

Public School Employees' Retirement System  
**Comprehensive Annual Financial Report**

Fiscal Year Ended June 30, 2006

A Component Unit of the  
Commonwealth of Pennsylvania

# **Public School Employees' Retirement System**

(A Component Unit of the Commonwealth of Pennsylvania)

PO Box 125  
Harrisburg, Pennsylvania 17108-0125

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## **Comprehensive Annual Financial Report**

for the

Fiscal Year Ended June 30, 2006

**Roger H. May**

***Chairman***

**Honorable Steven R. Nickol**

***Vice Chairman***

***Board of Trustees***

**Jeffrey B. Clay**

***Executive Director***

*Report prepared by the Public School Employees' Retirement System staff*

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Certificate of  
Achievement  
for Excellence  
in Financial  
Reporting

Presented to  
Public School  
Employees' Retirement System  
Pennsylvania

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
June 30, 2005

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



A handwritten signature in cursive script, appearing to read "Thomas H. ...".

President

A handwritten signature in cursive script, appearing to read "Jeffrey R. Emer".

Executive Director



Public Pension Coordinating Council  
Public Pension Standards  
**2006 Award**

Presented to

**Pennsylvania Public School Employees' Retirement System**

In recognition of meeting professional standards for  
plan design and administration as  
set forth in the Public Pension Standards.

*Presented by the Public Pension Coordinating Council, a confederation of*

National Association of State Retirement Administrators (NASRA)  
National Conference on Public Employee Retirement Systems (NCPERS)  
National Council on Teacher Retirement (NCTR)

A handwritten signature in cursive script that reads "Alan H. Winkle".

Alan H. Winkle  
Program Administrator

## Chairman's Report

COMMONWEALTH OF PENNSYLVANIA  
PUBLIC SCHOOL EMPLOYEES' RETIREMENT SYSTEM

Telephone (717) 720-4749

Roger H. May, Chairman of the Board

December 1, 2006

The Honorable Edward G. Rendell  
Governor of Pennsylvania

Members of the Legislature  
Members of the Retirement System

Dear Governor Rendell, Legislators, and Members:

On behalf of the Board of Trustees of the Pennsylvania Public School Employees' Retirement System (the System, PSERS), I am pleased to present this eighty-seventh *Comprehensive Annual Financial Report* for the fiscal year ended June 30, 2006. The report provides an in-depth review of the financial, actuarial, and investment status of the Retirement Fund and PSERS' postemployment healthcare programs.

As the System's report details, as of June 30:

1. The funded status of the pension plan as reported in the System's June 30, 2005 Actuarial Valuation was 83.6%.
2. The net assets held in trust for pension benefits were \$57.2 billion.
3. Net assets held in trust for postemployment healthcare benefits were \$181.6 million.
4. The active contributing membership of the System numbered approximately 263,000.
5. The number of annuitants totaled approximately 162,000 and received in excess of \$4.1 billion in pension and postemployment healthcare benefits during the fiscal year.

The Board of Trustees is committed to prudent management of the System's assets for the benefit of the membership. At the same time, we are aware of our responsibilities to the Commonwealth, its taxpayers, and the System's employers.

The Board of Trustees appreciates the cooperation extended to it by the Governor's Office and the Legislature which enables and empowers us to meet the challenges which face us currently and make timely provisions for the challenges ahead.

The Board of Trustees pledges to continue to administer the affairs of the Pennsylvania Public School Employees' Retirement System in the most competent and efficient manner possible.

Roger H. May  
Chairman  
Board of Trustees

Public School Employees' Retirement System

# Introductory Section



# *Mission Statement*



*The Board of Trustees and the employees of the Public School Employees' Retirement System serve the members and stakeholders of the System by:*

- *Prudently investing the assets of the System*
- *Maintaining a financially sound System*
- *Providing timely and accurate payment of benefits*
- *Clearly communicating members' and employers' rights and responsibilities, and*
- *Effectively managing the resources of the System*

adopted 12/9/2005

## Letter of Transmittal



COMMONWEALTH OF PENNSYLVANIA  
**PUBLIC SCHOOL EMPLOYEES' RETIREMENT SYSTEM**

**Mailing Address**  
 PO Box 125  
 Harrisburg PA 17108-0125

**Toll-Free** - 1-888-773-7748  
 (1-888-PSERS4U)  
**Local** - (717) 787-8540

**Building Location**  
 5 North 5th Street  
 Harrisburg PA 17101

December 1, 2006

The Board of Trustees  
 Pennsylvania Public School Employees' Retirement System  
 Harrisburg, PA 17101

We are pleased to present the eighty-seventh edition of the *Comprehensive Annual Financial Report* for the Pennsylvania Public School Employees' Retirement System (the System, PSERS) for the year ended June 30, 2006. The management of the System is solely responsible for the accuracy and completion of this report, pursuant to section 24 Pa.C.S. §8502(n) of the Public School Employees' Retirement Code (Retirement Code).

