, 2009 and 2008

Membership and Contributing Employers

Membership in the System consisted of the following at June 30, 2008 and 2007, the dates of the most recent actuarial valuations:

	2008	2007
Retirees and beneficiaries receiving benefits currently and terminated employees entitled to benefits but not yet receiving them	2,520	2,426
Active members:		
Vested	1,809	1,795
Nonvested	1,138	1,204
Total active members	2,947	2,999
Total	5,467	5,425

The State of New Jersey is the only contributing employer of this System.

(2) Summary of Significant Accounting Policies

Measurement Focus and Basis of Accounting

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. The System is accounted for using an economic resources measurement focus.

The accrual basis of accounting is used for measuring financial position and changes in fiduciary net assets of the System. Under this method, revenues are recorded in the accounting period in which they are earned, and deductions are recorded at the time the liabilities are incurred. The financial statements of the System conform to the provisions of Governmental Accounting Standards Board (GASB) Statement No. 25, *Financial Reporting for Defined Benefit Plans and Note Disclosures for Defined Contributions Plans*. Employer contributions are recognized when payable to the System. Benefits and refunds are recognized when due and payable in accordance with the terms of the System.

Investments

The Division of Investment, Department of the Treasury, State of New Jersey (Division of Investment) manages and invests certain assets of seven of the defined benefit plans (PERS, TPAF, JRS, PFRS, CPFPPF, SPRS and POPF). The Division of Investment separately reports the assets, liabilities and net assets of the underlying investment portfolio of the seven defined benefit plans in its Pension Fund report. The Division of Investment accounts included in the Pension Fund report are: Common Fund A, Common Fund B, Common Fund D, Common Fund E, Police and Firemen’s Mortgage Program accounts and other investments owned directly by the seven defined benefit pension plans (the Pension Funds). Common Fund A invests primarily in domestic equity securities. Common Fund B invests primarily in domestic fixed income securities. Common Fund D invests primarily in foreign equity and fixed income securities. Common Fund E invests primarily in alternative investments which includes private equity, real assets and

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Notes to Financial Statements

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absolute return strategy investments. The Police and Firemen's Retirement System includes a mortgage loan program administered by the New Jersey Housing and Mortgage Finance Agency that provides participants with mortgages from the program at rates which are fixed by formula. The law establishing the program provides that the System may not sell the mortgages, and no independent market exists for them.

Investments are reported at fair value as follows:

- U.S. Government and Agency, Foreign and Corporate obligations – prices quoted by a major dealer in such securities.
- Common Stock and Equity Funds, Foreign Equity Securities, Forward Foreign Exchange Contracts – closing prices as reported on the primary market or exchange on which they trade.
- Money Market Instruments – amortized cost which approximates fair value.
- Cash Management Fund – closing bid price on the last day of trading during the period as determined by the Transfer Agent.
- Mortgages – priced by a major dealer in such securities and reviewed by management for reasonableness.
- Alternative investments (private equity, real estate, real asset, and absolute return strategy funds) – estimated fair value provided by the general partner and/or investment manager and reviewed by management. The inputs into the determinations of fair value (particularly for private equity and real estate) require significant management judgment or estimation. Because by their very nature, alternative investments are not always readily marketable, their estimated value is subject to uncertainty and therefore may differ significantly from the value that would be used if a ready market for such investments existed. The development of fair value is further complicated by (1) the current lack of liquidity in the financial system and (2) the extreme levels of volatility in the market for public equity in general and for debt securities linked to these asset classes. For these reasons, the realized value received upon the sale of these investments in the open market might be different than the fair value reported in the financial statements.

Investment transactions are accounted for on a trade or investment date basis. Gains and losses from investment transactions are determined by the average cost method. Interest and dividend income is recorded on the accrual basis, with dividends accruing on the ex-dividend date.

The net asset value of Common Funds A, B, D and E (Common Funds) is determined as of the close of the last day of business of each month. Purchases and redemptions of participants' units are transacted each month within fifteen days subsequent to that time and are recorded at such net asset value.

Dividends and interest earned per unit are calculated monthly and distributed quarterly for Common Fund A and B. Dividends and interest earned per unit are calculated monthly for Common Fund D, and the income earned on Common Fund D units is reinvested. Income earned per unit is calculated monthly for Common Fund E, and the income earned on Common Fund E units is reinvested.

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Securities Lending

The State Investment Council policies permit Common Funds A, B and D and several of the direct pension plan portfolios to participate in securities lending programs, whereby securities are loaned to brokers or other borrowers and, in return, the pension funds have rights to the collateral received. All of the securities held in Common Funds A, B and D, and certain securities held directly by the pension plans, are eligible for the securities lending program. Collateral received may consist of cash, letters of credit, or government securities having a market value equal to or exceeding 102% (U.S. dollar denominated) or 105% (non-U.S. dollar denominated) of the value of the loaned securities at the time the loan is made. For Common Funds A and B, in the event that the market value of the collateral falls below 101% of the market value of all the outstanding loaned securities to an individual borrower, additional collateral shall be transferred by the borrower to the respective funds no later than the close of the next business day so that the market value of such additional collateral, when added to the market value of the other collateral, shall equal 102% of the market value of the loaned securities. For Common Fund D, in the event that the market value of the collateral falls below the collateral requirement of either 102% or 105% (depending on whether the securities are denominated in U.S. dollars or a foreign currency, respectively) of the market value of the outstanding loaned securities to an individual borrower, additional collateral shall be transferred in an amount that will increase the aggregate of the borrower's collateral to meet the collateral requirements. The securities lending contracts do not allow the Common Funds to pledge or sell any collateral securities unless the borrower defaults. As of June 30, 2009 and 2008, the Common Funds have no aggregate credit risk exposure to brokers because the collateral amount held by the Common Funds exceeded the market value of the securities on loan.

The contracts with the Common Funds' securities lending agent require them to indemnify the Common Funds if the brokers or other borrowers fail to return the securities or fail to pay the Common Funds for income distributions on the securities while they are on loan. The Common Fund D securities lending agent also indemnifies the Common Funds for any loss of principal or interest on the invested collateral. For any losses on the investment collateral in Common Funds A or B or other pension plan portfolios, the lending fee paid to the lending agent shall be reduced by 25% of the amount of such loss, up to an amount not to exceed 75% of the previous six months' securities lending fees. The securities loans can be terminated by notification by either the borrower or the Common Funds. The term to maturity of the securities loans is generally matched with the term to maturity of the investment (or, in the case of floating rate notes, to the next interest rate reset date) of the cash collateral.

Derivatives

The Division of Investment, from time to time, utilizes forward foreign currency contracts, a derivative security, as a means to hedge against the currency risk in the Common Funds' foreign equity and fixed income portfolios. Forward foreign currency contracts are agreements to buy or sell a specific amount of a foreign currency at a specified delivery or maturity date for an agreed upon price. A derivative security is an investment whose payoff depends upon the value of other assets such as bond and stock prices, a market index, or commodity prices. Derivative transactions involve, to varying degrees, credit risk and market risk. Credit risk is the possibility that a loss may occur because a party to a transaction fails to perform according to terms. Market risk is the possibility that a change in market prices or currency rates will cause the value of a financial instrument to decrease or become more costly to settle.

