

# **Municipal Fire and Police Retirement System of Iowa**

**MFPRSI  
2836 104th Street  
Des Moines, Iowa 50322**



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# **Introduction**



# ***MUNICIPAL FIRE & POLICE RETIREMENT SYSTEM OF IOWA***

2836 104th Street, Des Moines, IA 50322

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To: Members of the Retirement System,  
City Officials, Elected Officials and Interested Parties

On behalf of the Board of Trustees (the “Board”) of the Municipal Fire and Police Retirement System of Iowa, I am pleased to present the System’s report for the period ending June 30, 2006.

Created by the 1990 General Assembly, the state-wide retirement system was established effective January 1, 1992. Accomplishments of the Board and administration of the System since its inception are summarized on the following pages.

The firm of Deloitte & Touche, LLP, Certified Public Accountants, conducted an audit for the period ending June 30, 2006. A copy of the audit report has been provided to each of the employing cities and is viewable at the System’s office.

The Board and administration appreciate the efforts extended by city officials and the support given to the System by the active and retired membership and by city representatives.

Thank you for your interest.

Sincerely,

Judy Bradshaw, Chairperson  
Board of Trustees





## RETIREMENT SYSTEM'S ACCOMPLISHMENTS

Under the direction of its Board of Trustees (“the Board”), the retirement system has administered the benefit plan in accordance with the statutory requirements mandated by Iowa Code Chapter 411. Specific accomplishments of the consolidated retirement system since its inception (1/1/1992 – 6/30/2006) are described below. Additional information concerning the System’s activities may be obtained by contacting the Executive Director of the System.

### *Summary of Accomplishments*

Transition & Consolidation of Local Systems: Consolidated the assets and the liabilities of eighty-seven local systems into a single state-wide entity.

Program Development & Policy Establishment: Identified needed program areas, effected their creation and established applicable policies. Established an administrative staff and appointed external service providers (actuary, auditor, legal advisor and custodial bank).

Comprehensive Investment Program & Policy : At the initiation of the System in 1991, the Board selected an investment consultant to assist it with the development of the investment program. Subsequent thereto, the Board established a comprehensive investment policy and program in compliance with the governing statute.

Performance of the System’s portfolio since the plan’s inception has been as follows:

Annualized Performance of Fund (1/2/1992 – 6/30/2006):	9.0%
Size of Investment Portfolio, as of 6/30/2006:	\$1,655 million
Size of Investment Portfolio, as of 1/1/92:	\$574.6 million

The Board of Trustees has regularly reviewed the investment policy and program and has made modifications to the individual portfolio requirements and management team to enhance the return on the overall portfolio.

Accounting Requirements: Established compliance with State and national accounting standards (GASB Statements) and with auditor recommendations, including specific staffing recommendations.

Protocol Development: During 1992 – 1994, the System developed and issued initial fire and police medical examination protocols for hiring as required by 1990 legislation.

Disability Program Review: In 1999 the Board undertook a comprehensive examination of the disability provisions provided in the statute. Several recommendations were submitted to and adopted by the General Assembly in the 2000 legislative session. The System implemented each of the requirements established by the statutory changes. The System established the following: a) revised entrance medical examination protocols for the position of police officer and firefighter, b) a wellness guideline for utilization by the employing cities and the membership, and c) a state-wide network of sites for the conduct of the pre-employment medical examinations.

In 2004, the Board undertook a review of the protocols with the assistance of the Medical Board for the purpose of providing clarification of certain requirements. The Board in 2005, revised the protocol documents to enhance their usefulness to the employing cities and for the system's disability program.

Actuarial Assumption Reviews: In accordance with the requirements of the governing statute, the Board in cooperation with the System's actuary, periodically reviews and, as appropriate, modifies the existing assumptions which govern the conduct of the annual valuation of plan assets and liabilities.

Benefit Program: The system's administration has managed the retirement and the disability benefit programs at progressively increasing levels, as reflected on a chart contained within the Statistical Summary Section of this report.

Disability Benefits: Established and executed a systematic disability program, involving detailed requirements for each phase of the process, in compliance with the statute and as upheld by judicial decisions:

Number of disability cases:	684
Accidental disabilities granted:	516
Ordinary disabilities granted:	112
Disability applications denied:	56

The System has experienced a reduced rate of disabilities in comparison to the rate being experienced prior to the consolidation of the local retirement systems. The average number of disabilities has decreased from 55 per year to an average of 43 per year.

Qualification of Plan: The Board obtained the necessary State of Iowa statutory changes and established administrative provisions necessary to obtain a determination letter ("Qualified Plan Status") from the Internal Revenue Service under the Internal Revenue Code.

Pre-taxation of Member Contributions: Through its legislative efforts, the System was able to obtain modification of the necessary statutes to provide for pre-taxation of member contributions for both Federal and State of Iowa taxes. This change has resulted in a substantive reduction in the current year tax liability of each active member in the range of \$250 - \$675 per annum.

Federal & State Court Decisions: The administration maintains compliance with judicial decisions concerning marital property orders, child support orders and tax liens.

Communication Program: The System developed a comprehensive communication program to further the awareness of the membership and the cities concerning the programs of the retirement system. The communication program includes: the conduct of periodic visits to each city, issuance of annual reports, distribution of benefit handbooks and of a periodic newsletter, issuance of flash reports on the activities of the Board, distribution of minutes of the meetings of the Board, and presentations to the periodic meetings of the various associations and at the request of individual cities and membership groups.

Web Site: The System developed and maintains a web site which can be found at [www.mfprsi.org](http://www.mfprsi.org). The site contains information on the benefit plan, necessary forms, statutory and regulatory provisions, plan policies, descriptions of System activities, minutes of meetings and other plan information.

Benefit Program Options: The System established and administers benefit retirement options for possible selection by individuals retiring on service retirement or as a vested retirement.

Program Review & Evaluation: The Board systematically reviews the programs and activities of the System in consideration of the State and Federal statutory requirements, the plan's financial obligations and the adopted mission statement and goals.

Escalator Program: In accordance with a legislative request, the System developed and recommended to the General Assembly, an alternative escalator (cost of living) program to standardize the treatment of the membership and reduce the volatility of the cost associated with escalation. Following legislative enactment, the System implemented the new program on a state-wide basis, effective July 1, 1997. The administration annually performs a statistical assessment of the escalator program and reviews the findings with the Board.

Contribution Program: The System established a standard approach to member and employer contributions and developed automated reporting for the cities. In 2002, the Board adopted quarterly contribution reporting and established electronic contribution reporting.

Current Issues List: The administration periodically evaluates issues and trends affecting public pension plans and reports on issues to the Board and to the Iowa Legislature.

System's Goals: The Board has identified and implemented a mission statement and set of goals for the Board and administration of the System. The Board evaluates the progress toward achievement of the goals at each of its meetings and periodically conducts a systematic review to update the goal statement.

Legislative Study: In response to a directive of the Iowa General Assembly contained in 1998 pension legislation, the System participated with representatives of IPERS and POR in the examination of various subjects concerning the three public retirement systems. The individual associations provided input at several points during the development of the study and commented upon the findings of the report. The report was submitted to a legislative committee in December 1998.

Legislation: Periodically, the Board develops legislative packages concerning technical provisions of the plan, excluding benefit plan enhancements, and submits the proposed changes for consideration of the General Assembly. The administration implements plan changes as established by the General Assembly, including the recommended technical provisions and any benefit plan revisions adopted by the legislature.

Y2K Phenomena: The administration examined the implications of Y2K for the System's operating systems and data, and developed controls and redundant systems in anticipation of any problems created by Y2K. The System's operations were not affected by Y2K.

VEBA: The Board applied to and received the approval of the IRS to establish a Voluntary Employee Beneficiary Association for active members to provide for the members funding of post-retirement healthcare costs. In 2003, the System took steps to establish the VEBA through communication to the membership of the plan. Due to limited participation by the membership, the Board in November 2003 suspended its VEBA efforts.

Direct Deposit Payroll: The System established a direct deposit program for retirees' monthly payments through which the payments are sent directly to the member's financial institution. The program safeguards and assures speedy delivery of payments (93+% participation).

Reciprocity with POR: In response to legislative action, the System established portability with the Peace Officers Retirement System to provide for transfer of credit of service.

Taxation Reporting: The administration maintains compliance with Federal regulations for tax reporting, including the determination of retirees' cost basis recovery and the taxable portion of accidental disability benefits.

Benefit Estimates: The administration has expanded programs to provide an estimate of a member's future retirement benefit and to assist with pre-retirement planning.

Earnings Test & Disability Re-Examinations: In accordance with statutory requirements, the System annually conducts an earnings test program and a re-examination program for individuals retired on disability benefits under the plan

Benefit Payroll Safeguarding: The System administers a program to provide for the secure delivery of benefit payments; including a signature verification program, the review of available obituary reports, and the screening of returned mail.

Selection of Auditor: In 2004, the Board issued a Request for Proposal to select a firm to provide audit services in replacement of the System's prior auditor. The firm selected (Deloitte & Touche) initiated audit services for the fiscal year ending June 30, 2004.

Drop Program: In 2006, the Board, responding to a request from a member of Iowa Senate, completed an analysis of alternative DROP program concepts and submitted a plan design for consideration by the Iowa General Assembly. The plan design was submitted without recommendation by the Board. The Iowa Legislature subsequently adopted DROP legislation which modified Iowa Code Chapter 411. The Board has undertaken steps to implement the plan in accordance with the legislative mandate. The System has submitted a request for a Private Letter Ruling to the Internal Revenue Service. Implementation of the DROP is contingent upon receipt of a favorable letter ruling.

Local Real Estate: The Board in 2006 initiated efforts to invest in local real estate by the construction of a multi-tenant office building, a portion of which will be occupied by the retirement System, for completion in 2007.

## **The Retirement System**

The System was created as a result of action taken by the Iowa General Assembly in 1990 to establish a state-wide retirement system for fire and police personnel covered by the provisions of Iowa Code Chapter 411. Upon its establishment, the System accomplished the consolidation of eighty-seven local fire and police retirement systems formerly administered by forty-nine of Iowa's largest cities.

The Municipal Fire and Police Retirement System of Iowa (the "System") initiated its formal operations on January 1, 1992 to administer the retirement benefits for fire and police personnel in Iowa's largest cities.

The purpose of the System is to provide a sound and secure retirement income for individuals receiving benefits under its programs. The programs of the System include the payment of pension benefits for service retirement, for ordinary and accidental disability retirement, to survivors of deceased members (spouse and dependent benefits), and the payment of contribution refunds upon withdrawal by a terminated member.

The comprehensive disability program includes standards for entrance physical examinations, guidelines for ongoing fitness and wellness, and post-disability retirement compliance requirements.

The System administers a defined benefit plan. The fiscal year for the System is July 1 through June 30.

Permanent, full-time firefighters and police officers in the participating cities are granted membership by Iowa Code Chapter 411. Participants are vested upon attaining four years of membership service under the System.

## Board of Trustees

The activities of the retirement system are under the direction of a Board of Trustees with nine voting members and four non-voting legislative representatives. The voting membership of the Board is comprised of representatives of the active and retired fire and police membership (four), the cities (four), and one private citizen.

Individuals are appointed to the Board by the fire and police associations and by the Iowa League of Cities. The eight voting members select a private citizen to serve as the ninth voting member. The voting membership of the Board, as of June 30, 2005, serving four year terms are identified below:

Judy Bradshaw  
Police Officer – Des Moines  
Current Term Expires April 2009

Marty Pottebaum  
Retired Police Officer – Sioux City  
Current Term Expires April 2007

June Anne Gaeta  
Fire Fighter – Muscatine  
Current Term Expires April 2010

Tom Ryan  
Retired Fire Fighter – Davenport  
Current Term Expires April 2008

Allen McKinley  
Research and Budget Officer –  
Des Moines  
Current Term Expires April 2007

Jody E. Smith  
Director of Administrative Services -  
West Des Moines  
Current Term Expires April 2008

Cindy Kendall  
City Treasurer – Marshalltown  
Current Term Expires April 2009

Duane Pitcher  
Finance Director – Ames  
Current Term Expires April 2010

Mary Bilden  
Citizen Member – Boone  
Current Term Expires April 2010

The legislative members appointed to the Board of Trustees by the leadership of the Iowa Senate and the Iowa House are as follows:

Senator Ron Wieck  
Senator Wally E. Horn

Representative Paul Bell  
Representative Charles Gipp

### *Fiduciary Responsibilities*

Upon appointment to the Board of Trustees, the individual board members have a fiduciary responsibility to the state-wide retirement system.