The System was established on July 18, 1917 to provide retirement benefits to public school employees of the Commonwealth of Pennsylvania. The System has experienced various benefit modifications throughout its existence.

The members eligible to participate in the System include all full-time public school employees, part-time hourly public school employees who render at least 500 hours of service in the school year, and part-time per diem public school employees who render at least 80 days of service in the school year for any of the 733 reporting entities in Pennsylvania. As of June 30, 2006, the System had approximately 263,000 active members with an estimated annual active payroll of \$11.4 billion.

The annuitant membership at June 30, 2006 was comprised of approximately 162,000 retirees and beneficiaries who receive nearly \$273 million each month. The average yearly benefit paid to annuitants is \$20,236. The average benefits for each option type are detailed in the **Statistical Section** of this report.

The System is a governmental cost-sharing multi-employer defined benefit pension plan, to which 733 reporting units contribute. PSERS is administered by a staff of 300. The System is headquartered in Harrisburg, Pennsylvania, and maintains eight field offices in strategic areas of the Commonwealth to enable direct contact with the membership and the System's employers.

This report has been prepared in accordance with the principles of governmental accounting and reporting as promulgated by the Governmental Accounting Standards Board (GASB). The report consists of five sections: the **Introductory Section** containing the Chairman's Report, the Transmittal Letter, and the Administrative Organizational Structure; the **Financial Section** containing the opinion of the independent certified public accounting firm, the financial statements of the System, and Management's Discussion and Analysis of the financial statements (MD&A); the **Investment Section** containing an overview of the System's investment activities; the **Actuarial Section** containing the opinion of the independent actuarial firm and the results of its latest actuarial valuation; and the **Statistical Section** containing significant data pertaining to the System.

PSERS was established by law as an independent administrative board, directed by a governing board of trustees (Board) which exercises control and management of the System, including the investment of its assets. PSERS is considered a component unit of the Commonwealth of Pennsylvania as defined by the GASB. An annual audit of the System by a certified public accounting firm is required by the Retirement Code. PSERS has contracted with Clifton

Gunderson LLP for this audit of its financial statements and has received an unqualified opinion as evidenced in the **Independent Auditors' Report** in the **Financial Section** of this report.

### **Economic Summary**

Investment market conditions showed continued strength during the fiscal year ended June 30, 2006 (FY 2006) enabling PSERS' investment portfolio to generate a rate of return of 15.26%. The total net assets of the System increased from \$52.1 billion to \$57.4 billion from July 1, 2005 to June 30, 2006. The increase is primarily attributable to net investment income and member and employer contributions combined that exceeded the payment of pension benefits and administrative expenses.

The Board has continued to fulfill its mission to maintain stability and the long-term optimum value of the Fund. This is evidenced in the long-term growth of the System's assets and the strength of the System with respect to its funding status. Of utmost importance to the Board is the assurance that the required reserves are available for payment of current and prospective retirement benefits. PSERS has maintained its position among the top twenty-five largest pension systems in the nation.

### **Major Initiatives**

#### **New Pension Administration System (NPAS)**

PSERS' largest project ever, the "New Pension Administration System" or NPAS, continued throughout FY 2006.

In January of 2006, PSERS implemented benefit payment processing functions. The payment processing functions control the disbursement of all PSERS benefits, including the monthly retirement benefit payroll as well as refund and death benefit payments. From January 2006 through November 2006, PSERS issued more than 1.8 million benefit payments totaling about \$3.7 billion using the new system.

In April of 2006, PSERS started the implementation of the purchase of service credit application processing and billing functions. Work is proceeding to bring those features up to full-speed and eventually to service levels above those of the past.

Efforts continue on maintaining and enhancing those functions implemented in earlier phases of the project, the most notable being the Employer Reporting functions (how public school employers report public school employee information to PSERS) and Employer Accounting functions (how employer and member contribution billing and payment information is maintained), the Member Accounting functions (how member account information is maintained), and the Statement of Account functions (how member account information is reported to members).

PSERS is in the final stages of developing and testing of the remaining core benefit processing functions. Core benefit processing functions include such items as retirement estimates, the retirement benefit calculations, and death benefit and refund calculations. The target is to have the complete system implemented early in 2007. At that point, PSERS will move into the maintenance and enhancement phase of the overall system, which is where work on an ongoing basis to fine-tune the new system and eventually add features and functions that will further benefit the employers and members will occur.