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The fair value of foreign forward currency contracts held directly by the Common Funds as of June 30, 2009 and 2008 was as follows:

	<u>2009</u>	<u>2008</u>
Forward currency receivable	\$ 4,865,537,164	1,353,214,830
Forward currency payable	4,739,424,464	1,358,471,309
Net unrealized gain (loss)	126,112,700	(5,256,479)

The Common Funds utilize covered call and put options in an effort to add value to or reduce the risk level in the portfolio. Options are agreements that give the owner of the option the right, but not obligation, to buy (in the case of a call option) or to sell (in the case of a put option) a specific amount of an asset for a specific price (called the strike price) on or before a specified expiration date. The Common Funds enter into covered calls when they write (or sell) call options on underlying stocks held by the Common Funds or stock indices. The Common Funds enter into covered put options when they purchase put options on underlying stocks held by the Common Funds or stock indices. The purchaser of put options pays a premium at the outset of the agreement and stands to gain from an unfavorable change (i.e., a decrease) in the price of the instrument underlying the option. The writer of call options receives a premium at the outset of the agreement and bears the risk of an unfavorable change (i.e., an increase) in the price of the instrument underlying the option. The Common Funds had written call options on 25,737,000 shares, and these options had a fair value of \$10,862,850 as of June 30, 2009. The Common Funds had written call options on 5,661,100 shares with a fair value of \$895,504 as of June 30, 2008. The Common Funds owned 10,295,000 put option contracts on the S&P 500 index with a fair value of \$22,717,250 as of June 30, 2009. The Common Funds owned 880,000 put option contracts on the S&P 500 index with a fair value of \$72,334,000 as of June 30, 2008. Put option contracts are included in investments in the accompanying financial statements.

Certain alternative investment funds and partnerships may use derivative instruments to hedge against market risk and to enhance investment returns. At any point during the year, the Common Funds may have additional exposure to derivatives primarily through limited liability vehicles such as limited partnerships and commingled investment funds. The Common Funds recognize the fair value of all derivative instruments as either an asset or liability in the accompanying financial statements with the offsetting gains or losses recognized in earnings.

Members' Loans

Members who have at least three years of service in the System may borrow up to 50% of their accumulated member contributions. Repayment of loan balances is deducted from payroll checks and bears a commercially reasonable interest rate. Members who retire with an outstanding loan have the option of paying the loan in full prior to receiving any benefits or continuing their monthly loan payment schedule into retirement.

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Under the Internal Revenue Service regulations effective January 1, 2004, the Division changed its pension loan repayment policy: Members who take multiple loans must repay the outstanding balance of the original loan, and all subsequent loans taken before the original loan is completely paid off, within a period not to exceed 5 years from the issuance of the first loan taken after January 1, 2004. Failure to repay the loan within the five-year period will result in the unpaid balance being declared a taxable distribution.

Chapter 92, P.L. 2007 eliminated the 4% fixed rate of interest for loans from the defined benefit plans and provided that the rate of interest will be set by the State Treasurer at a commercially reasonable rate as required by the Internal Revenue Code and permitted that an administrative processing fee may be charged for such loans. As such, effective January 1, 2008, an \$8.00 processing fee per loan was charged, and the new pension loan interest rate became 4.69% per year for year 2008 and 3.33% for year 2009.

Administrative Expenses

The System is administered by the State of New Jersey Division of Pensions and Benefits. Administrative expenses are paid by the System to the State of New Jersey, Department of the Treasury, and are included in the accompanying financial statements.

Miscellaneous expenses and reimbursements from the System that comprise various adjustments to member and employer accounts are incorporated into the administrative expense amounts included in the accompanying financial statements.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of income and expense during the reporting period. Actual results could differ from those estimates.

Funded Status and Funding Progress

The required supplementary information regarding the funded status and funding progress is based on actuarial valuations which involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. These amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the probability of future events.

The required schedule of funding progress presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Actuarial calculations reflect a long-term perspective and are based on the benefits provided under State statutes in effect at the time of each valuation and also consider the pattern of the sharing of costs between the employer and members at that point in time. The projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects of legal or contractual funding limitations on the pattern of cost sharing between the employer and members in the future.

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Actuarial Methods and Assumptions

In the June 30, 2008 and 2007 actuarial valuations, the projected unit credit was used as the actuarial cost method, and the five year average of market value was used as the asset valuation method for the System. The actuarial assumptions included (a) 8.25% for investment rate of return and (b) 5.45% for projected salary increases as of June 30, 2008 and 2007.

	June 30, 2008	June 30, 2007
Actuarial valuation date		
Actuarial value of assets	\$ 2,127,263,509	\$ 2,066,754,160
Actuarial accrued liability	2,609,164,869	2,485,649,230
Unfunded actuarial accrued liability	481,901,360	418,895,070
Funded ratio	81.5%	83.1%
Covered payroll	\$ 281,087,566	\$ 275,301,995
Unfunded actuarial accrued liability as a percentage of covered payroll	171.4%	152.2%
Actuarial cost method	Projected unit credit	Projected unit credit
Asset valuation method	5 year average of market value	5 year average of market value
Amortization method	Level percent, open	Level percent, open
Payroll growth rate for amortization	4.00%	4.00%
Remaining amortization period	30 years	30 years
Actuarial assumptions:		
Interest rate	8.25%	8.25%
Salary range	5.45%	5.45%
Cost-of-living adjustments	1.80%	1.80%

(3) Investments

The System is invested in Common Fund A, Common Fund B, Common Fund D, Common Fund E, and other investments, including mortgage backed securities, which represent 2.51%, 2.73%, 2.49%, 1.88%, and 0.18%, respectively, of each investment total of the Pension Fund as of June 30, 2009.

The System is invested in Common Fund A, Common Fund B, Common Fund D, Common Fund E, and other investments, including mortgage backed securities, which represent 2.29%, 2.52%, 2.53%, 3.01%, and 0.21%, respectively, of each investment total of the Pension Fund as of June 30, 2008.