Statutory responsibilities, as delineated within Iowa Code Chapter 411, include the following:

- a) The Board is responsible for the overall operation and administration of the System and for the establishment of rules which govern the administration of the System.
- b) The Board is to establish the System's budget and to oversee its execution.
- c) The Board is to keep a record of all its proceedings and submit an annual report to the Governor, the General Assembly and the City Council of each of the participating cities.
- d) The Board is to engage necessary actuarial and other services and may employ a staff as necessary to assist it in carrying out its responsibilities.
- e) The Board is responsible for ensuring that proper determinations are made on applications for benefits and that monthly benefits are paid in a timely and accurate manner.
- f) The Board is responsible for establishing the rate of interest to be paid on withdrawn contributions.
- g) The Board is responsible for the management of the fund and the establishment of an investment policy on an annual basis. Funds are to be invested in accordance with that policy.
- h) The Board is to provide for the maintenance of actuarial data for the purpose of valuing the fund and of assessing the experience of the System. The Board is to determine a rate of contribution for the cities based upon an annual actuarial valuation and is to certify the rate to the proper officials of the cities.

To maintain the System's status as a "qualified plan," the Trustees must act in accordance with the "exclusive benefit" provision of the Internal Revenue Code which stipulates that decisions of the System must be made in the best interest of the general membership.

## **The Legislative Mandate**

The programs of the System, its organization, and its authority to act are each provided for by the Code of Iowa. The specific authority for the System's activities is found in Iowa Code Chapter 411.

The authority for the existence and operation of the state-wide system is found in Iowa Code Section 411.35. This section also provided for the termination of the local fire and police retirement systems as of December 31, 1991.

Section 411.36 establishes a Board of Trustees which is responsible for the operation and administration of the state-wide system and which, under Iowa Code Section 411.37, had responsibility for accomplishing the transition to the state-wide system from the terminated local systems.

The administrative activities of the System are provided for by Iowa Code Section 411.5, to include specific authorization for each of the following:

Actuarial Services	Medical Board
Legal Services	Organization and Staff

Various sections of Chapter 411 address the benefit programs of the System, but Iowa Code Section 411.6 provides the primary description of the differing benefits for which the members and beneficiaries are eligible.

### ***CHAPTER 411.6***

- Service retirement benefit
- Allowance on service retirement
- Ordinary disability benefit
- Allowance on ordinary disability benefit
- Accidental disability benefit
- Retirement after accident
- Re-examination of beneficiaries retired on account of disability
- Ordinary death benefit
- Accidental death benefit
- Pensions offset by compensation benefits
- Pension to spouse and children of deceased pensioned members
- Annual re-adjustment of pensions
- Re-marriage of surviving spouse
- Beneficiary designation
- Line of duty death benefit
- Ineligibility for disability benefits
- Limitations on benefits - prisoners
- Optional retirement benefits
- Rollover of members' accounts
- DROP program



## Administration

Under the direction of the Board of Trustees, the programs of the System are developed and executed by an administrative staff, which currently numbers nine individuals. These individuals are available to assist members, city officials, and interested parties with any questions or concerns they may have about the retirement program.

The members of the Administration of the System are identified below:

Dennis L. Jacobs  
Executive Director

Larry Thompson  
Deputy Director

Daniel Cassady  
Accountant/Investment Officer Supervisor

Sally Prince  
Administrative Assistant

James Bybee  
Accountant/Investment Officer

Amy Houston  
Accountant/Investment Officer

Sandra Wells  
Senior Pension Officer

Jill Hagge  
Senior Pension Officer

Janice Bell  
Senior Pension Officer

The offices of the System are located at:

MFPRSI  
2836 104<sup>th</sup> Street  
Des Moines, IA 50322

The System may be contacted at the following numbers:

Local phone: (515) 254-9200

Toll free phone: (888) 254-9200

Fax number: (515) 254-9300

E-mail address: [pensions@mfprsi.org](mailto:pensions@mfprsi.org)

Web Site [www.mfprsi.org](http://www.mfprsi.org)

The offices of the System are open for operation from 8:00 a.m. to 4:30 p.m., Monday through Friday, excluding recognized national holidays.



# **Financial Report**



## **Management's Discussion and Analysis**

The following discussion and analysis of the Municipal Fire and Police Retirement System of Iowa's (System) financial performance provides an overview of the System's financial activities for the fiscal years ended June 30, 2006 and 2005. Please read in conjunction with the basic financial statements, which follow this discussion. These statements represent the current condition from an accounting perspective, but do not reflect the System's actuarial status. Refer to the System's actuarial valuation for the System's funding status regarding long term benefit obligations.

### **FINANCIAL HIGHLIGHTS**

- System assets exceeded its liabilities at the close of the fiscal years 2006 and 2005 by \$1,658,428,273 and \$1,469,753,955 (reported as plan net assets), respectively. Net assets are held in trust to meet future benefit payments.
- Additions for the year ended June 30, 2006 were \$277,422,113, which is comprised of contributions of \$77,349,656, net investment income of \$200,059,824, service credit actuarial adjustments of \$8,918 and other income of \$3,715. Additions for the year ended June 30, 2005 were \$229,305,254, which is comprised of contributions of \$68,135,238, net investment income of \$161,161,757 and other income of \$8,259.
- Benefit payments were \$86,196,920 and \$80,930,453 for the years ended June 30, 2006 and 2005, respectively, a 6.5% increase from year to year.

### **THE STATEMENTS OF PLAN NET ASSETS AND THE STATEMENTS OF CHANGES IN PLAN NET ASSETS**

This Annual Financial Report consists of two financial statements; The Statements of Plan Net Assets and The Statements of Changes in Plan Net Assets. These financial statements report information about the System, as a whole, and financial condition that should help answer the question: Is the System, as a whole, better off or worse off as a result of this fiscal year's experience? These statements include all assets and liabilities using the accrual basis of accounting. Under the accrual basis of accounting, all revenue and expenses are taken into account regardless of when cash is received or paid.

The Statements of Plan Net Assets present all of the System's assets and liabilities, with the difference between assets and liabilities reported as plan net assets. Over time, increases and decreases in plan net assets is one way to measure whether the System's financial position is improving or deteriorating. The Statements of Changes in Plan Net Assets present the change in plan net assets during the fiscal year.

## FINANCIAL ANALYSIS

System assets as of June 30, 2006 and 2005 were approximately \$1.76 billion and \$1.66 billion, respectively, and were primarily comprised of investments, cash, receivables from brokers, and contributions due from employers. The \$99,173,338, or 6.0%, increase in assets from June 30, 2005 to June 30, 2006 was primarily due to investment earnings and contributions.

Total liabilities as of June 30, 2006 and 2005 were \$102,725,395 and \$192,226,375, respectively, and were primarily comprised of payables for unsettled trades and obligations under securities lending. The \$89,500,980, or 46.6%, decrease in liabilities from June 30, 2005 to June 30, 2006 was primarily due to a decrease in payables from the purchase of investments and a decrease in payables for securities lending.

System assets exceeded liabilities at the close of fiscal year 2006 by \$1,658,428,273. During the year ending June 30, 2006 plan net assets held in trust for pension benefits increased \$188,674,318, or 12.8%, from the previous fiscal year, primarily due to investment earnings and contributions. This is in comparison to the previous fiscal year, when net assets increased by \$146,062,431, or 11.0%, from the prior year.

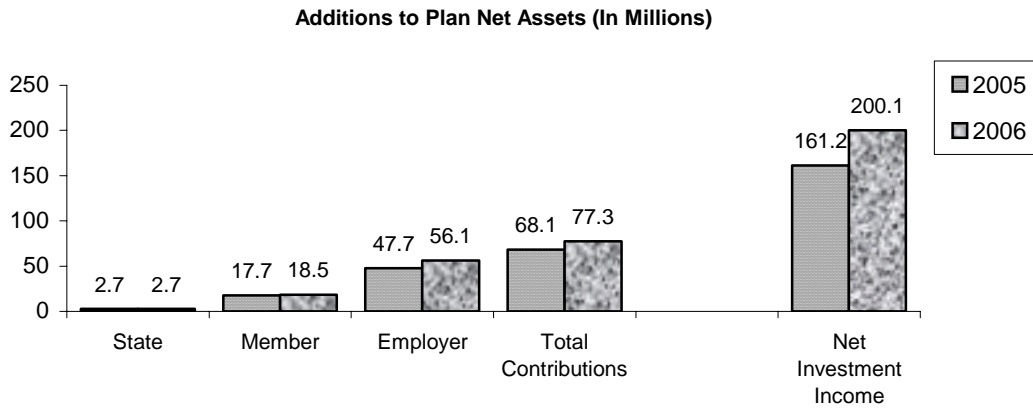
### Municipal Fire and Police Retirement System of Iowa Condensed Statements of Plan Net Assets (In Thousands)

	2006	2005	Total Percentage Change	
<b>Assets:</b>				
Cash	\$ 611	\$ 1,560	(60.8)	%
Investments	1,715,235	1,580,621	8.5	%
Receivables	45,156	79,565	(43.2)	%
Fixed assets	108	165	(34.5)	%
Other assets	43	69	(37.7)	%
Total Assets	1,761,153	1,661,980	6.0	%
<b>Liabilities:</b>				
Benefits and refunds payable	41	14	192.9	%
Investment management expenses payable	2,132	1,474	44.6	%
Administrative expenses payable	341	430	(20.7)	%
Payable for securities lending	45,873	112,315	(59.2)	%
Payable to brokers for unsettled trades	54,338	77,993	(30.3)	%
Total Liabilities	102,725	192,226	(46.6)	%
Plan Net Assets	\$ 1,658,428	\$ 1,469,754	12.8	%

## REVENUES – ADDITIONS TO PLAN NET ASSETS

Reserves needed to finance retirement benefits are accumulated through the collection of contributions and earnings on investments. Contributions and net investment income (losses) for the fiscal year 2006 totaled \$277,409,480.

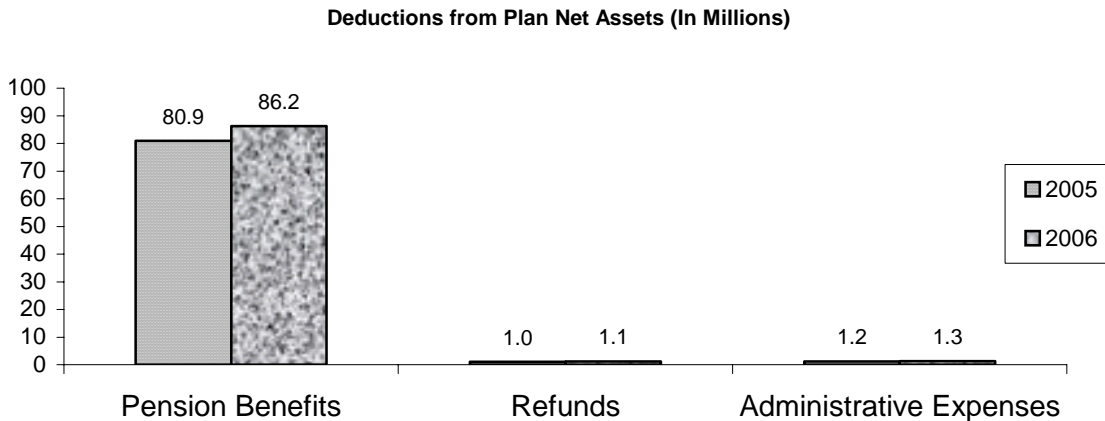
Contributions increased from the previous year by \$9,214,418. This increase is primarily due to an increase in the employer contribution rate and increases in active members' earnable compensation. Net investment income increased from the previous year by \$38,898,067. This change is primarily due to a larger increase in the net appreciation in fair value of investments than the previous year.



## EXPENSES – DEDUCTIONS FROM PLAN NET ASSETS

The principal expenses of the System include the payment of pension benefits to retired members and beneficiaries, refund of contributions to former members, and the cost of administering the System. Total deductions for the fiscal year 2006 were \$88,747,795, an increase of 6.6% over fiscal year 2005 deductions.

Pension benefit payments increased by \$5,266,467, or 6.5%, from the previous year. Refund of contributions increased by \$131,038, or 13.0%.



## **RETIREMENT SYSTEM AS A WHOLE**

It is important to note the financial obligations established by the Iowa legislature in Iowa Code Chapter 411 are committed benefits, which are to be funded through the contributions made by the employers and the membership, in concert with the long-term return on investments. The “public policy” within Iowa has always been to meet the benefit commitments of the pension plans. The history of the plan benefits under Chapter 411 traces to 1934. The funding methods established by the legislature in the Iowa Code, whereby contributions are made from the individual employers and members, coupled with the “prudent person” concept for investment policy, provides the financial foundation for this public policy.

## **CONTACTING THE SYSTEM**

This financial report is designed to provide the System’s Board of Trustees, membership, and cities a general overview of the System’s finances and to demonstrate accountability for assets. If you have any questions about this or need additional financial information, contact the System’s office, 2836 104th Street, Des Moines, IA 50322.