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The Pension Funds' investments as of June 30 are as follows:

	<u>2009</u>	<u>2008</u>
Domestic equities	\$ 16,372,011,087	23,849,523,038
International equities	11,998,610,775	14,728,747,252
Domestic fixed income	20,694,709,131	20,276,259,245
International fixed income	30,760,749	2,913,035,116
Bank loan funds	1,027,830,211	—
Police and Fireman's mortgages	1,367,881,305	1,288,049,378
Private equity funds	2,982,420,463	2,850,167,142
Real estate funds	1,588,971,807	1,916,228,663
Absolute return strategy funds	2,743,253,999	3,739,013,571
Real asset funds	547,120,061	975,518,400
	<u>\$ 59,353,569,588</u>	<u>72,536,541,805</u>

New Jersey state statute provides for a State Investment Council (Council) and a Director. Investment authority is vested in the Director of the Division of Investment and the role of the Council is to formulate investment policies. The Council issues regulations which establish guidelines for permissible investments which include domestic and international equities and exchange traded funds, covered call and put options, equity futures contracts, obligations of the U.S. Treasury, government agencies, corporations, international governments and agencies, bank loans, interest rate swap transactions, credit default swaps, fixed income exchange traded funds, U.S. Treasury futures contracts, New Jersey State and Municipal general obligations, public authority revenue obligations, collateralized notes and mortgages, commercial paper, certificates of deposit, repurchase agreements, bankers acceptances, guaranteed income contracts, funding agreements, money market funds, private equity funds, real estate funds, other real assets, absolute return strategy funds, and the State of New Jersey Cash Management Fund (CMF). The CMF is a short-term cash fund and is open to state and certain nonstate participants.

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The Pension Funds' investment in the Cash Management Fund is not evidenced by securities that exist in physical or book entry form held by the Pension Funds.

The System's investments are subject to various risks. Among these risks are custodial credit risk, credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. Each one of these risks is discussed in more detail below.

Custodial credit risk, as it relates to investments, is the risk that in the event of a bank failure, the Pension Funds will not be able to recover the value of investments or collateral securities that are in the possession of the third party. The Pension Funds' investment securities are not exposed to custodial credit risk as they are held in segregated trust accounts in the name of the Pension Funds with the custodians.

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The credit risk of issuers and debt instruments is evaluated by nationally recognized statistical rating agencies such as Moody's Investors Service, Inc. (Moody's), Standard & Poor's Corporation (S&P), and Fitch Ratings (Fitch). Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. There are no restrictions in the amount that can be invested in United States treasury and government agency obligations. Council regulations require minimum credit ratings for certain categories of fixed income obligations held directly by the Pension Funds and limit the amount that can be invested in any one issuer or issue.

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Effective July 1, 2008, these limits were as follows:

Category	Minimum rating ⁽¹⁾			Limitation of issuer's outstanding debt	Limitation of issue	Other limitations
	Moody's	S&P	Fitch			
Corporate obligations	Baa3	BBB-	BBB-	10%	25%	Not more than 5% of fund assets can be invested in debt and non-convertible preferred stock of one issuer (3)
International corporate obligations	Baa3	BBB-	BBB-	10%	25%	Not more than 5% of fund assets can be invested in debt and non-convertible preferred stock of any one issuer (2)(3); not more than 10% of fund assets can be invested in this category
International government and agency obligations	Baa3	BBB-	BBB-	25%	Greater of 25% or \$10 million	—
Collateralized notes and mortgages	Baa3	BBB-	BBB-	—	25%	Not more than 5% of fund assets can be invested in any one issue; not more than 10% of fund assets (or 20% of Common Fund B assets) can be invested in this category
Commercial paper	P-1	A-1	F1	—	—	—
Certificates of deposit and Banker's acceptances:						Certificates of deposit and banker's acceptances cannot exceed 10% of issuer's primary capital
Domestic	A3/P-1	A-/A-1	A-/F1	—	—	
International	Aa3/P-1	AA-/A-1	AA-/F1	—	—	
Credit default swap transactions (4)	A1	A+	A+	—	—	Nominal value of net exposure to any one counterparty shall not exceed 10% of fund assets
Guaranteed income contracts and funding agreements	A3	A-	A-	—	—	—
Money market funds	—	—	—	—	—	Not more than 10% of fund assets can be invested in money market funds; limited to 5% of shares or units outstanding

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Category	Minimum rating ⁽¹⁾			Limitation of issuer's outstanding debt	Limitation of issue	Other limitations
	Moody's	S&P	Fitch			
Interest rate swap transactions (5)	A1	A+	A+	—	—	Notional value of net exposure to any one counterparty shall not exceed 10% of fund assets
Repurchase agreements	Aa3	AA-	AA-	—	—	—
NJ state & municipal obligations	A3	A-	A-	10%	10%	Not more than 2% of fund assets can be invested in debt of any one political entity maturing more than 12 months from purchase
Public authority revenue obligations	A3	A-	A-	—	10%	Not more than 2% of fund assets can be invested in any one public authority
Mortgage backed pass-through securities	A3	A-	A-	—	—	Not more than 5% of fund assets can be invested in any one issue
Mortgage backed senior debt securities	—	—	—	—	25%	Not more than 5% of fund assets can be invested in any one issue
Non-convertible preferred stocks of US corporations (4)	Baa3	BBB-	BBB-	10%	25%	Not more than 5% of fund assets can be invested in debt and non-convertible stock of any one corporation
Bank loans (4)	Baa3	BBB-	BBB-	—	—	Not more than 10% of fund assets can be invested in this category

(1) Short term ratings (e.g. P-1, A-1, F1) are used for commercial paper and certificates of deposit.

(2) Prior to December 15, 2008, this restriction only applied to maturities exceeding 12 months.

(3) Prior to December 15, 2008, this restriction applied to debt only.

(4) Effective December 15, 2008.

(5) Prior to December 15, 2008, the minimum rating requirements were A3 (Moody's) and A- (S&P and Fitch).

Effective December 15, 2008, up to 5% of the market value of the combined assets of the pension and annuity funds may be invested in corporate obligations, international corporate obligations, collateralized notes and mortgages, bank loans, non-convertible preferred stock, and mortgage backed pass-through securities that do not meet the minimum credit rating requirements set forth above. Prior to that, the limitation excluded bank loans and non-convertible preferred stock.

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Effective September 5, 2006 through June 30, 2008, the following limits were effective:

Category	Minimum rating ⁽¹⁾			Limitation of issuer's outstanding debt	Limitation of issue	Other limitations
	Moody's	S&P	Fitch			
Corporate obligations	Baa3	BBB-	BBB-	10%	25%	Not more than 5% of fund assets can be invested in one corporation
U.S. finance company debt and bank debentures	Baa3	BBB-	BBB-	10%	25%	Not more than 5% of fund assets can be invested in one corporation
International corporate obligations	Baa3	BBB-	BBB-	10%	25%	Not more than 5% of fund assets can be invested in any one issuer with maturities exceeding 12 months; not more than 10% of fund assets can be invested in this category
International government and agency obligations	Aa3	AA-	AA-	25%	Greater of 25% or \$10 million	Not more than 1% of fund assets can be invested in any one issuer
Collateralized notes and mortgages	Baa3	BBB-	BBB-	—	25%	Not more than 5% of fund assets can be invested in any one issue; not more than 10% of fund assets (or 20% of Fund B assets) can be invested in this category
Commercial paper	P-1	A-1	F1	—	—	—
Certificates of deposit and Banker's acceptances:						Certificates of deposit and banker's acceptances cannot exceed 10% of issuer's primary capital
Domestic	A3/P-1	A-/A-1	A-/F1	—	—	
International	Aa3/P-1	AA-/A-1	AA-/F1	—	—	
Guaranteed income contracts and funding agreements	A3	A-	A-	—	—	—
Money market funds	—	—	—	—	—	Not more than 10% of fund assets can be invested in money market funds; limited to 5% of shares or units outstanding

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Category	Minimum rating ⁽¹⁾			Limitation of issuer's outstanding debt	Limitation of issue	Other limitations
	Moody's	S&P	Fitch			
Interest rate swap transactions	A3	A-	A-	—	—	Notional value of net exposure to any one counterparty shall not exceed 10% of fund assets
Repurchase agreements	Aa3	AA-	AA-	—	—	—
NJ state & municipal obligations	A3	A-	A-	10%	10%	Not more than 10% of fund assets can be invested in debt of any one political entity maturing more than 12 months from purchase
Public authority revenue obligations	A3	A-	A-	—	10%	Not more than 2% of fund assets can be invested in any one public authority
Mortgage backed pass-through securities	A3	A-	A-	—	—	Not more than 5% of fund assets can be invested in any one issue
Mortgage backed senior debt securities	—	—	—	—	25%	Not more than 5% of fund assets can be invested in any one issue

(1) Short term ratings (e.g. P-1, A-1, F-1) are used for commercial paper and certificates of deposit.

Effective August 20, 2007, up to 5% of the market value of the combined assets of the pension and annuity funds may be invested in corporate obligations, finance company debt, bank debentures, international corporate obligations, collateralized notes, and mortgages and mortgage backed pass-through securities that do not meet the minimum credit rating requirements set forth above; prior to that, the limitation was 5% of the market value of Common Fund B.

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For securities in the fixed income portfolio, the following tables disclose aggregate market value, by major credit quality rating category as of June 30, 2009 and 2008. The first table of 2009 is for bonds rated by Moody's. The second table of 2009 uses S&P ratings not rated by Moody's.

(In thousands)	June 30, 2009										
	Moody's rating										
	Aaa	Aa	A	Baa	Ba	B	Bb	C	Ca	Caa	Totals
United States Treasury TIPS	\$ 3,317,891	—	—	—	—	—	—	—	—	—	3,317,891
United States Treasury bonds	2,238,574	—	—	—	—	—	—	—	—	—	2,238,574
United States Treasury strips	664,234	—	—	—	—	—	—	—	—	—	664,234
United States Treasury notes	49,612	—	—	—	—	—	—	—	—	—	49,612
Title XI Merchant Marine notes	1,828	—	—	—	—	—	—	—	—	—	1,828
Government agency obligations	200,236	—	—	—	—	—	—	—	—	—	200,236
Government agency strips	522,265	—	—	—	—	—	—	—	—	—	522,265
Floating rate notes	—	—	11,294	26,825	2,525	6,285	—	—	—	2,450	49,379
Corporate obligations	367,489	1,411,812	4,146,458	3,565,825	230,477	148,640	214	124	20,796	67,577	9,959,412
Convertible bonds	—	—	—	27,289	50	527	—	—	—	801	28,667
Federal farm credit/FHL bank bonds	74,151	—	—	—	—	—	—	—	—	—	74,151
Federal home loan discounted bonds	41,360	—	—	—	—	—	—	—	—	—	41,360
International corporate obligations	—	129,361	705,097	648,390	16,264	28,180	—	569	—	2,615	1,530,476
International bonds and notes	70,745	85,047	—	—	—	—	—	—	—	—	155,792
International floating rate notes	—	—	—	—	—	1,540	—	—	—	—	1,540
Foreign government obligations	29,885	303,592	24,817	—	—	—	—	—	—	—	358,294
Municipal bonds	—	11,131	23,954	1,574	—	—	—	—	—	—	36,659
Remic/FHLMC/FNMA	618,437	—	—	—	—	—	—	—	—	—	618,437
Mortgages/FHLMC/FNMA/GNMA	139,418	—	—	—	—	—	—	—	—	—	139,418
Asset backed obligations	32,499	29,604	98	105,046	—	—	—	—	—	—	167,247
SBA passthrough certificates	170,589	—	—	251	—	238	—	—	—	—	171,078
Private export obligations	24,985	—	—	—	—	—	—	—	—	—	24,985
High yield structured notes	—	—	—	—	—	—	—	—	—	79,076	79,076
	<u>\$ 8,564,198</u>	<u>1,970,547</u>	<u>4,911,718</u>	<u>4,375,200</u>	<u>249,316</u>	<u>185,410</u>	<u>214</u>	<u>693</u>	<u>20,796</u>	<u>152,519</u>	<u>20,430,611</u>

(In thousands)	June 30, 2009								
	Standard & Poor's rating								
	A	AA	B	BB	BBB	CC	CCC	D	Totals
Corporate obligations	\$ 26,627	—	—	—	1,194	1,009	1,803	1,101	31,734
Convertible bonds	—	—	—	1,376	—	—	—	—	1,376
International corporate obligations	—	—	570	923	—	—	—	45	1,538
Asset backed obligations	—	21,181	—	—	—	—	—	—	21,181
	<u>\$ 26,627</u>	<u>21,181</u>	<u>570</u>	<u>2,299</u>	<u>1,194</u>	<u>1,009</u>	<u>1,803</u>	<u>1,146</u>	<u>55,829</u>

The 2009 tables above do not include certain domestic and international corporate obligations including certain exchange traded funds (ETFs) totaling \$239,029,550 which invest in an underlying portfolio of fixed income securities and do not have a Moody's, Standard & Poor's or Fitch rating. The Police and Firemen's Mortgages and the Cash Management fund are unrated.