# MUNICIPAL FIRE AND POLICE RETIREMENT SYSTEM OF IOWA

## Statements of Plan Net Assets

June 30, 2006 and 2005

	2006	2005
<b>ASSETS</b>		
Cash	\$ 611,316	\$ 1,560,474
Investments, at fair value:		
U.S. government obligations	27,606,233	63,660,614
U.S. corporate fixed income	111,940,443	99,571,070
U.S. equity securities	446,461,867	447,636,309
Foreign government obligations	5,365,841	3,329,407
Foreign corporate fixed income	7,873,257	5,818,952
Foreign equity securities	494,204,381	413,046,743
Commingled fixed income	123,418,111	160,350,931
Short-term investments and currency positions	119,293,849	120,578,383
Securities lending short-term collateral investment pool	45,873,289	112,315,472
Real estate	184,059,542	117,377,564
Private equity	74,072,649	36,935,162
Multi-strategy commingled fund	75,065,914	0
Total investments, at fair value	<u>1,715,235,376</u>	<u>1,580,620,607</u>
Receivables:		
Contributions	3,804,950	2,370,859
Investment income	2,171,174	2,619,477
Receivable from brokers for unsettled trades, net	39,180,249	74,574,764
Total receivables	<u>45,156,373</u>	<u>79,565,100</u>
Fixed assets (net of accumulated depreciation of \$236,429 and \$184,803 in 2006 and 2005, respectively)	107,953	164,725
Other assets	42,650	69,424
Total assets	<u>1,761,153,668</u>	<u>1,661,980,330</u>
<b>LIABILITIES</b>		
Benefits and refunds payable	40,915	14,081
Investment management expenses payable	2,132,226	1,474,314
Administrative expenses payable	340,971	429,836
Payable for securities lending	45,873,289	112,315,472
Payable to brokers for unsettled trades, net	54,337,994	77,992,672
Total liabilities	<u>102,725,395</u>	<u>192,226,375</u>
Plan net assets held in trust for pension benefits	<u>\$1,658,428,273</u>	<u>\$1,469,753,955</u>
See notes to financial statements.		

**MUNICIPAL FIRE AND POLICE RETIREMENT SYSTEM OF IOWA**

**Statements of Changes in Plan Net Assets**

**Years Ended June 30, 2006 and 2005**

	<b>2006</b>	<b>2005</b>
Additions:		
Contributions:		
Member	\$ 18,525,032	\$ 17,672,155
Employer	56,078,840	47,717,299
State appropriations	<u>2,745,784</u>	<u>2,745,784</u>
Total contributions	<u>77,349,656</u>	<u>68,135,238</u>
Investment income:		
Interest	11,551,580	9,906,044
Dividends	18,169,047	11,386,028
Securities lending	3,984,152	2,399,118
Net appreciation in fair value of investments	<u>178,891,533</u>	<u>146,446,519</u>
Total investment income	212,596,312	170,137,709
Less investment expenses:		
Securities lending	3,701,170	2,124,290
Management fees and other	<u>8,835,318</u>	<u>6,851,662</u>
Net investment income	<u>200,059,824</u>	<u>161,161,757</u>
Service credit actuarial adjustments	8,918	0
Other income	<u>3,715</u>	<u>8,259</u>
Total additions	<u>277,422,113</u>	<u>229,305,254</u>
 Deductions:		
Benefit payments	86,196,920	80,930,453
Refund payments	1,137,028	1,005,990
Administrative expenses	1,259,950	1,210,123
Disability expenses	81,593	84,466
Other	<u>72,304</u>	<u>11,791</u>
Total deductions	<u>88,747,795</u>	<u>83,242,823</u>
Net increase	188,674,318	146,062,431
 Plan net assets held in trust for pension benefits:		
Beginning of year	<u>1,469,753,955</u>	<u>1,323,691,524</u>
End of year	<u>\$1,658,428,273</u>	<u>\$1,469,753,955</u>

See notes to financial statements.

## NOTES TO FINANCIAL STATEMENTS YEARS ENDED JUNE 30, 2006 AND 2005

### 1. PLAN DESCRIPTION

#### **General**

The Municipal Fire and Police Retirement System of Iowa (System) was created under Chapter 411.35 of the Code of Iowa to replace 87 separate fire and police retirement systems from 49 cities and 1 county in Iowa (Separate Systems). Effective January 1, 1992, the Separate Systems were terminated, and the respective entities were required to transfer assets to the System equal to their respective accrued liabilities (as measured by the System's actuary). Upon transfer of the assets, the System assumed all membership, benefits rights and financial obligations of the Separate Systems.

The System is the administrator of a multi-employer, cost sharing, defined benefit pension plan for the exclusive benefit of eligible employees of participating cities (substantially all full-time employees of the respective cities' fire and police departments). It is governed by a nine-member Board of Trustees (Board) who are appointed to the Board by police and fire associations and by the Iowa League of Cities. The eight voting members select a private citizen to serve as the ninth voting member. The Board is authorized by the state legislature to make investments, pay benefits, set contributions rates, hire staff and consultants and perform all necessary functions to carry out the provisions of the Code of Iowa. The System is separate and apart from state government and is not included in the state's financial statements.

At June 30, 2006, the System was comprised of 49 cities covering 3,816 active members; 286 terminated members entitled to benefits; and 3,531 retired firefighters, police officers, bailiffs, and eligible beneficiaries across Iowa.

#### **Funding**

*Member* - Member contribution rates are set by state statute. In accordance with House File 2418, Act of the 1994 General Assembly, to establish compliance with the Federal Older Workers Benefit Protections Act, the contribution rate was 9.35% of earnable compensation for the years ended June 30, 2006 and 2005.

*Employer* - Employer contribution rates are based upon an actuarially determined normal contribution rate and set by state statute. The required actuarially determined contributions are calculated on the basis of the aggregate actuarial cost method set forth in Chapter 411 of the Code of Iowa. The normal contribution rate is provided by state statute to be the actuarial liabilities of the plan less current plan assets, with such total divided by 1 percent of the actuarially determined present value of prospective future compensation of all members, further reduced by member contributions and state appropriations. Under the Code of Iowa the employer's contribution rate cannot be less than 17% of earnable compensation. The contribution rate was 28.21% and 24.92% for the years ended June 30, 2006 and 2005, respectively.

*State Appropriations* – State appropriations are approved by the state legislature and may further reduce the employer’s contribution rate, but not below the minimum statutory contribution rate of 17.00% of earnable compensation.

## **Benefits**

Participating members are entitled to the benefit provisions in effect on the member’s date of termination. The following is a summary of the System benefit provisions as of June 30, 2006 and 2005:

*Retirement* - Members with 4 or more years of service are entitled to pension benefits beginning at age 55. Full service retirement benefits are granted to members with 22 years of service, while partial benefits are available to those members with 4 to 22 years of service based on the ratio of years completed to years required (22 years). Members with less than 4 years of service are entitled to a refund of their contribution only, with interest for the period of employment.

Benefits are calculated based upon the member’s highest 3 years of compensation. The average of these 3 years becomes the member’s average final compensation. The base benefit is 66 percent of the member’s average final compensation. Additional benefits are available to members who perform more than 22 years of service (2 percent for each additional year of service, up to a maximum of 8 years). Survivor benefits are available to the beneficiary of a retired member according to the provisions of the benefit option chosen plus an additional benefit for each child. Survivor benefits are subject to a minimum benefit for those members who chose the basic benefit with a 50 percent surviving spouse benefit.

*Disability and Death* - Disability coverage is broken down into two types, accidental and ordinary. Accidental disability is defined as permanent disability incurred in the line of duty, with benefits equivalent to the greater of 60 percent of the member’s average final compensation or the member’s service retirement benefit calculation amount. Ordinary disability occurs outside the call of duty and pays benefits equivalent to the greater of 50 percent of the member’s average final compensation, for those with 5 or more years of service, or the member’s service retirement benefit calculation amount, and 25 percent of average final compensation for those with less than 5 years of service.

Death benefits are similar to disability benefits. Benefits for accidental death are 50 percent of the average final compensation of the member plus an additional amount for each child, or the provisions for ordinary death. Ordinary death benefits consist of a pension equal to 40 percent of the average final compensation of the member plus an additional amount for each child, or a lump-sum distribution to the designated beneficiary equal to 50 percent of the previous year’s earnable compensation of the member or equal to the amount of the member’s total contributions plus interest.

Benefits are increased (escalated) annually in accordance with Iowa Code Chapter 411.6 which states a standard formula for the increases.

*Traumatic Personal Injury* - The surviving spouse or dependents of an active member who dies due to a traumatic personal injury incurred in the line of duty receives a \$100,000 lump-sum payment.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

***Basis of Presentation*** -The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. The System has elected to apply only applicable Financial Accounting Standards Board (FASB) Statements and interpretations issued on or before November 30, 1989, that do not contradict Governmental Accounting Standards Board (GASB) pronouncements.

The System prepared its financial statements using the accrual basis of accounting. It recognizes member and employer contributions as revenues in the month member earnings are paid. Benefits and refunds are recognized as expenses when payable. Expenses are recorded when the corresponding liabilities are incurred, regardless of when payment is made.

***New Accounting Pronouncements*** – The System has adopted GASB Statement No. 44 (GASB 44), *Economic Condition Reporting: The Statistical Section*. GASB 44 requires the System to add an additional year of history to the statistical table entitled ‘Schedule of Contributions from the Employers and Other Contributing Entities’ each year until a total of 10 years of history is disclosed. Adoption of this pronouncement had no impact on the operations or financial position of the System.

***Use of Estimates*** - The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts in the financial statements. Actual results could differ from those estimates.

***Investments*** - The System’s securities are reported at fair value. Where appropriate, the fair value includes estimated disposition costs. Interest income is recognized when earned. Dividend income is recognized on the ex-dividend date. Gains or losses on stocks and bonds are recognized on an average cost basis calculated separately for each investment manager. Other gains and losses are recognized on an identified cost basis. Gains and losses on sales and exchanges are recognized on the trade date. The fair values of securities held at June 30 are determined by using the closing price listed on national securities exchanges and quoted market prices provided by independent pricing services. For commingled funds, the net asset value is determined and certified by the commingled fund manager. Investments in real estate, private equities, and multi-strategy commingled fund which invest in both publicly and privately owned securities are valued based on estimates and assumptions of general partners, partnership valuation committees, or third party appraisal firms, in the absence of readily determined market values. Such valuations generally reflect discounts for illiquidity and consider variables

such as financial performance of investments, recent sales prices of investments, and other pertinent information.

**Fixed Assets** - Fixed assets are stated at cost, net of accumulated depreciation. Depreciation is recognized on a straight-line basis over estimated useful lives of three to ten years.

**Income Taxes** – The System has a tax determination letter from the Internal Revenue Service stating that it qualifies under the provision of Section 401 of the Internal Revenue Code and is exempt from federal and state income taxes.

### 3. CASH

For cash deposits, custodial credit risk is the risk that in the event of a bank failure, the System’s deposits may not be returned. The table below presents a summary of cash balances of the System at June 30, 2006 and 2005:

	2006	2005
Bank balance at June 30:		
Insured	\$ 100,000	\$ 100,000
Uninsured and uncollateralized	511,316	1,460,474
Carrying amount at June 30	<u>\$ 611,316</u>	<u>\$ 1,560,474</u>

### 4. INVESTMENTS

#### *Investment Policy*

The investment authority, as prescribed by the Code of Iowa, is governed by the “prudent person rule.” This rule requires that an investment be made with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an entity of a like character with like aims. Within the “prudent person” framework, the Board has adopted investment guidelines for the System’s investment program.

The following investment vehicles are permitted by the System’s investment policy and may be considered for the System’s funds:

#### **Stocks and Bonds (Domestic, International & Emerging Markets)**

- Securities issued by and the obligations of or guaranteed by the United States of America or U.S. government sponsored enterprises or by the Dominion of Canada or any province thereof, financial futures and options;
- Bonds issued by the State of Iowa or its political subdivisions;

- Common stock, American Depository Receipts, corporate bonds or other evidences of indebtedness issued under the laws of the Dominion of Canada or any province thereof;
- Common stock, bonds or other evidences of indebtedness issued under the laws of selected foreign countries or their political subdivisions;
- Debt instruments issued by multinational organizations, on behalf of selected nations or groups of nations, such as Brady Bonds, whether in U.S. dollars or foreign currencies;
- Mutual funds, commingled funds, or private equity which are, comprised of stocks, equity and or debt instruments, including those which hold positions in emerging markets, whether in U.S. dollars or foreign currencies;
- Derivative instruments, such as futures and options, can by utilized as an alternative to a stock or bond position, as specified.

### **Other Asset Classes**

The currency positions of the System include the currency of a group of selected nations, which have well established and stable economic and political structures. Currency positions are only taken in countries or in multinational currencies (for examples, Euros) in which the System has determined to invest the System's assets. The currency assets of the System are represented within the individual portfolios of the investment managers, which have mandates, which include international bonds or stocks. The benchmark against which these managers run the portfolios shall include a zero percent hedged position to the U. S. dollar for the international portions of the mandate.