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(In thousands)	June 30, 2008						
	Moody's rating						
	Aaa	Aa	A	Baa	Ba	B	Caa
United States Treasury TIPS	\$ 3,573,893	—	—	—	—	—	—
United States Treasury bonds	3,914,404	—	—	—	—	—	—
United States Treasury strips	622,327	—	—	—	—	—	—
Title XI merchant marine notes	2,646	—	—	—	—	—	—
United States government agency	78,910	—	—	—	—	—	—
Federal home loan bank notes							
and bonds	120,820	—	—	—	—	—	—
Federal home loan discounted bonds	6,670	—	—	—	—	—	—
Floating rate notes	28,070	—	—	—	—	—	—
Tennessee Valley Authority strips	166,919	—	—	—	—	—	—
Domestic corporate obligations	428,516	674,633	3,024,990	2,642,103	90,580	41,315	84,813
Domestic corporate discounted							
obligations	105,177	—	4,879	—	—	—	—
International corporate obligations	—	—	205,817	193,352	—	—	—
Real estate investment trust							
obligations	—	—	—	19,391	—	—	—
Finance company debt	385,235	476,076	744,296	268,772	—	86,584	64,347
Foreign government obligations	1,077,186	150,700	—	—	—	—	—
Foreign government discount							
obligations	879,287	—	—	—	—	—	—
Adjustable rate municipal bonds	31,000	135,665	135,000	—	—	—	—
International bonds and notes	298,755	20,274	67,775	19,889	—	—	—
Remic/FHLMC	546,377	—	—	—	—	—	—
Remic/FNMA	50,343	—	—	—	—	—	—
SBA pass-through certificates	100,373	—	—	—	—	—	—
GNMA mortgage backed certificates	148,306	—	—	—	—	—	—
FHLM mortgage backed certificates	440,058	—	—	—	—	—	—
FNMA mortgage backed certificates	448,589	—	—	—	—	—	—
Asset backed obligations	63,791	119,057	—	139,267	—	—	—
Private export obligations	85,742	—	—	—	—	—	—
Exchange traded securities	—	—	131,820	—	—	4,700	—
	<u>\$ 13,603,394</u>	<u>1,576,405</u>	<u>4,314,577</u>	<u>3,282,774</u>	<u>90,580</u>	<u>132,599</u>	<u>149,160</u>

The 2008 table does not include certain exchange traded funds (ETFs) totaling \$39,805,000 which invest in an underlying portfolio of fixed income securities and do not have a Moody's rating. The Police and Firemen's Mortgages and the Cash Management fund are unrated.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Commercial paper must mature within 270 days. Certificates of deposits and bankers acceptances are limited to a term of one year or less. Repurchase agreements must mature within 30 days. The investment in guaranteed income contracts and funding agreements is limited to a term of 10 years or less.

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The following tables summarize the maturities (or, in the case of Remics, Police and Firemen's Mortgages and mortgage-backed securities, the expected average life) of the fixed income portfolio as of June 30, 2009 and 2008:

(In thousands)	June 30, 2009				
	Total fair value	Maturities in years			
		Less than 1	1-5	6-10	More than 10
<u>Fixed income investment type</u>					
United States Treasury TIPS	\$ 3,317,891	—	—	—	3,317,891
United States Treasury bonds	2,238,574	—	—	—	2,238,574
United States Treasury strips	664,234	—	—	—	664,234
United States Treasury notes	49,612	—	—	49,612	—
Title XI merchant marine notes	1,828	—	—	—	1,828
Government agency obligations	200,236	—	—	—	200,236
Government agency strips	522,266	—	—	—	522,266
Floating rate notes	49,379	13,216	6,023	3,440	26,700
Corporate obligations	9,991,476	54,324	572,727	3,051,119	6,313,306
Convertible bonds	40,146	50	2,246	1,281	36,569
Federal farm credit/FHL bank bonds	74,151	—	—	74,151	—
Federal home loan discounted bonds	41,360	—	—	—	41,360
International corporate obligations	1,532,266	390	14,444	308,715	1,208,717
International bonds and notes	155,791	—	—	155,791	—
International floating rate notes	11,540	—	10,000	1,540	—
Foreign government obligations	368,205	15,174	24,623	75,192	253,216
Municipal bonds	36,659	—	—	—	36,659
Remic/FHLMC/FNMA	618,437	—	20,344	—	598,093
Police & firemen's obligations	1,367,881	—	—	—	1,367,881
Mortgages/FHLMC/FNMA/GNMA	139,419	—	7,340	4,224	127,855
Asset backed obligations	233,536	—	—	15,284	218,252
SBA passthrough certificates	171,078	—	238	170,840	—
Private export obligations	24,985	—	—	24,985	—
High yield structured notes	79,076	—	79,076	—	—
	<u>\$ 21,930,026</u>	<u>83,154</u>	<u>737,061</u>	<u>3,936,174</u>	<u>17,173,637</u>

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(In thousands)	June 30, 2008				
	Total	Maturities in years			
		market value	Less than 1	1-5	6-10
United States Treasury TIPS	\$ 3,573,893	—	—	369,231	3,204,662
United States Treasury bonds	3,914,404	—	—	—	3,914,404
United States Treasury strips	622,327	—	—	—	622,327
Title XI merchant marine notes	2,646	—	—	—	2,646
United States government agency	78,910	—	—	—	78,910
Federal home loan bank notes and bonds	120,820	—	—	38,492	82,328
Federal home loan discounted bonds	6,670	—	—	—	6,670
Floating rate notes	28,071	—	18,071	10,000	—
Tennessee Valley Authority strips	166,919	—	—	—	166,919
Domestic corporate obligations	6,986,947	4,993	756,272	1,655,983	4,569,699
Domestic corporate discounted obligations	110,056	—	8,234	—	101,822
International corporate obligations	399,169	—	—	69,560	329,609
Real estate investment trust obligations	19,391	—	19,391	—	—
Finance company debt	2,025,311	154,379	183,305	989,819	697,808
Foreign government obligations	1,227,887	70,477	230,400	45,001	882,009
Foreign government discount obligations	879,287	879,287	—	—	—
Adjustable rate municipal bonds	301,665	—	—	—	301,665
International bonds and notes	406,693	—	25,795	196,102	184,796
Remic/FHLMC	546,377	—	—	19,647	526,730
Remic/FNMA	50,343	—	—	—	50,343
SBA pass-through certificates	100,373	—	—	100,373	—
Police and Firemen's mortgages	1,288,049	—	—	—	1,288,049
GNMA mortgage backed certificates	148,306	—	—	—	148,306
FHLM mortgage backed certificates	440,058	6	181	1,820	438,051
FNMA mortgage backed certificates	448,589	339	2,146	11,959	434,145
Asset backed obligations	322,115	—	31,144	14,594	276,377
Private export obligations	85,743	12,547	21,219	51,977	—
	<u>\$ 24,301,019</u>	<u>1,122,028</u>	<u>1,296,158</u>	<u>3,574,558</u>	<u>18,308,275</u>

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The Pension Funds invest in global markets. Effective August 20, 2007, the market value of international preferred and common stocks and issues convertible into common stocks, when combined with the market value of international government and agency obligations, cannot exceed 30% of the market value of the Pension Funds; previously, this limitation was 22%. The market value of emerging market securities cannot exceed more than 1.5 times the percentage derived by dividing the total market capitalization of companies included in the Morgan Stanley Capital International (MSCI) Emerging Market Index by the total market capitalization of the companies included in the MSCI All-Country World Ex-United States Index of the total market value of the assets held by Common Fund D. Not more than 10% of the market value of the emerging market securities can be invested in the common and preferred stock of any one corporation; the total amount of stock purchased of any one corporation cannot exceed 5% of its stock classes eligible to vote. Council regulations permit the Pension Funds to enter into foreign exchange contracts for the purpose of hedging the international portfolio. The Pension Funds held forward contract receivables totaling approximately \$4.9 billion and payables totaling approximately \$4.7 billion

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(with a \$126 million net exposure) as of June 30, 2009. The Pension Funds held forward contracts totaling approximately \$1.4 billion (with a \$5.3 million net exposure) as of June 30, 2008.

The Pension Funds had the following foreign currency exposure as of June 30, 2009 and 2008 (expressed in U.S. dollars and in thousands):

<u>Currency</u>	<u>June 30, 2009</u>			
	<u>Total fair value</u>	<u>Equities</u>	<u>Foreign government/ corporate obligations</u>	<u>Alternative investments</u>
Australian dollar	\$ 656,680	656,680	—	—
Brazilian real	91,406	91,406	—	—
British pound sterling	1,557,089	1,542,240	—	14,849
Canadian dollar	186,979	186,979	—	—
Chilean peso	3,407	3,407	—	—
Czech koruna	7,828	7,828	—	—
Danish krone	186,258	186,258	—	—
Euro	3,706,589	3,484,999	29,885	191,705
Egyptian pound	19,003	19,003	—	—
Hong Kong dollar	457,362	457,362	—	—
Hungarian forint	7,456	7,456	—	—
Indonesian rupiah	31,511	31,511	—	—
Israeli shekel	14,258	14,258	—	—
Japanese yen	1,944,838	1,944,838	—	—
Malaysian ringgit	12,409	12,409	—	—
Mexican peso	9,001	9,001	—	—
Norwegian krone	176,722	176,722	—	—
Pakistan rupee	2,378	2,378	—	—
Philippines peso	711	711	—	—
Polish zolty	7,104	7,104	—	—
Singapore dollar	172,635	172,635	—	—
South African rand	89,543	89,543	—	—
South Korean won	105,001	105,001	—	—
Swedish krona	165,297	164,422	875	—
Swiss franc	879,433	879,433	—	—
New Taiwan dollar	10,823	10,823	—	—
Thailand baht	25,597	25,597	—	—
Turkish lira	39,062	39,062	—	—
	<u>\$ 10,566,380</u>	<u>10,329,066</u>	<u>30,760</u>	<u>206,554</u>

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June 30, 2009 and 2008

June 30, 2008				
Currency	Total market value	Equities	Foreign government obligations	Alternative investments
Australian dollar	\$ 614,583	456,834	157,749	—
Brazilian real	118,301	118,301	—	—
Canadian dollar	546,560	546,560	—	—
Chilean peso	1,286	1,286	—	—
Czech koruna	4,512	4,512	—	—
Danish krone	205,512	205,512	—	—
Euro	6,983,288	5,829,751	1,005,136	148,401
Egyptian pound	20,424	20,424	—	—
Hong Kong dollar	263,291	263,291	—	—
Hungarian forint	6,528	6,528	—	—
Indonesian rupiah	22,783	22,783	—	—
Israeli shekel	14,716	14,716	—	—
Japanese yen	2,822,687	1,943,400	879,287	—
Malaysian ringgit	18,557	18,557	—	—
Mexican peso	19,444	19,444	—	—
New Zealand dollar	18,052	18,052	—	—
Norwegian krone	451,099	451,099	—	—
Omani rial	1,991	1,991	—	—
Pakistan rupee	2,679	2,679	—	—
Philippines peso	1,050	1,050	—	—
Polish peso	9,910	9,910	—	—
Qatar rial	4,497	4,497	—	—
Singapore dollar	135,551	135,551	—	—
South African rand	69,675	69,675	—	—
South Korean won	110,363	110,363	—	—
Swedish krona	521,596	521,596	—	—
Swiss franc	1,460,269	1,460,269	—	—
New Taiwan dollar	13,978	13,978	—	—
Thailand baht	17,001	17,001	—	—
Turkish lira	27,871	27,871	—	—
British pound sterling	1,970,705	1,916,931	—	53,774
	\$ 16,478,759	14,234,412	2,042,172	202,175

The Pension Funds' interests in alternative investments may contain elements of credit, currency and market risk. Such risks include, but are not limited to, limited liquidity, absence of regulatory oversight, dependence upon key individuals, speculative investments (both derivatives and nonmarketable investments), and nondisclosure of portfolio composition. Effective August 18, 2008, Council regulations provide that not more than 28% of the market value of the Pension Funds can be invested in alternative investments, with the individual categories of real estate, real assets, private equity and absolute return strategy investments limited to 7%. Prior to that, the overall limitation was 18%. Not more than 5% of the market value of Common Fund E, plus outstanding commitments, may be committed to any one

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Notes to Financial Statements

June 30, 2009 and 2008

partnership or investment, without the prior written approval of the Council. The investments in Common Fund E cannot comprise more than 20% of any one investment manager's total assets.

(4) Securities Lending Collateral

The System's share in the securities lending program is 2.65% and 2.47% of the total market value of the collateral as of June 30, 2009 and 2008, respectively.

The securities lending collateral is subject to various risks. Among these risks are credit risk, concentration of credit risk, and interest rate risk. Agreements with the lending agents require minimum credit ratings for certain categories of fixed income obligations and limit the amount that can be invested in any one issuer or issue. These limits are consistent with Council regulations and internal policies for funds managed by the Division of Investment.

Effective December 15, 2008, the following limits became effective:

Category	Minimum rating			Limitation of issuer's outstanding debt	Limitation of issue	Other limitations
	Moody's	S&P	Fitch			
Corporate obligations	A2	A	A	10%	25%	—
Collateralized notes and mortgages	Aa	AA	AA	—	25%	Limited to not more than 10% of the assets of the collateral portfolio
Commercial paper	P-1	A-1	F1	—	—	Dollar limits by issuer
Certificates of deposit/ Banker's acceptances:						Certificates of deposit and banker's
Domestic	A2/P-1	A/A-1	A/F1	—	—	acceptances' cannot
International	Aa3/P-1	AA-/A-1	AA-/F1	—	—	exceed 10% of issuer's
						primary capital; dollar
						limits by issuer
Guaranteed income contracts and funding agreements	A2	A	A	—	—	Limited to 5% of the assets of the collateral portfolio
Money market funds	—	—	—	—	—	Limited to 10% of the assets of the collateral portfolio; limited to approved money market funds

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Effective September 5, 2006 through December 14, 2008, the following limits were effective:

<u>Category</u>	<u>Minimum rating</u>			<u>Limitation of issuer's outstanding debt</u>	<u>Limitation of issue</u>	<u>Other limitations</u>
	<u>Moody's</u>	<u>S&P</u>	<u>Fitch</u>			
Corporate obligations	Baa3	BBB-	BBB-	10%	25%	—
U.S. finance company debt and bank debentures	Baa3	BBB-	BBB-	10%	25%	—
Collateralized notes and mortgages	Baa3	BBB-	BBB-	—	25%	Limited to not more than 10% of the assets of the collateral portfolio
Commercial paper	P-1	A-1	F1	—	—	Dollar limits by issuer
Certificates of deposit/ Banker's acceptances:						Certificates of deposit and banker's acceptances' cannot exceed 10% of issuer's primary capital; dollar limits by issuer
Domestic	A3/P-1	A-/A-1	A-/F1	—	—	
International	Aa3/P-1	AA-/A-1	AA-/F1	—	—	
Guaranteed income contracts and funding agreements	A3	A-	A-	—	—	Limited to 5% of the assets of the collateral portfolio
Money market funds	—	—	—	—	—	Limited to 10% of the assets of the collateral portfolio; limited to approved money market funds

Prior to December 15, 2008, all investments in the collateral portfolio matured or were redeemed within one year, except that up to 25% of the portfolio could be invested in eligible securities which matured within 25 months; provided, however, that the average maturity of all investments did not exceed one year. Effective December 15, 2008, all investments in the collateral portfolio must mature or be redeemed within one year.