### **Derivative Instruments**

Derivative instruments, such as futures and options, may be utilized in selected portfolios for the following purposes:

- 1) As an alternative to maintaining a selected asset position,
  - 2) To maintain the duration of securities in a portfolio,
  - 3) To gain exposure in a time of dollar strength to a foreign bond market with minimal exposure to the currency of the country,
  - 4) To hedge or otherwise protect existing or anticipated portfolio positions,
  - 5) To establish and maintain the currency positions for the currency overlay portfolio and for the individual currency activities of the individual portfolios, and
  - 6) Not to speculate or leverage (gear-up) the portfolio.
- Derivative instruments are generally defined as contracts whose value depends on ("derives" from) the value of an underlying asset, reference rate, or index. Derivative instruments include both of the following:

- a) "Over the counter" (OTC) derivatives: privately negotiated contracts provided directly by dealers to end-users; which include swaps, futures and options, based upon interest rates, currencies, equities, and commodities; and
- b) Standardized contracts sold on exchanges: futures and options.

**Real Estate**

The real estate positions of the System may include domestic or international real estate investments in individual properties or groups of properties, through one or more of the following: direct purchase or mortgage of individual properties, participation in a commingled fund (open-ended or closed-ended) or in a trust or a partnership, which has positions in one or more properties.

The real estate positions of the System may include investment in securitized real estate, via publicly traded or privately held Real Estate Investments Trusts (REITS).

**Investment Risk Disclosure**

**Credit Risk**

The quality ratings of investments in fixed income securities as described by nationally recognized statistical rating organizations as of June 30, 2006 are as follows:

Quality Rating	Fair Value	Percentage of Portfolio
AAA	\$ 148,542,692	53.79 %
AA	71,728,772	25.97 %
A	10,805,982	3.91 %
BBB	7,016,670	2.54 %
BB	8,283,337	3.00 %
B	867,638	0.31 %
Unrated	1,352,561	0.49 %
Total credit risk debt securities	248,597,652	90.01 %
U.S. Government Fixed Income Securities*	27,606,233	9.99 %
Total fixed income securities	\$ 276,203,885	100.00 %

\* Obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk.

The System does not have a formal policy that limits the quality grade in which the System may invest.



### **Custodial Credit Risk**

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the pension fund will not be able to recover the value or collateral securities that are in the possession of an outside party. Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the System, and are held by either the counterparty or the counterparty's trust department or agent but not in the System's name.

Iowa Code 411.7 establishes the secretary of the Board as the custodian of the fund and provides for the System to select master custodian banks to provide custody of the System's assets. The System has arranged for Mellon Trust of New England, N.A. to act as the master custodian bank. The master custodian bank may hold System property in the name of its nominee, bearer form, or in book entry form, so long as the Custodian's records clearly indicate that such property is held as part of the System's account.

### **Concentration of Credit Risk**

The System is guided by statute and policy in the selection of security investments. No investments in any one organization represent 5% or more of plan assets.

### **Interest Rate Risk**

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of the investment.

	<b>Fair Value</b>	<b>Duration</b>
Investment Type:		
Short-term	\$ 119,293,849	0.0802
Fixed income	152,785,774	4.2706
Commingled	<u>123,418,111</u>	<u>4.0811</u>
Total fair value	<u>\$ 395,497,734</u>	
Portfolio modified duration		<u>2.9475</u>

Duration is a measure of interest rate risk. The greater the duration of a bond, or portfolio of bonds, the greater its price volatility will be in response to a change in interest rates and vice-versa. Duration is the measure of a bond price's sensitivity to a 100-basis point change in interest rates. Duration of eight would mean that, given a 100-basis point change up/down in rates, a bond's price would move up/down by 8%.

## Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The System had exposure to foreign currency fluctuations as follows:

	<b>Fair Value</b>	<b>Percentage of Holdings</b>
Currency:		
Euro Currency Unit	\$ 72,973,813	26.19 %
British Pound Sterling	71,987,200	25.84 %
Japanese Yen	47,881,073	17.18 %
Australian Dollar	20,293,607	7.28 %
Chinese Yuan Renminbi	16,969,259	6.09 %
Canadian Dollar	13,319,310	4.78 %
Swedish Krona	10,580,752	3.80 %
Hong Kong Dollar	6,617,407	2.37 %
Other	18,030,192	6.47 %
Total foreign currency holdings	<u>\$ 278,652,613</u>	<u>100 %</u>

## Commitments

The System is committed, as of June 30, 2006, to invest approximately \$213,314,009 in certain private equity, real estate partnerships, and real estate commingled funds.

## **5. SECURITIES LENDING PROGRAM**

Under the provisions of state statutes and the System's investment policy, the System lends securities, both equity and fixed income, to securities firms on a temporary basis primarily through the master trustee, Mellon Trust of New England, N.A. The System receives a portion of the earnings (split) for all loans and retains the right to amounts equal to all interest and dividend payments while securities are on loan.

Security loan agreements are collateralized by cash, U.S. government issued securities or irrevocable bank letters of credit. Domestic loans are initially collateralized at 102 percent of the market value plus any accrued interest. If the loans fall below 100 percent collateralization, the loan is marked back to 102 percent. Loans of non-U.S. securities are initially collateralized at 105 percent and are marked back to 105 percent if they fall below 105 percent. Notwithstanding the forgoing, however, standard industry practices may from time to time preclude the lending agent from obtaining additional collateral in connection with loans of global securities by the close of the next business day, unless the value of collateral held by the lending agent in connection with such loans is less than 100 percent.

Mellon Bank Global Securities Lending, a division of Mellon Trust of New England, N.A., invests all of the cash collateral generated from the System's securities loans into a collective cash collateral pool. The System holds an undivided share of the collateral provided by the borrower of its securities. The System cannot pledge nor sell the collateral unless the borrower fails to return the securities borrowed.

All securities loans can be terminated on demand by either the lender or the borrower. When a loan is closed, the securities on loan are returned to the System and the collateral associated with the loan is returned to the borrower. The lending agent shall hold the System harmless for any losses, cost or expenses arising as a result of negligence, misconduct or fraud by the lending agent.

The System had no credit risk as a result of its securities lending program as the collateral held exceeded the market value of the securities lent.

## **6. DERIVATIVES**

The System's investment managers may invest in derivative securities as permitted by their contracts. A derivative security is an investment whose payoff depends upon the value of an underlying asset such as bond and stock prices or a market index. Derivative financial instruments 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. To limit credit risk, each investment manager screens potential counter-parties and establishes and maintains an approved list of acceptable firms which meet a high level of credit-worthiness.

Market risk is the possibility that a change in interest or currency rates will cause the value of a financial instrument to decrease or become more costly to settle. The market risk associated with derivatives, the prices of which are constantly fluctuating, is managed by imposing contractual requirements on the investment managers as to the types, amounts and degree of risk they may undertake. Investment managers' derivative activities are reviewed on a periodic basis to monitor compliance with the contracts. The System does not purchase derivatives with borrowed funds and does not allow the leveraging of the portfolios.

The System's derivative investments may include foreign currency forward contracts, options, futures, and collateralized mortgage obligations. Foreign currency forward contracts are used to hedge against the currency risk in foreign stock and fixed income security portfolios. The remaining derivative securities are used to improve yield, adjust the duration of the fixed income portfolio, or to hedge changes in interest rates.

A forward contract is an agreement to buy or sell a specific currency position or security at a specified delivery or maturity date for an agreed-upon price. As the fair value of the forward contract fluctuates, the System records an unrealized gain or loss. A summary of net forward currency contracts outstanding at June 30, 2006 and 2005, are as follows:

	<u>2006</u>	<u>2005</u>
Long forward currency positions	\$ 77,506,210	\$ 37,325,037
Short forward currency positions	<u>77,800,757</u>	<u>37,220,030</u>
Unrealized gain (loss)	<u>\$ (294,547)</u>	<u>\$ 105,007</u>

A financial option is an agreement that gives one party the right, but not the obligation, to buy or sell a specific amount of an asset for a specified price, called the strike price, on or before a specified expiration date. The same leverage prohibitions which apply to forwards and futures are applicable to options. There were no financial options outstanding at June 30, 2006 or 2005.

Contractual amounts, which represent the fair value of the underlying assets the derivative contracts control, are often used to express the volume of these transactions but do not reflect the extent to which positions may offset one another. These amounts do not represent the much smaller amounts potentially subject to risk. Every position which is sold or purchased must be backed by assets, since the investment managers are not allowed to leverage the portfolio.

**Required Supplementary Information**

**Schedule of Contributions from the Employers and Other Contributing Entities**

<b>Year Ended June 30,</b>	<b>Annual Required Contributions</b>			<b>Percentage Contributed</b>		
	<b><u>Employer</u></b>	<b><u>Member</u></b>	<b><u>State</u></b>	<b><u>Employer</u></b>	<b><u>Member</u></b>	<b><u>State</u></b>
2006	\$56,078,840	\$18,525,032	\$2,745,784	100%	100%	100%
2005	47,717,299	17,672,155	2,745,784	100%	100%	100%
2004	36,868,735	16,772,145	2,745,784	100%	100%	100%
2003	28,857,743	15,871,489	2,816,189	100%	100%	100%
2002	28,542,482	15,696,746	2,816,189	100%	100%	100%
2001	27,345,914	15,039,155	2,942,724	100%	100%	100%
2000	26,170,758	14,393,323	2,942,724	100%	100%	100%

**Notes to Required Supplementary Information**

Valuation Date	July 1, 2006 and 2005
Actuarial cost method	Aggregate
Asset valuation method	Fair value adjusted for a four-year amortization of asset gains (losses)

Note: The System is not required to present the schedule of funding progress under the requirements of Governmental Accounting Standards Board Statement No. 25, "Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans," because the System uses the aggregate cost method to determine its aggregate actuarial liabilities. This method does not identify or separately amortize unfunded actuarial liabilities.

Actuarial assumptions:	
Investment rate of return	7.50 percent
Projected salary increases	4.50 to 12.59 percent

Mortality table	Effective with the July 1, 1999 actuarial valuation, the System began a 12 year phase-in of the 1994 Group Annuity Mortality Table from the 1971 Group Annuity Mortality Table. However, if the Cities' Contribution Rate exceeds 17% after reflecting an additional year of the phase-in, the phase-in will be deferred one year.
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## **Benefit Information**





## **Description of Benefit Plan**

The following section describes the eligibility of the membership of the System for different types of retirement benefits. Benefit formulas are established by Iowa Code Chapter 411. Revisions to the benefit program can only be instituted by the Iowa General Assembly. The Board of Trustees and the administration of the retirement system are required to administer the System in compliance with the statutory provisions. Questions concerning an individual's eligibility should be directed to the administration of the retirement system.

### **Retirement Age**

To qualify for a full service retirement, the member shall be age 55 or older with a minimum of 22 years of service at termination of employment. The other forms of benefits, with the exception of vested retirement, do not have specific age or length of service requirements. Retirement under the "ordinary or accidental" disability programs of the System are available to members who become permanently (defined as a duration of one year or longer) disabled while employed as a firefighter or police officer, without regard to the age of the member.

### **Benefit Amounts**

Current benefit amounts are based upon a percentage of the member's average monthly earnable compensation. The average monthly earnable compensation is calculated by adding the member's earnable compensation for the highest three years of service and dividing it by 36. The percentage multiplier varies by type of retirement and the length of the member's service. The benefit percentage for a service retirement is 66%, with 22 years of services, and 82%, with 30 year of service.

### **Refunds**

Members who terminated service after July 1, 1990 (other than by death, disability, or an involuntary layoff) may withdraw their contributions in total from their date of hire through their termination date. If a member withdraws contributions, the member waives any claim to benefits for the period of membership for which the withdrawal is made. Effective July 1, 1994, members who terminate service also have the option to rollover the eligible portion of their refund to another qualified retirement plan or to an Individual Retirement Account (IRA). Such rollovers must be approved in advance by the System. The contributions being withdrawn are credited with an annualized simple interest rate determined by the Board, currently set at 5%.

## Vesting

If the employment of a member is terminated (other than by death or disability) before age 55, or after age 55 but with less than 22 years of service, and the member has at least four years of service, the member is entitled to a vested service retirement payable at age 55. The benefit formula is a fraction of the pension the member would have received under a regular service retirement.

## Optional Forms of Payment

Members retiring as service or vested service retirement have the opportunity to select either the “basic benefit” as provided by Chapter 411, or one of four optional forms of benefit. Each of the optional forms are based on the member’s average monthly compensation and number of years of service. The options are calculated using actuarial tables which consider the age of the member at retirement, the age of the member’s beneficiary, and the assumed life expectancy of both. An explanation of each option is listed below:

Joint and 75% Survivor Annuity Benefit – An actuarial adjusted retirement allowance based upon the basic benefit. Following the member’s death, the **designated beneficiary** of the member will receive for their lifetime 75% of the member’s retirement allowance at the time of the member’s death. (If the designated beneficiary dies prior to the member, the benefit ceases upon the member’s death.)

Joint and 100% Survivor Annuity Benefit – An actuarial adjusted retirement allowance based upon the basic benefit. Following the member’s death, the **designated beneficiary** of the member will receive for their lifetime 100% of the member’s retirement allowance at the time of the member’s death. (If the designated beneficiary dies prior to the member, the benefit ceases upon the member’s death.)

Single Life Annuity with Designated Lump Sum Benefit – An actuarial adjusted retirement allowance based upon the basic benefit. Following the member’s death, the **designated beneficiary** of the member will receive a specified amount of money in a lump sum. The lump sum designated by the member must be evenly divisible by one thousand and may not reduce the member’s monthly retirement allowance by more than 50% of the straight life annuity benefit amount. (If the designated beneficiary dies prior to the member, the lump sum will be paid to the member’s estate.)

Straight Life Annuity Benefit – An actuarial adjusted retirement allowance based upon the basic benefit. Following the member’s death, no further benefits are payable.

## Examples of Monthly Benefit Computations

### Assumptions:

Member Age:	55	Beneficiary Age:	54
Spouse Age:	54	Lump Sum:	\$100,000
Average Monthly Compensation:	\$4,000		

### Service Retirement:

66% of the member's average final compensation. Additional benefits are available to members who perform more than 22 years of service (2 percent for each additional year of service, up to a maximum of 8 additional years).

Base Benefit:	\$4,000	x	66%	=	\$2,640
Maximum Benefit:	\$4,000	x	82%	=	\$3,280

### Optional Forms of Payment (Based on 66% Base Benefit of \$2,640):

Joint & 75% Survivor:	\$2,516
Joint & 100% Survivor:	\$2,402
Single Life Annuity with Lump Sum	\$2,702
Straight Life Annuity	\$2,930

### Accidental Disability

Greater of 60% of the member's average final compensation or the member's service retirement benefit calculation amount.

Base Benefit:	\$4,000	x	60%	=	\$2,400
Maximum Benefit:	\$4,000	x	82%	=	\$3,280

### Ordinary Disability

Greater of 50% of the member's average final compensation, for those with 5 or more years of service, or the member's service retirement benefit calculation amount, and 25% of average final compensation for those with less than 5 years of service.

Base Benefit with less than 5 years service:	\$4,000	x	25%	=	\$1,000
Base Benefit with more than 5 years service:	\$4,000	x	50%	=	\$2,000
Maximum Benefit:	\$4,000	x	82%	=	\$3,280

### Accidental/Ordinary Death

Accidental death benefits are 50% of the member's average final compensation and Ordinary death benefits are 40% of the member's average final compensation of the member.

Accidental Death Benefit:	\$4,000	x	50%	=	\$2,000
Ordinary Death Benefit:	\$4,000	x	40%	=	\$1,600

### Death after Retirement (Spousal and Child Benefit)

Survivor benefits are available to the beneficiary of a retired member according to the provisions of the benefit option chosen plus an additional benefit for each child.

Survivor (Assumes member elected Basic Benefit):	\$2,640	x	50%	=	\$1,320
Child Benefit:	\$4,000	x	6%	=	\$240



# **Statistical Summaries**



## Membership Data

The following table provides a profile of the current membership of the System:

### MEMBERSHIP PROFILE

July 1, 2006

#### Active Members:

• Number	3,816
• Average age	40.2
• Average past service	13.3
• Annual participating payroll	
~ Total	\$206,385,084
~ Average	\$54,084

#### Non-Active Members with Deferred Benefits:

• Number	286
• Average age	44.7
• Annual benefits	
~ Total	\$4,110,600
~ Average	\$14,373

#### Members and Beneficiaries in Pay Status:

• Number	3,531
• Average age	67.7
• Annual benefits	
~ Total	\$90,485,508
~ Average	\$25,626

*Membership Data, continued*

The membership of the MFPRSI includes firefighters and police officers from the largest cities within the State of Iowa. The forty-nine cities, whose fire and/or police personnel are covered by Chapter 411 of the Iowa Code, are as follows (*italics denotes police department only*):

Ames	Council Bluffs	<i>Indianola</i>	Ottumwa
Ankeny	Creston	Iowa City	<i>Pella</i>
Bettendorf	Davenport	Keokuk	Sioux City
Boone	Decorah	<i>Knoxville</i>	Spencer
Burlington	Des Moines	<i>LeMars</i>	Storm Lake
Camanche	<i>DeWitt</i>	<i>Maquoketa</i>	Urbandale
<i>Carroll</i>	Dubuque	Marion	Waterloo
Cedar Falls	<i>Estherville</i>	Marshalltown	Waverly
Cedar Rapids	<i>Evansdale</i>	Mason City	Webster City
Centerville	Fairfield	Muscatine	West Des Moines
Charles City	Fort Dodge	Newton	
Clinton	Fort Madison	Oelwein	
<i>Clive</i>	Grinnell	Oskaloosa	



*Membership Data, continued*

The following table reflects a statistical history of the benefit, disability, beneficiary, and refund activity of the System since its inception on January 1, 1992.

MEMBERSHIP APPLICATION ACTIVITY  
Through June 30, 2006

Type	FYS 92-94	FYS 95-97	FYS 98-00	FY 01-03	FY 2004	FY 2005	FY 2006	Total
<b>MEMBERS</b>								
Service Retirements	140	238	152	253	77	63	58	981
Disability Retirements								
Accidental	72	114	107	126	36	28	33	516
Ordinary	11	29	23	26	7	7	9	112
Denied	10	18	11	6	1	5	5	56
Vested Into Pay Status	19	23	26	41	16	11	25	161
<b>BENEFICIARIES</b>								
Service Retirements	50	76	81	75	31	37	26	376
Disability Retirements								
Accidental	43	29	44	44	15	10	14	199
Ordinary	8	9	7	10	1	1	4	40
Vested Into Pay Status	5	6	7	10	4	3	6	41
Accidental Death	3	4	6	3	2	0	2	20
Ordinary Death	4	5	7	4	1	1	2	24
Dependents	29	14	21	19	14	4	10	111
Lump Sum	2	2	2	4	4	1	1	16
<b>SUBTOTAL</b>	<b>396</b>	<b>567</b>	<b>494</b>	<b>621</b>	<b>209</b>	<b>171</b>	<b>195</b>	<b>2653</b>
Marital Property Orders								424
Child Support Orders								54
IRS Levies								14
Disability Re-examinations*	7	15	17	16	2	2	6	65
Refunds	108	149	204	180	66	95	74	876
<b>TOTAL ACTIVITY</b>	<b>511</b>	<b>731</b>	<b>715</b>	<b>817</b>	<b>277</b>	<b>268</b>	<b>275</b>	<b>4086</b>

## **Contributions to the Plan**

The financing of the System is derived from the payment of funds in the form of regular contributions from the membership and the cities and from the growth of invested assets.

### **Members' Rate of Contribution**

Member contributions to the System are based on a percentage of earnable compensation as defined in Chapter 411 of the Iowa Code, and further defined in the Administrative Rules of the System. To establish compliance with the Federal Older Workers Benefit Protection Act, the contribution rate for all active membership was statutorily adjusted to 9.35% in 1995.

### **Cities' Rate of Contribution**

Contributions to the System by the member cities are based on an annual actuarial valuation of the accrued liabilities and assets of the System and the amount needed to fund future benefit accruals of the membership. The contribution rate for the cities is discussed in the Actuarial Information Section.

### **Funds from the State of Iowa**

The Board and administration of the System have actively sought re-establishment of the full contributions from the State of Iowa and repayment of the under-funding over the last several fiscal years. The State provided \$2,745,784 this year toward its commitment (enacted by 1976 legislation).

# **Investment Report**



## Investment Performance

The performance of the retirement system's composite portfolio and that of the individual managers' portfolios is periodically reviewed by the Board of Trustees and administration.

An investment consulting firm submits a report to the System each quarter and provides technical information and investment advisory services to the Board and administration. Periodically, the Board reviews the investment policy of the System and implements changes to the strategic and tactical policies of the investment program. Effective July 1, 2004 Summit Strategies began to provide investment consulting services to the Board, including the periodic performance reports.

The performance of the System's portfolio from the inception of the fund through the latest fiscal year is reported on the following chart:

"Investment Performance"

	One Year	Three Years	Five Years	Since Inception
Total Fund	13.7%	14.9%	9.0%	9.0%
Policy Index	11.3%	12.9%	7.3%	8.2%
Target Actuarial Rate	7.5%	7.5%	7.5%	7.5%

[\* Inception Date: January 1, 1992]

Additional information which describes the performance of the investment portfolio(s) is available upon request to the retirement system.

Caveat: It is important to note that historical performance is not a guarantee of future performance of the portfolio due to the cyclical nature of markets and the individual components thereof.

## **Investment Policy - For the Fiscal Year Ending June 30, 2006**

(from "Statement of Investment Policies and Objectives")

### **I. DESCRIPTION OF SYSTEM**

The Municipal Fire and Police Retirement System of Iowa (the "System") is a statewide retirement system for fire fighters and police officer personnel employed in Iowa's largest cities.

Pursuant to State of Iowa Code Section 411.7 (as amended by Chapter 1240, Act of the 1990 Iowa General Assembly), effective January 1, 1992, the retirement System consolidated eighty-seven local retirement systems previously administered in forty-nine cities.

Permanent, full-time firefighters and police officers in the participating cities are automatically System members ("Participants"). Participants are vested upon attaining four years of membership service under the System.

The System is a defined benefit plan, maintained to provide income to employees upon their retirement. The System also provides benefits in the event of an employee's death or disability, or in the event of a vested employee's termination of employment prior to normal retirement. The System's fiscal year runs from July 1 through June 30.

### **II. A. STATEMENT OF PURPOSE**

The "Statement of Investment Policies and Objectives" (the "Statement") is intended to:

- A. Delineate the investment related responsibilities of the Board of Trustees, the Administration, and the providers of investment services which the System retains to manage the System's assets.
- B. Establish formal yet flexible investment guidelines, which incorporate prudent asset allocation and realistic total return goals.
- C. Provide a framework for ongoing communication between the Board of Trustees, the Administration of the System and the System's providers of investment services.
- D. Create standards of investment performance that are reasonable, consistent with the goals of the Board of Trustees, and by which the Investment Managers agree to be measured over time.

It is anticipated that this Statement will be reviewed annually by the Board of Trustees to insure the relevance of its contents to investment market conditions and System needs.

## II. B. INVESTMENT GOALS & STRATEGIC ASSUMPTIONS

### 1) INVESTMENT GOALS

The investment activities of the System are designed to meet the ongoing funding requirements of the benefit plans with which it is charged under Iowa Code Chapter 411.

The comprehensive goals of the investment program are as follows:

- 1) Meet the ongoing financial needs of the benefit plan as defined by the System's actuary, consistent with conservative actuarial policies.
- 2) Create the opportunity for periodic consideration (targeted at every 2 - 5 years) of benefit program enhancements and contribution rate adjustments, contingent upon the availability of favorable returns in the various capital markets.

Additional goals for the retirement system's investment program are as follows:

- To implement the requirements of the program as delineated within this "Statement of Investment Policies and Objectives".
- To provide for an investment program which shall serve the best interests of the members and beneficiaries of the System and which are reflective of the financial capabilities of their employers.
- To provide for a return on investment that, when combined with the periodic contributions of the membership and their employers, will meet the funding needs of the benefit plans.
- To meet or exceed the actuarial interest rate assumption as established by the Board of Trustees, over extended periods.
- To meet or surpass the performance expectations established for the portfolios as described in this document.
- To provide for the establishment of relationships with investment management firms and consultants who further the achievement of the System's financial purposes and which provide for the continuing refinement of a comprehensive investment program.

Obtaining specific performance goals in individual portfolios and in the various investment markets is contingent upon the continuing growth of the capital markets. Performance over specific periods will vary in concert with the economic conditions of the environments in which the assets are invested.

## 2) STRATEGIC ASSUMPTIONS

Certain basic assumptions concerning the investment markets are the foundation for the development of the System's investment policy.

- 1) Over the long-term there is a distinct relationship between return and risk. Cash should be used for liquidity, bonds to provide income and reduce volatility of quarterly returns, stocks for long-term appreciation of assets above inflation, and real estate for diversification of risk.
- 2) It is extremely difficult to "time the stock market." Therefore, cash should be kept to a minimum and target allocations to stocks and bonds should be maintained within reasonable bands.
- 3) Diversification into global markets, by investment style, and across the market capitalization spectrum (in stocks) is essential both to manage risk and to maintain exposure to the entire capital markets opportunity set for maximum return.
- 4) The role of active portfolio management is to add incremental value relative to the diversification strategy of the plan. "The role of passive management is to provide a core exposure in each of the various markets and to lower the overall costs of the management of the assets of the plan."
- 5) Diversification of the plan may include consideration and potential implementation of portfolios involving additional asset classes, such as real estate, emerging markets, etc.

## II. C. GENERAL INVESTMENT POLICIES

The following general investment policies of the System are intended to meet the System's investment goals and represent the resolution of the Board of Trustees, in accordance with the "Prudent Person" mandate of Iowa Code Chapters 411 and 97B.