Commercial paper maturities cannot exceed 270 days. Repurchase agreement maturities cannot exceed 30 days. Certificates of deposit and banker's acceptances must mature in one year or less.

**STATE OF NEW JERSEY
STATE POLICE RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2009 and 2008

The collateral for repurchase agreements is limited to obligations of the U.S. Government or certain U.S. Government agencies, collateralized notes and mortgages and corporate obligations meeting certain minimum rating criteria.

Total exposure to any individual issuer is limited, except for U.S. Treasury and Government agency obligations. For money market funds, the total amount of shares or units purchased or acquired of any money market fund shall not exceed 5% of the shares or units outstanding of said money market fund. For Collateralized notes and mortgages, not more than 2% and 5% of the assets of the collateral portfolio shall be invested in the obligations of any one issuer and issue, respectively. For Guaranteed income contracts and funding agreements, the total investment in any one issuer shall be limited to 2.5% of the collateral portfolio. Prior to December 15, 2008, the Division of Investment set individual issuer limits for Commercial paper and Certificate of deposits; subsequently, the Division of Investment set issuer limits for all investments in the collateral portfolio.

For securities exposed to credit risk in the collateral portfolio, the following tables disclose aggregate market value, by major credit quality rating category as of June 30, 2009 and 2008.

		June 30, 2009							
		Rating							
(In thousands)		Aaa/AAA	Aa/AAA	Aa/AA	a/AA	Aa/A	A/A	A/AA	Not rated
Corporate obligations	\$	—	99,755	642,443	15,001	109,694	759,910	169,039	29,603
Commercial paper		—	—	—	—	—	—	—	199,970
Certificates of deposit		—	—	100,000	—	100,039	—	—	50,000
Guaranteed investment contracts		—	—	100,000	—	—	—	150,000	—
Repurchase agreements		—	—	—	—	—	—	—	1,726,824
Money market funds		151,555	—	—	—	—	—	—	315,697
United States agencies		70,020	—	—	—	—	—	—	—
Cash		—	—	—	—	—	—	—	11
	\$	<u>221,575</u>	<u>99,755</u>	<u>842,443</u>	<u>15,001</u>	<u>209,733</u>	<u>759,910</u>	<u>319,039</u>	<u>2,322,105</u>

At June 30, 2009, all investments in the collateral portfolio will mature in less than one year.

		June 30, 2008									
		Rating									
(In thousands)		Aaa/AAA	Aaa/AA	Aa/AAA	Aa/AA	Aa/A	A/A	AA/A	A/Baa	Baa/BBB	Not rated
Corporate obligations	\$	711,148	269,317	224,455	2,835,773	570,502	1,796,638	9,988	142,151	139,676	—
Commercial paper		—	—	—	—	200,000	—	—	—	—	—
Certificates of deposit		—	—	—	608,740	753,645	—	—	—	—	—
Repurchase agreements		—	—	—	—	—	—	—	—	—	3,110,553
Asset backed securities		431,457	—	—	104,024	—	—	—	—	—	—
Money market funds		507,192	—	—	—	—	—	—	—	—	377,979
Cash		—	—	—	—	—	—	—	—	—	315
	\$	<u>1,649,797</u>	<u>269,317</u>	<u>224,455</u>	<u>3,548,537</u>	<u>1,524,147</u>	<u>1,796,638</u>	<u>9,988</u>	<u>142,151</u>	<u>139,676</u>	<u>3,488,847</u>

At June 30, 2008, if an issuer and/or security have both a long-term and short-term rating, the short-term rating is presented.

STATE OF NEW JERSEY
STATE POLICE RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2009 and 2008

As of June 30, 2009, the Pension Funds had outstanding loaned investment securities with an aggregate fair value of \$4,666,568,972 and received cash collateral with an aggregate fair value of \$4,803,489,627 and noncash collateral of \$13,474,666. As of June 30, 2008, the Pension Funds had outstanding loaned investment securities with an aggregate fair value of \$12,580,839,859 and received cash collateral with an aggregate fair value of \$12,793,553,099 and non-cash collateral of \$70,403,098. In accordance with GASB accounting standards, the noncash collateral is not reflected in the accompanying financial statements. There were no borrower or lending agent default losses, and no recoveries or prior-period losses during the year.

(5) Contributions

The contribution policy is set by N.J.S.A. 53:5A-34 and requires contributions by active members and the State of New Jersey. Plan member and employer contributions may be amended by State of New Jersey legislation. Members contribute at a uniform rate of 7.5% of base salary. Employers are required to contribute at an actuarially determined rate. The annual employer contributions include funding for basic retirement allowances, cost-of-living adjustments and non-contributory death benefits.

The State made a contribution of \$3.38 million, which was received in September 2009 after the close of the fiscal year, excluding the State's contribution of non-contributory group insurance (NCGI) of \$2.20 million and others of \$0.07 million for fiscal year 2009. The State made a contribution of \$34.92 million, excluding the State's contribution of NCGI of \$1.53 million and others of \$0.06 million for fiscal year 2008. The amounts contributed for fiscal years 2009 and 2008 are equal to 4.5% and 45.04% of the actuarially determined statutory amounts, respectively.

(6) Funds

SPRS maintains the following legally required funds as follows:

Members' Annuity Savings Fund (2009 – \$178,485,657; 2008 – \$169,942,630)

The Members' Annuity Savings Fund (ASF) is credited with all contributions made by active members of the System. Member withdrawals are paid out of this Fund.

Contingent Reserve Fund (2009 – \$799,060,766; 2008 – \$1,220,150,489)

The Contingent Reserve Fund is credited with the contributions of the State of New Jersey. Interest earnings, after crediting the Retirement Reserve Fund, as required, are credited to this account. Additionally, payments for life insurance premiums and administrative expenses are made from this Fund.