### 1) ASSET ALLOCATION POLICIES

- a) "Asset Allocation Policy" - The System shall adopt and execute an asset allocation policy that is predicated on a number of factors, to include:
  - The projected liability stream of benefits and their cost,
  - The level of expected risk and of long-term capital markets' performance,
  - The historical performance of the capital markets,
  - The view of future economic conditions, to include inflation and interest rates assumptions,
  - The relationship between the current and projected assets of the plan and its actuarial requirements, and
  - The projected or expected changes in the level of financial support from its funding sources.



## II. C. GENERAL INVESTMENT POLICIES (continued)

The policy will identify the classes of assets the System will utilize and the percentage they are intended to represent of the total fund. The policy is designed to provide for diversification of assets in an effort to enhance the investment return to the System consistent with market and economic risk. Additionally, this policy provides the framework for distribution of cash flows and establishes the projected rate of return and standard deviation of return. Section IV of this document delineates the "Asset Allocation Policy" as adopted by the Board of Trustees.

- b) "Operational Expectations" - The System will invest its resources in conformity with the asset allocation policy enumerated in Section IV. The System expects that compliance with the specific allocation targets will, due to the fluctuation of the capital markets, be difficult to exactly obtain. Therefore, the Systems shall be viewed to be in compliance with the Asset Allocation Policy if the range of weights for the overall equity and debt portfolios is maintained.

### 2) PERFORMANCE POLICIES

"General Performance Expectations" - The performance of the System's investment program shall periodically be evaluated by the Board of Trustees. The general long-term performance expectations for the composite fund are as follows:

- 1) Performance that exceeds the rate of inflation as determined by the consumer price index (CPI),
- 2) Performance that exceeds the assumed actuarial rate of interest,
- 3) Performance that reflects the target asset allocation and appropriate indices for the various asset categories.

[See Section VI for specific performance expectations.]

### 3) RELATIONSHIP POLICIES:

- a) "Investment Manager Policies" - To achieve optimum performance results in concert with diversification of its assets the System selects and utilizes external investment managers to manage portions of its assets. The selection of the managers is accomplished through a Request for Proposal (RFP) process or Request for Information process (RFI) (see 3-h below). Each investment manager functions under a formal contract that delineates its responsibilities and the appropriate performance expectation. When appropriate, the System may compensate the external investment managers through the use of performance fees. Soft dollars generated through brokerage activity may, if authorized by the contract, be used to acquire investment research and analysis and to defray various administrative expenses. The System may determine to have a portion of its portfolio managed by the Administration of the System.
- b) "Manager Investment Discretion" - The investment managers under contract to the System shall have full discretion to direct and manage the investment and reinvestment of assets allocated to their accounts in accordance with this document, applicable federal and state statutes and regulations, and the executed contracts.

## II. C. GENERAL INVESTMENT POLICIES (continued)

- c) "Manager Brokerage Discretion" - The investment managers under contract to the System shall have discretion to establish and execute through accounts with one or more securities broker/dealer as the managers may select. The investment managers will attempt to obtain the "best available price and most favorable execution" with respect to portfolio transactions, unless such standard is not applicable in the applicable markets (foreign markets). At the direction of the System, selected portions of the manager's transactions may be directed to specific brokers by the System's Administration for the purpose of recapturing commissions for the System.
- d) "Manager Evaluation" - The external investment managers under contract with the System will meet with the administration and/or the Board of Trustees for the purpose of reviewing the investment activities of the individual portfolio, its performance under the contract, the investment strategy which governs its management and the market place in which it exists. The external investment managers are expected to meet periodically with the Administration at the Administration's request. Such meetings may be conducted at the offices of the investment firms.
- e) "Short Term Investments" - Cash allocated for investment by the investment management firms is managed in accordance with the guidelines established in the contractual agreement with each firm. Said guidelines stipulate that the firms shall invest their cash primarily in the STIF account of the System's custodial bank. Due to the fluid nature of the capital markets, cash allocation decisions shall be made by the Administration of the System consistent with the Board of Trustees asset allocation policy.
- f) "Investment Consultants" - The System may utilize the services of investment consultants for the purpose of performance review, asset allocation studies, manager selection screening and topical studies. The comments and recommendations of the consultant(s) will be considered in conjunction with other available information for the purpose of making an informed and prudent decision. The selection of the consultant(s) is accomplished through a Request for Proposal (RFP) process (see 3-h below). Each consultant shall function under a formal contract that delineates its responsibilities.
- g) "Custodial Bank" - The investment assets of the System shall be held in a custody/record keeping account in a master custody bank and in the international sub-custodian banks under contract to the custodian bank. The selection of the Custodial Bank is accomplished through a Request for Proposal (RFP) process (see 3-h below). The Custodial Bank shall function under a formal contract that delineates its responsibilities. The System authorizes the execution of a "Security Lending Program" which will be performed by the Custody Bank, under contract to the System.

## II. C. GENERAL INVESTMENT POLICIES (continued)

- h) "Selection and Retention" - The System will normally utilize a competitive Request for Proposal (RFP) or Request for Information process to select investment managers, consultants and the custodian bank. The contract with each of the firms shall provide for an ongoing relationship with the System and will establish definite service requirements for the firm. In selecting an individual firm through the RFP or RFI process, the System will evaluate, at a minimum, information relating to the following general categories:
- Organizational Structure & Relevant Experience
  - Investment Philosophy or Service Philosophy
  - Personnel & Staff Qualifications and Experience
  - Cost to the System.

The contract with the firm will provide for the termination of the relationship at the System's discretion. Action to terminate a relationship with a firm will be based upon the firm's performance under the contract and may take into consideration up to date information relating to the above general categories.

### 4) ADMINISTRATIVE POLICIES

- a) "Proxy Voting" - Voting rights of the stocks of American corporations will be exercised by the System's Administration or, at its direction by selected managers, in the best interest of the System and in accordance with the applicable statutes. The custodial bank will forward all proxies to the Administration of the System or to the designated Manager. The Administration or the Managers will execute the voting of the proxies in accordance with the "prudent person" standard delineated in Iowa Code Chapter 97B. It is the general policy of the System to vote its shares against measures that would hinder or preclude the acquisition or takeover of a corporation or company where a takeover or acquisition may be beneficial to the long-term earnings of the fund. Additionally, it is the general policy of the System to abstain from voting its shares on social issues, except where the voting of said proxy may serve to further the safety of the membership of the System, if consistent with the execution of the System's fiduciary responsibility. Issues arising in the proxy process may include:
- 1) Election of directors, including the number and terms of office, attendance and the number of meetings held.
  - 2) Selection and ratification of auditors.
  - 3) Stock splits, dividend and fractional share issues.
  - 4) Application for listing of securities.
  - 5) Corporate name changes.
  - 6) Remuneration of management, directors and employees, including ratification of employee stock option plans.
  - 7) Employment issues.
  - 8) Cumulative voting issues.
  - 9) Fees paid to auditors or consultants.
  - 10) Date or location of annual meetings.
  - 11) Contributions to charities or educational institutions.

## II. C. GENERAL INVESTMENT POLICIES (continued)

- 12) All other items which are not expected to have a material adverse effect on the price of the security or which would not substantially affect the rights or privileges of the security.
  - 13) Acquisitions, mergers and divestitures.
  - 14) Significant changes in the company's articles of incorporation or by-laws, such as anti-takeover provisions, "poison pills" or "rights" issues.
  - 15) Increases in the number of authorized shares.
  - 16) Business abroad.
- b) "Education and Due Diligence" - To maintain and strengthen the investment management of the System, the members of the Board of Trustees and/or the Administration may, when appropriate:
- 1) Participate in conferences/seminars related to the investment activities of public and private institutional investors and participate in the meetings of organizations, of which the System is a member,
  - 2) Meet periodically with the System's investment managers at the home office of each firm to perform a review and to clarify investment or administrative issues related to the management of the portfolio,
  - 3) Participate in the investors meetings conducted by the various managers of the System's assets, and
  - 4) Conduct due diligence visits to ascertain the acceptability of a firm or firms under consideration for management of the System's assets.
- c) "Organizations" - To maintain and strengthen the investment management of the System, the retirement System shall join national organizations related to institutional management, finance, and education.

### III. RESPONSIBILITIES

#### A. BOARD OF TRUSTEES

The Board of Trustees acknowledges their responsibility as fiduciaries of the System. In the management and administration of the invested assets (the “Funds”) that comprise the System, the Board of Trustees strives to act prudently and for the best long-term interest of the System and the membership.

The Board will periodically review the progress of the System in achieving its investment objectives, on the compliance with the policies and guidelines as outlined in this Statement, and on other matters, as appropriate. The Board of Trustees' shall, as an Investment Committee of the whole, or periodically through an AD-HOC Investment Committee appointed to represent the Board, perform the following:

- 1) Ensure that the contributions to the System and the proceeds from the investments are used in accordance with the objectives of the System.
- 2) Evaluate and select an independent investment consultant, if deemed necessary, to assist the Board of Trustees in forming investment objectives and policies, allocating assets, selecting investment vehicles and Managers, monitoring performance, and considering other appropriate issues as they may occur.
- 3) Develop investment objectives, guidelines and performance standards, which are consistent with the risk, return, and policy parameters of each investment component.
- 4) Evaluate and select Investment Managers, pooled funds, mutual funds, or other appropriate investment vehicles for each investment component of the System's assets.
- 5) Communicate the investment objectives, guidelines and standards (including any material changes that may occur) to the Investment Managers or responsible representatives of the selected investment alternatives of the Funds.
- 6) Review and evaluate results of each investment component in context with established standards of performance.
- 7) Take or direct the taking of appropriate action as deemed prudent and appropriate if investment results are below expectations or if prevailing conditions deem to warrant.
- 8) Ensure the compliance with the provisions and reporting requirements of pertinent federal, state, and local regulations and rulings.
- 9) Oversee the allocation of the State, City and membership contributions.

### III. RESPONSIBILITIES (continued)

#### B. INVESTMENT CONSULTANT

The Investment Consultant(s), in recognition of their role as a fiduciary of the System, shall perform the following:

- 1) Support the development of the "Statement of Investment Policies and Objectives" which identifies the various policy issues affecting the System's investment of assets.
- 2) Make recommendations, when deemed necessary, as to changes in the objectives, guidelines, or standards, based upon material and sustained changes in the capital markets.
- 3) Make recommendations, with supporting materials, as to the appropriate portfolio weights among the various major asset classes (stocks, bonds, cash) within the Funds.
- 4) Assist the Board of Trustees in the conduct of manager selections by:
  - a) Identifying and screening candidates for appropriate portfolio and organizational characteristics;
  - b) Performance of due diligence reviews and evaluations;
  - c) Quantifying of the trade-off between expected returns and risks among various investment alternatives; and
  - d) Functioning as an information-gathering agent.
- 5) Perform a quarterly performance evaluation of the System's portfolios and their components and provide a written report to the Board of Trustees following the end of each quarter. The written report will cover five basic areas:
  - a) Returns - Total time-weighted rates of returns.
  - b) Comparisons - Returns will be compared to appropriate benchmark indices and a universe of similar funds.
  - c) Diagnostics - Measurement of risk-adjusted performance, analysis of risks, style characteristics, and return attribution.
  - d) Compliance - Manager's compliance with the requirements of the individual contracts.
  - e) Risk profile of the System's portfolio and that of its individual components.

### III. RESPONSIBILITIES (continued)

- 6) Participate in periodic review meetings with the Board of Trustees and/or the administration to evaluate and assess the performance and quality of the individual managers. The purpose of such meetings will be to provide:
  - a) A review and re-appraisal of the investment program.
  - b) A commentary on investment results in light of the appropriate standards of performance.
  - c) A discussion of any key policy issues.
  - d) Any other matters as deemed appropriate by the Board of Trustees or the administration.

### C. ADMINISTRATION

The Administration shall perform the following on behalf of the Board of Trustees:

- 1) Coordinate the development of the "Statement of Investment Policies and Objectives" which identifies the various policy issues affecting the System's investment of assets.
- 2) Make recommendations concerning changes in the objectives, or guidelines, or standards, based upon material and sustained changes in the capital markets.
- 3) Administer the various policies delineated by this document to include the development of the asset allocation policy. Execute decisions made by the Board of Trustees concerning the investment program.
- 4) Participate in periodic review meetings with the Board of Trustees to evaluate and assess the performance and quality of the individual managers. Periodically, meet with individual investment managers, the custodian bank, and consultants to assess the quality of the services being provided to the System.
- 5) Establish contracts with the support of the System's legal counsel with investment managers, consultants and the custodian bank.
- 6) Vote the shares of the System's equity assets through the proxy process in consideration of its economic interests or direct the managers to vote the proxies of the System.
- 7) Upon authorization of the Board of Trustees and the establishment of specific guidelines, manage a portion of the System's assets.