**STATE OF NEW JERSEY
STATE POLICE RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2009 and 2008

Retirement Reserve Fund (2009 – \$583,353,985; 2008 – \$577,704,871)

The Retirement Reserve Fund is the account from which retirement benefits including cost-of-living adjustments are paid. Upon retirement of a member, accumulated contributions are transferred to the Retirement Reserve Fund from the Members' ASF. Any additional reserves needed to fund the balance of the retirement benefit are transferred from the Contingent Reserve Fund. Annually, interest as determined by the State Treasurer (8.25% for fiscal years 2009 and 2008) is credited to the Retirement Reserve Fund.

Non-Contributory Group Insurance Premium Fund (2009 – \$0; 2008 – \$0)

The Non-Contributory Group Insurance Premium Fund represents the accumulation of employer group insurance contributions in excess of premiums disbursed to the insurance carrier since the inception of the noncontributory death benefit program plus reserves held by the insurance carrier. Members are eligible by statute for the noncontributory group insurance plan in the first year of membership.

(7) Income Tax Status

Based on a May 2007 declaration of an outside tax council retained by the Attorney General of the State of New Jersey, the System complies with the qualification requirements of Section 401(a) of the Internal Revenue Code.

**STATE OF NEW JERSEY
STATE POLICE RETIREMENT SYSTEM**

Required Supplementary Information

Schedule of Funding Progress

(Unaudited - See accompanying independent auditors' report)

Actuarial valuation date	Actuarial value of assets (a)	Actuarial accrued Liability (b)	Unfunded (overfunded) actuarial accrued liability (b - a)	Funded ratio (a / b)	Covered payroll (c)	Unfunded (overfunded) actuarial accrued liability as a percentage of covered payroll ((b - a) / c)
June 30, 1999	\$ 1,600,165,104	1,469,144,146	(131,020,958)	108.9%	\$ 178,203,420	(73.5)%
June 30, 2000	1,752,423,441	1,512,909,805	(239,513,636)	115.8	188,466,237	(127.1)
June 30, 2001	1,829,414,353	1,626,631,656	(202,782,697)	112.5	199,727,203	(101.5)
June 30, 2002	1,853,684,177	1,739,427,739	(114,256,438)	106.6	215,161,126	(53.1)
June 30, 2003	1,865,079,083	1,815,725,256	(49,353,827)	102.7	217,448,864	(22.7)
June 30, 2004	1,897,525,210	1,949,309,641	51,784,431	97.3	223,552,154	23.2
June 30, 2005	1,922,443,732	2,075,266,080	152,822,348	92.6	241,813,372	63.2
June 30, 2006	1,970,398,511	2,319,656,532	349,258,021	84.9	263,220,592	132.7
June 30, 2007	2,066,754,160	2,485,649,230	418,895,070	83.1	275,301,995	152.2
June 30, 2008	2,127,263,509	2,609,164,869	481,901,360	81.5	281,087,566	171.4

**STATE OF NEW JERSEY
STATE POLICE RETIREMENT SYSTEM**

Required Supplementary Information

Schedule of Funding Progress – Additional Actuarial Information

(Unaudited - See accompanying independent auditors' report)

Significant actuarial methods and assumptions used in the most recent 2008 and 2007 actuarial valuations included the following:

	<u>June 30, 2008</u>	<u>June 30, 2007</u>
Actuarial cost method	Projected unit credit	Projected unit credit
Asset valuation method	5 year average of market value	5 year average of market value
Amortization method	Level percent, open	Level percent, open
Payroll growth rate for amortization	4.00%	4.00%
Remaining amortization period	30 years	30 years
Actuarial assumptions:		
Interest rate	8.25%	8.25%
Salary range	5.45%	5.45%
Cost-of-living adjustments	1.80%	1.80%

**STATE OF NEW JERSEY
STATE POLICE RETIREMENT SYSTEM**

Required Supplementary Information

Schedule of Employer Contributions

(Unaudited - See accompanying independent auditors' report)

Year ended June 30	Annual required contribution	Employer contributions⁽¹⁾⁽²⁾	Percentage contributed
1999	\$ 33,116,255	—	—%
2000	33,598,843	—	—
2001	35,341,259	—	—
2002	24,990,652	—	—
2003	29,449,164	—	—
2004	37,600,821	—	—
2005	37,943,519	187,909	0.5
2006	47,196,900	12,941,000	27.4
2007	56,502,006	29,875,748	52.9
2008	78,761,279 ⁽³⁾	36,443,502 ⁽³⁾	46.3
2009	86,385,254	10,244,000	11.9

Notes to schedule:

- (1) Employer contributions exclude contributions received primarily from the Police and Firemen's Retirement System of New Jersey for certain members who transferred their eligible prior service credit to the State Police Retirement System.

In accordance with Chapter 115, P.L. 1997, available excess valuation assets were used to cover, in full or in part, the employer pension contributions from year 1997 to 2004.

- (2) Differences between the amounts in the employer contribution column in this schedule and the amounts recorded in the financial statements and footnotes are attributed to timing differences between the 2008 actuarial valuations and the actual amounts received in fiscal year 2009. Employer contributions per this schedule represent anticipated contribution amounts determined at the time the actuarial valuations were prepared and finalized prior to the end of fiscal year 2009. The financial statements and footnotes reflect the actual amounts received in 2009.
- (3) 2008 annual required contributions and employer contributions have been reduced in accordance with the provisions of the Appropriation Act for fiscal year 2008 for State contributions.

STATE OF NEW JERSEY
STATE POLICE RETIREMENT SYSTEM
 Schedule of Changes in Fiduciary Net Assets by Fund
 Year ended June 30, 2009

	Members' Annuity Savings Fund	Contingent Reserve Fund	Retirement Reserve Fund	Non-Contributory Group Insurance Premium Fund	Total
Additions:					
Contributions:					
Members	\$ 18,652,049	—	—	—	18,652,049
Employers	—	3,447,199	—	2,196,860	5,644,059
Total contributions	18,652,049	3,447,199	—	2,196,860	24,296,108
Distribution of net investment (loss) income	—	(346,135,749)	47,660,652	—	(298,475,097)
Total additions	18,652,049	(342,688,550)	47,660,652	2,196,860	(274,178,989)
Deductions:					
Benefits	—	—	129,777,885	2,196,860	131,974,745
Refunds of contributions	158,163	—	—	—	158,163
Administrative and miscellaneous expenses	—	585,685	—	—	585,685
Total deductions	158,163	585,685	129,777,885	2,196,860	132,718,593
Net increase (decrease) before transfers among reserves	18,493,886	(343,274,235)	(82,117,233)	—	(406,897,582)
Transfers among reserves:					
Retirements	(9,950,859)	(77,815,488)	87,766,347	—	—
Net increase (decrease)	8,543,027	(421,089,723)	5,649,114	—	(406,897,582)
Net assets held in trust for pension benefits:					
Beginning of year	169,942,630	1,220,150,489	577,704,871	—	1,967,797,990
End of year	\$ 178,485,657	799,060,766	583,353,985	—	1,560,900,408