### III. RESPONSIBILITIES (continued)

#### D. INVESTMENT MANAGERS

The Investment Managers, in recognition of their role as fiduciaries of the System, shall assume the following responsibilities as they pertain to:

- 1) Legally commit to invest the System's funds in accordance with the objectives, guidelines and standards delineated in the contractual document established between the System and the investment firm.
- 2) Exercise full discretionary authority as to all buy, hold, and sell decisions for each asset under the firm's management, subject to the requirements of the contract.
- 3) Make recommendations, when deemed necessary, as to changes in the objectives, guidelines, or standards, contained within the contract, based upon material and sustained changes in the capital markets.
- 4) Produce a statement for the System at the end of each month describing the portfolio asset class weights, individual security positions showing both cost and market value, and all principal cash transactions, including all buys and sells in sufficient descriptive detail. For commingled assets, this statement should show unit position and unit value.

Submit reports as requested by the system (quarterly, monthly, weekly ad-hoc) on the management of the System's assets, to include performance review.

- 5) At the request of the System, participate in periodic review meetings with any or all of the following: the Board of Trustees, the System's administration, or the System's Consultant. The subjects to be discussed shall include:
  - a) A review of the activities of the manager pertaining to the individual portfolio and commentary upon the specifics of the investment strategy.
  - b) A commentary on investment results in light of the appropriate standards of performance.
  - c) A synopsis of the key investment decisions made by the Manager, the underlying rationale, and how those decisions could affect future results.
  - d) A discussion of the Manager's outlook, what specific investment decisions outlook may trigger and how these decisions could affect future results.
- 6) Provide frequent and open communication with the System on all material matters pertaining to investment policies and the management of the System's assets. In particular, the Investment Managers will:



### III. RESPONSIBILITIES (continued)

- a) Provide notice of any material changes in their investment outlook, strategy, and portfolio structure.
  - b) Notify the System of material changes in the investment firm's ownership, organizational structure, financial condition, senior staffing and management.
  - c) Provide a copy to the System of each Manager's periodic S.E.C. Form ADV filing and of any other documents required by the contract with the System.
- 7) The Investment Managers will use their best judgment to obtain brokerage services based upon consideration of the objective of the best execution of trades and the lowest cost to the System. The System may direct the Investment Manager to direct a reasonable amount of brokerage fees to particular brokerage firms in payment for certain third-party services as may be determined to be needed by the System.
- 8.) The Investment Managers shall, upon request from the Administration, provide information concerning individual proxy issues. Issues arising in the proxy process may include both routine and non-routine matters.

### E. CUSTODIAN BANK

The Custodian Bank, in recognition of its role as a fiduciary of the System, shall assume the following responsibilities as they pertain to:

- 1) Hold all System deposits in the appropriate accounts, and provide highly secure storage of stock certificates and bonds, such that there is essentially no risk of loss due to theft, fire, or accident. Maintain appropriate records on computer files (data bases) that are secure and free from inappropriate manipulation.
- 2) Arrange for timely and business-like settlement of all purchases and sales made for the System. Transactions shall be on a "delivery versus payment" basis unless dictated by the requirements of the markets in which the transactions are conducted. The Bank shall act to insure the safety of the assets in the markets in which the transactions are conducted.
- 3) Provide for receipt and prompt crediting of all dividend and interest payments received as a result of the System's holdings. Monitor income receipts to ensure that income is received when due and institute investigative process to track and correct late or insufficient payments, including reimbursement of interest lost due to tardiness or shortfall.
- 4) Sweep excess cash daily into an interest bearing account featuring a high degree of safety of principal and liquidity.

### III. RESPONSIBILITIES (continued)

- 5) Provide monthly reports showing individual asset holdings with sufficient descriptive detail to include units, unit price, cost, market value, CUSIP number (where available), and any other information requested by the System. Principal cash transactions, including dividends and interest received, deposits and withdrawals, securities purchased, sold, and matured, and fee payments will also be listed.
- 6) At the direction of the (Executive Director) or their appointed representative, transfer funds into and out of specified accounts.
- 7) The Custodian Bank will promptly forward all proxy materials received to the Administration of the System or at the Administration's direction, to the appropriate investment manager for execution.

## IV. ASSET ALLOCATION

### A. ASSET ALLOCATION

The asset allocation policy shall be as follows:

#### “ASSET ALLOCATION POLICY”

U.S. Equity	30.0%	
Non-U.S. Equity	20.0%	
Real Estate	10.0%	
Alternative Investments	10.0%	
Total Equity Oriented Investments		70.0%
U.S. Fixed Income	12.0%	
Tactical Fixed Income	18.0%	
Cash	0.0%	
Total Debt Oriented Investments		30.0%

Total Plan Performance Expectation %	8.00%*
Standard Deviation (Risk) %	10.40%

[\* Allocation, performance expectation and risk projection based upon Summit’s 2005 assumptions.]

#### “ALLOCATION POLICY DETAIL” COMPONENTS OF PORTFOLIO

	Core	Alternative	Strategic
U.S. Equity Target	37.5%		37.5%
International Equity	25.0%		25.0%
Real Estate		50%	
Alternative Equity		50%	
Component Equity Target	62.5%	100.0%	62.5%
U.S. Fixed Income	15.0%		
Tactical Fixed Income	22.5%		
Universal Fixed Income			37.5%
Cash	0.0%		0.0%
Component Debt Target	37.5%		37.5%

#### CAVEATS:

- 1) In the absence of suitable opportunities within a specific market, the funds shall be directed to the other components within the debt or equity category. Due to the fluctuation of market values, positioning within a range shall constitute compliance with the policy. The acceptable range is identified for each major component of assets

#### IV. ASSET ALLOCATION - (continued)

- 2) A review of the allocation policy shall occur periodically to allow the Board of Trustees to consider the affect of any changes in market conditions or of the expectations for the retirement system.

#### B. PORTFOLIO DEFINITIONS

The individual portfolios are established through contracts with the investment management firms selected to manage the assets of the System. The definition of each portfolio is described In Exhibit A to this document. Refinements and additions to the portfolios and to the applicable definitions will be performed as the Board of Trustees reviews the investment program periodically.

#### C. PORTFOLIO ADJUSTMENTS

The System will allocate cash flows to establish the portfolios consistent with the target allocation for each portfolio type. Periodically, the Board of Trustees will examine the weights of each portfolio relative to the targets and to the ranges established by the Asset Allocation policy. The System may act to adjust the size of individual portfolios through the withdrawal of funds from individual portfolios and the reallocation to under-weighted portfolios or may rely upon the commitment of future cash flow to increase the size of individual portfolios.

## V. ASSET GUIDELINES

The assets to be held in each portfolio shall be delineated in the contract to be established with the individual investment management firm. The requirements for the individual manager's shall be consistent with the general policies described, as follows:

### A. STOCKS AND BONDS (DOMESTIC, INTERNATIONAL & EMERGING MARKETS)

The stock and bond holdings of the System may include:

- Securities issued by and the obligations of or guaranteed by the United States of America or U.S. government sponsored enterprises or by the Dominion of Canada or any province thereof, financial futures and options;
- Bonds issued by the State of Iowa or its political subdivisions;
- Common stock, American Depository Receipts, corporate bonds or other evidences of indebtedness issued under the laws of the Dominion of Canada or any province thereof;
- Common stock, bonds or other evidences of indebtedness issued under the laws of selected foreign countries or their political subdivisions;
- Debt instruments issued by multinational organizations, on behalf of selected nations or groups of nations, such as Brady Bonds, whether in U.S. dollars or foreign currencies;
- Mutual funds or commingled funds, which are, comprised of stocks and or debt instruments, including those which hold positions in emerging markets, whether in U.S. dollars or foreign currencies;
- Derivative instruments, such as futures and options, which shall be utilized as an alternative to a stock or bond position, as specified.

### B. OTHER ASSET CLASSES

The currency position of the system shall include the currency of a group of selected nations, which have well established and stable economic and political structures. Currency positions will be only taken in countries or in multinational currencies (for examples, Euros) in which the System has determined to invest the System's assets. The currency assets of the System shall be represented within the individual portfolios of the investment managers, which have mandates, which include international bond or stocks. The benchmark against which these managers run the portfolios shall include a zero percent hedged position to the U. S. dollar for the international portions of the mandates.

## V. ASSET GUIDELINES - (continued)

### C. DERIVATIVE INSTRUMENTS

Derivative instruments, such as futures and options, may be utilized in selected portfolio for the following purposes:

- 1) As an alternative to maintaining a selected asset position,
- 2) To maintain the duration of securities in a portfolio,
- 3) To gain exposure in a time of dollar strength to a foreign bond market with minimal exposure to the currency of the country,
- 4) To hedge or otherwise protect existing or anticipated portfolio positions,
- 5) To establish and maintain the currency positions for the currency overlay portfolio and for the individual currency activities of the individual portfolios, and
- 6) Not to speculate or leverage (gear-up) the portfolio.

Derivative instruments are generally defined as contracts whose value depends on ("derives" from) the value of an underlying asset, reference rate, or index. Derivative instruments include both of the following:

- a) "Over the counter" (OTC) derivatives: privately negotiated contracts provided directly by dealers to end-users; which include swaps, futures and options, based upon interest rates, currencies, equities, and commodities; and
- b) Standardized contracts sold on exchanges: which include futures and options.

### D. REAL ESTATE

The real estate positions of the System may include domestic or international real estate investments in individual properties or groups of properties, through one or more of the following: direct purchase or mortgage of individual properties, participation in a commingled fund (open-ended or closed-ended) or in a trust or a partnership, which has positions in one or more properties.

The real estate positions of the System may include investment in securitized real estate, via publicly traded or privately held Real Estate Investment Trusts (REITS).

## VI. INVESTMENT OBJECTIVE & PERFORMANCE STANDARDS

The primary objective of the System is to pay benefits when and as they come due. The assets of the System will be actively invested to achieve growth of capital through appreciation of securities and through the accumulation and reinvestment of dividend and interest income.

The performance standards for the System's portfolios are developed consistent with those commonly found to be applicable to large institutional investors of a similar nature to the System.

### A. TIME HORIZON

Progress of the System, its Funds and their components against their return objectives will typically be measured over a full market cycle. Market cycles may differ markedly in length, and there is no standardized measure for a market cycle's term. For the System's purposes, a full market cycle encompasses both a down leg and an up leg, in either order. The up or down portions each will be of at least two consecutive quarters in length. Thus, a full market cycle may be as short as one year, though generally market cycles are expected to last from three to five years.

The above-described concept does not preempt the periodic review and evaluation of the activities and performance of individual investment managers over a period of time that is of longer or shorter duration than a market cycle. The Board of Trustees reserves to itself the right to take action relative to individual managers or to the portfolio as a whole without regard to the above described concept.

### B. RETURN OBJECTIVE

Over a full Market Cycle, the assets of the System will be invested in a diversified manner which has as its performance objective a return of 8.00% with an annualized rate of inflation of 2.25% and a Standard Deviation of 10.40%

### C. STATISTICAL COMPARISON

The total returns on each asset class, equity and fixed income manager, and the total investment portfolios will be compared to the appropriate index for the market in which they invest and/or to the interest rate assumption of the retirement System.

## EXHIBIT A - DEFINITIONS & DESCRIPTIONS OF PORTFOLIOS

The System shall utilize both index fund management and active portfolio management for investment of the portfolio:

### "INDEX MANAGEMENT":

A portfolio that is intended to emulate the performance of a specific index, which is representative of all or a portion of a specific capital market or markets. The portfolio will be fully invested except during periods of re-balancing.

### "ACTIVE MANAGEMENT"

A portfolio that is actively managed by individual investment management firms with the intent of achieving performance, which surpasses that of the capital market(s) in which it is invested, as measured by a relevant market index or a composite benchmark.



## "PORTFOLIO DESCRIPTIONS"

### **CORE PORTFOLIO**

#### **A. DOMESTIC INDEX STOCK FUND (“INDEX MANAGEMENT”)**

*SSgA (State Street Global Advisors) (Boston, MA.)*  
- Russell 1000 (stock) Index Fund

#### **B. DOMESTIC ENHANCED INDEX FUND**

*PIMCO (Pacific Investment Management Co.) (Newport Beach, CA.)*  
A portfolio comprised of S&P 500 Futures Contracts, U. S. Treasury Securities and Cash which is intended to outperform the performance of the U.S. equity market as represented by the S&P 500 index, with index-like volatility (risk) and with no leverage.

#### **C. DOMESTIC SMALL CAPITALIZATION EQUITY PORTFOLIO**

*DIMENSIONAL FUND ADVISORS (Santa Monica, CA.)*  
A diversified portfolio comprised of small capitalization stocks and cash, which is intended to outperform the performance of an index, which represents the small companies within the U.S. stock market.

#### **D. ACTIVELY MANAGED INTERNATIONAL EQUITY PORTFOLIO**

- 1. BAILLIE GIFFORD OVERSEAS, LTD. (Edinburgh, Scotland)*
- 2. DELAWARE INTERNATIONAL ADVISERS, LTD (London, England)*

A diversified portfolio comprised of equity and cash, which is invested in stocks listed on established international stock markets with the intent to out-perform a broad-based international equity index . The portfolio shall also invest in emerging markets.

#### **E. DOMESTIC FIXED INCOME (CORE)**

*BLACKROCK (New York)*  
A diversified fixed income portfolio which contains securities issued by and the obligations of or guaranteed by the United States of America or U.S. government sponsored enterprises or by the Dominion of Canada or any province thereof, financial futures and options, and of corporate bonds or other evidences of indebtedness issued under the laws of the United States or its political subdivisions. The portfolio may invest opportunistically in the securities issued by and obligations guaranteed by developed foreign countries. Securities issued by emerging market or developing market countries shall not be included in the portfolio. Securities acquired for the portfolio shall be of investment grade as rated by a recognized rating agency.

## **F. TACTICAL FIXED INCOME (ABSOLUTE RETURN) PORTFOLIO**

1. *JULIUS BAER*
2. *ALLIANCE BERNSTEIN*

A fixed income portfolio in which the manager is expected to implement a “best ideas” portfolio, i.e. not a bench-mark sensitive approach to portfolio construction. The portfolio will include, but may not be limited to investments in the following markets: domestic fixed income, high yield, emerging market debt, global bonds, non-dollar tips, global tips, and bank loans.

The benchmark for the portfolio will be an absolute return target, (such as Libor +300bp) rather than measuring a return relative to an investable index.

**ALTERNATIVE PORTFOLIO - See addendum one**

## **G. REAL ESTATE PORTFOLIO**

“DIVERSIFIED CORE PORTFOLIO”

1. *J.P. MORGAN INVESTMENT MANAGEMENT, INC. (New York)*
2. *TA ASSOCIATES (Boston)*

A diversified portfolio comprised of investments in non-leveraged and leveraged real estate properties, either directly through individual ownership, through participation in one or more commingled real estate property funds, or through the acquisition of REITs, either directly or through a fund. The portfolio will have a target investment strategy of sixty-five percent in funds, which acquire direct real estate assets, and thirty-five percent in a fund, which acquires REIT securities.

“ACTIVE REAL ESTATE PORTFOLIO- Partnership, Trust or Funds”

1. *FIDELITY MANAGEMENT TRUST COMPANY (New York)*
2. *HINES CAPITAL MARKETS (Houston)*
3. *SENTINEL REALTY ADVISORS CORPORATION (New York)*

A portfolio comprised of investments held in a partnership, trust, or fund, which acquires, manages and disposes of non-leveraged and leveraged real estate properties.

The retirement System’s overall portfolio will invest in one or more funds, partnerships, or trusts, which are each focused on an individual sector or sectors of the direct real estate market. Real estate portfolios, investing in the following sectors may be included: apartments, industrial, retail, commercial office, turn-around opportunities, as well as others not identified.

## **H. ALTERNATIVE INVESTMENTS IN PRIVATE EQUITY & DEBT**

1. *ADAM STREET PARTNERS, LLC (Chicago)*
2. *HARBOURVEST PARTNERS (Boston)*

A portfolio comprised of investment in a “fund of funds” which acquires positions in various venture capital funds, buyout funds and opportunistic funds. Investments made by the individual funds shall be via equity ownership and/or privately placed debt.

**ADDENDUM ONE: “ALTERNATIVE PROGRAM – INVESTMENT ALLOCATION UTILIZATION OF INDEX FUNDS Adopted: November 28, 2002”**

The Board of Trustees has established, as an element of its investment allocation policy, a targeted commitment to alternative asset classes: 10% to Real Estate and 10% to Private Equity. Conditions exist which make it difficult to achieve the fully invested market commitments:

- a) The nature of the investment vehicles used to implement the strategy, require an extended period of time (3 to 6 years) before the commitments are fully drawn.
- b) During the investment period, liquidation of earlier investments may occur within the partnerships, which causes a return of dollars from the earlier draw-downs.

To address this problem, the Board adopted the following policy for the placement of the committed funds, prior to the funds being drawn by the individual real estate and private equity partnerships.

*Concept for Real Estate*

To achieve the real estate target, utilization of the “Index REIT (Real Estate Investment Trust) Strategy” fund, as offered by State Street Global Advisors. This approach allows the System to have a ten percent allocation to the real estate markets, through the combination of active direct real estate investments and the REIT market. Dollars not yet called by the individual partnerships will be placed in the index fund until they are called by the individual managers.

- 1) The initial funding will be at approximately \$50 million and will be drawn downward from that level.
- 2) The SSGA REIT index fund is a portfolio of securities that replicates, as closely as possible, the returns and characteristics of the Wilshire REIT Index.
- 3) Liquidity is available on a monthly basis.

*Concept for Private Equity*

To establish additional equity funding as a proxy for private equity, utilization of the “World Index Plus Strategy”, an equity fund offered by State Street Global Advisors. This approach will allow the System to have a ten percent commitment, through the combination of the private equity partnership and the index plus fund. Dollars not yet called by the private equity partnership will be placed in the index fund until they are drawn down by the investment manager (Adams Street).

- 1) The initial funding will be at approximately \$100 million and will be drawn downward from that level.
- 2) The SSGA fund is a portfolio of securities that replicates the characteristics of the global index, with risk controls that seek to ensure that the strategy does not have a style or size bias. The Strategy employs a quantitative multi-factor selection model to construct a portfolio, which is intended to consistently outperform the benchmark by low to moderate amounts. Portfolios are designed to provide equity exposure with tightly constrained country and industry mis-weights.
- 3) Liquidity is available on a daily basis.

## STRATEGIC PORTFOLIO

### I. STRATEGIC (GLOBAL BALANCED) PORTFOLIOS

(U.S. Equity, International Equity, Fixed Income, Emerging Market Equity)

1. *MORGAN STANLEY DEAN WITTER ASSET MANAGEMENT (New York)*
2. *J.P. MORGAN FLEMING INVESTMENT MANAGEMENT, INC. (New York)*
3. *GRANTHAM, MAYO, VAN OTTERLOO AND CO. LLC (Boston)*

A diversified portfolio comprised of fixed income, equity, emerging market equity and debt, and cash which is invested in securities of global markets with the intent to out-perform a composite index which is weighted sixty-two and one-half percent to equity and thirty-seven and one-half percent to fixed income.

## TRANSITION ASSETS

### *CUSTODIAL BANK - MELLON TRUST (Boston)*

Cash and Short Term Investments - Effective April 2005, the cash portion of the System's assets will be invested either in a STIF product available from the custodial bank (Mellon Trust) or in an enhanced cash fund which is managed by Standish Mellon, a subsidiary of Mellon Trust.

Transition Assets - Selected assets transferred to the System as of the date of the consolidation, which due to the market conditions, the maturity of the asset or the specific nature of the asset, have not been liquidated by the System.

# **Actuarial Information**



## Actuarial Summary

An actuarial valuation of the Municipal Fire and Police Retirement System of Iowa was made as of July 1, 2006 based on the funding method mandated under Iowa Code Chapter 411.

As of July 1, 2006, the System covered 3,816 active employees with an annual payroll (earnable compensation) of \$206.4 million, and 3,817 inactive participants.

The required contribution rate for the Cities for the 2006-07 plan year has been certified by the Board of Trustees at 25.48% of covered payroll (earnable compensation). The contribution rate was calculated by the actuary as shown on the following page.

The following table shows the required contribution rates for the Cities since the inception of the System.

TABLE: CITIES REQUIRED CONTRIBUTION RATE

17.00% for the period 1/1/92 - 6/30/93 *
19.66% for the period 7/1/93 - 6/30/94
18.71% for the period 7/1/94 - 6/30/95
17.66% for the period 7/1/95 - 6/30/96
17.00% for the period 7/1/96 - 6/30/97*
17.00% for the period 7/1/97 - 6/30/98*
17.00% for the period 7/1/98 - 6/30/99*
17.00% for the period 7/1/99 - 6/30/00*
17.00% for the period 7/1/00 - 6/30/01*
17.00% for the period 7/1/01 - 6/30/02*
17.00% for the period 7/1/02 - 6/30/03*
20.48% for the period 7/1/03 - 6/30/04
24.92% for the period 7/1/04 - 6/30/05
28.21% for the period 7/1/05 - 6/30/06
27.75% for the period 7/1/06 - 6/30/07
25.48% for the period 7/1/07 - 6/30/08
* Rate certified at statutory minimum of 17.00%

The 2006 valuation is based on asset values as of June 30, 2006, participant census data as of July 1, 2006 and current System provisions.

All other System provisions and actuarial assumptions remained unchanged from the prior valuation.

## Contribution Rate

The required contribution rate as determined by the System's actuary is developed below:

	<u>July 1, 2006</u>
1. Actuarial Present Value of all Future Benefits	
a. Active Members:	
• Service Retirement	788,390,684
• Ordinary Disability	91,933,308
• Accidental Disability	246,030,676
• Ordinary Death	28,073,947
• Accidental Death	30,609,793
• Withdrawal	24,535,979
• <u>Total Active</u>	<u>1,209,574,387</u>
b. Inactive Members:	
Members receiving benefits	1,054,402,106
• Deferred vested terminations	27,946,999
• Refund of member contributions due	145,938
• <u>Total Inactive</u>	<u>1,082,495,043</u>
c. <u>Total Present Value of Future Benefits</u>	<u>2,292,069,430</u>
2. Actuarial Value of Plan Assets	1,528,572,608
3. Actuarial Present Value of Future Member Contributions	197,411,942
4. Present Value of Unfunded Future Benefits (1) – (2) – (3)	566,084,880
5. Present Value of Future Payroll of all Covered Members	2,111,357,666
6. Total (Cities plus State) Normal Contribution Rate (4)/(5)	26.81%
7. Covered Payroll	206,385,084
8. Preliminary Total Contribution from Cities and State (6) x (7)	55,331,841
9. Estimated State Contribution	2,745,784
10. Estimated State Contribution as a Percent of Payroll: (9)/(7)	1.33%
11. Preliminary Cities' Contribution (8) – (9)	52,586,057
12. Cities' Contribution as a Percent of Covered Payroll (11)/(7)	25.48%
13. Minimum Required Contribution Rate for Cities	17.00%
14. Cities' Contribution (Greater of 12 or 13) x (7)	52,586,919



## Actuarial Present Value of Accrued Benefits

A comparison of market value of assets with the actuarial present value of accumulated plan benefits provides one measure of the funded status of the System. The actuarial present value of accumulated plan benefits consists of the liability for pension and ancillary benefits that have been earned on the basis of each participant's salary and service history as of the valuation date. These values under the current assumptions as of the current valuation date are shown below along with funded percentage (the market value of assets divided by the actuarial present value of accumulated plan benefits).

	<u>July 1, 2006</u>
1. Present value of vested accrued benefits	
a. Present value of vested accrued benefits for active members	600,186,185
b. Present value of benefits for terminated members	28,092,937
c. Present value of benefits being paid to retirees and beneficiaries	<u>1,054,402,106</u>
Total	1,682,681,228
2. Present value of accrued non-vested benefits	34,880,791
3. Present value of all accrued benefits (1) + (2)	1,717,562,019
4. Market value of assets	1,658,428,273
5. Ratio of market value of assets to the present value of all accrued benefits (4) / (3)	97%
6. Ratio of market value of assets to the present value of vested accrued benefits (4) / (1)	99%

## **Actuarial Cost Method**

The Aggregate Actuarial Cost method was used to determine recommended contributions. Using this method, the present value of benefits to be funded by future contributions is determined by subtracting the actuarial value of plan assets and the actuarial present value of future member contributions from the present value of projected benefits. This result, the present value of unfunded future benefits, is divided by the present value of future salaries of active members included in the valuation to determine a normal cost accrual rate. The normal cost accrual rate is multiplied by the total of current annual salaries of members in the valuation to determine the recommended contribution.

Using the aggregate method, gains and losses that arise due to actual experience are not directly determined and recognized each year. Gains and losses are included in the present value of unfunded future benefits and affect the normal cost accrual rate. As a result, gains and losses are spread over the remaining period to retirement members in the valuation and are recognized as a portion of future annual contributions.

## **Funded Status**

Measurements used to evaluate the funding status of the System are based on procedures set forth by GASB (Government Accounting Standards Board). In an effort to enhance the understandability and usefulness of the pension information that is included in the financial reports of pension plans for state and local governments, GASB has issued Statement No. 25—Financial Reporting for Defined Benefit Pension Plans.

GASB Statement No. 25 establishes a financial reporting framework for defined benefit plans. In addition to two required statements regarding plan assets, the statement requires two schedules, the Schedule of Funding Progress and Schedule of Employer contributions, and accompanying notes disclosing information relative to the funded status of the plan and historical contribution patterns.

- The Schedule of Funding Progress is not required for systems which use the Aggregate Method to determine the Annual Required Contribution (ARC). Since the System uses the Aggregate Method to determine the ARC, this schedule has not been developed.
- The Schedule of Employer Contributions provides historical information about the Annual Required Contribution (ARC) and the percentage of the ARC that was actually contributed. For the System, the ARC is equal to the normal contribution rate multiplied by the covered payroll for the year or \$55,331,841 for 2006. This is the total ARC before any adjustment for minimum contribution rates or state contributions.