#### **Performance Audit and Fiduciary Review of Investment Operations**

During FY 2006 PSERS underwent a performance audit and fiduciary review of its investment program and operations by the Auditor General and Independent Fiduciary Services, Inc. (IFS), respectively. The results were announced in September of 2006. IFS stated that PSERS' practices are generally in line with best practices in terms of PSERS' overall governance, administration and management of its investment program. The Auditor General stated that the fund appears to be managed by a staff of qualified professionals who are committed to

maximizing return on investments while at the same time protecting the interests of the members.

Both the Auditor General and IFS made recommendations for improvement, principally with respect to documentation and written procedures. PSERS will be addressing those recommendations during FY 2007.

### **Independent Accounting Book of Record Project**

The System continued its multi-year project to implement an independent accounting book of record for the System's investment transactions and holdings. In FY 2006, the System completed its conversion of all public market portfolios to its internal accounting software provided by Financial Control Systems, Inc. and began work on converting its real estate and alternative investment portfolios from an Excel-based accounting system to the internal accounting software. The System expects to complete the conversion of all remaining portfolios and develop various management reports in 2007.

### **PSERS Health Options Program (HOP) — and Medicare Prescription Drug Benefits**

In 2006, PSERS operated the largest Employer/Union Direct Medicare Prescription Drug Program in the country. PSERS offered two Medicare Prescription Drug Plans through its Health Option Program (HOP). In May 2006, PSERS issued a request for proposal to the public and subsequently awarded a contract for a Pharmacy Benefits Management Service to be effective January 1, 2007.

PSERS conducted the annual option selection period from early October to November 15, 2006 for benefit coverage effective January 1, 2007. This open selection period allowed HOP participants to change their coverage options for the 2007 calendar year.

### **Financial Highlights**

The System maintains a full accrual accounting system. More specific accounting information is detailed in the **Summary of Significant Accounting Policies (Note 2)** in the notes to the financial statements found in the **Financial Section** of this report.

The System has established policies and procedures for the review and verification of all payments made by PSERS.

The fair value of the System's net assets totaled \$57.4 billion as of June 30, 2006. The System is the 14th largest public pension fund in the nation and the 21st largest among public and corporate pension funds in the nation. More specific information on the System's assets is detailed in the Statements of Plan Net Assets and Management's Discussion and Analysis included in the **Financial Section** of this report.

The System's administrative budget request is appropriated by the Pennsylvania General Assembly and funded by the investment income of the System. For FY 2006, the appropriation was \$39.5 million.

### **Funding**

Funding is the process of specifically setting aside money for current and future use. Proper funding entails an actuarial examination of the fund balances to ensure money will be available for future and current benefit payments.

The results of the latest published actuarial valuation (as of June 30, 2005) indicated that the rates of contribution payable by the members and employers, when taken together with the current assets of the System, are adequate to fund the actuarial liabilities on account of all benefits payable under the System at that date. The actuarial valuation measures the progress toward funding pension obligations of the System by comparing the actuarial assets to the actuarial

liabilities of the System. The funded status as of the latest actuarial valuation was 83.6%. Additional comparative information on the funded status of PSERS can be found in the **Actuarial Section** and MD&A in the **Financial Section** of this report.

### **Investments**

Income from the investment portfolio represents the major source of revenue to the System, accounting for nearly 79% of total revenues over the period from FY 1997 to FY 2006. During FY 2006 net investment income was \$7.9 billion. The investment portfolio totaled \$58.7 billion, at fair value, as of June 30, 2006. For FY 2006, the time-weighted rate of return on the System's investments was 15.26%.

The investment portfolio is well diversified to emphasize a long-term investment approach. The overall objective of the System is to provide benefits to its members through a carefully planned and well-executed investment program. The return objectives are to (i) realize a return sufficient to achieve funding adequacy on an inflation-adjusted basis and that exceeds the Policy Index (the Policy Index is a custom benchmark based on the Board-established asset allocation structure to generate a return that meets or exceeds the actuarial rate of return assumption); and (ii) invest the assets to maximize returns for the level of risk taken. The risk objectives are to (i) diversify the assets of the System to minimize the risk of losses within any one asset class, investment type, industry or sector distribution, maturity date, or geographic location; and (ii) invest the assets so that the probability of investment losses (as measured by the Policy Index) in excess of 12.0% in any one year is no greater than 2.5% (or two standard deviations below the expected return).

Additional information on the System's investments is contained in the **Investment Section** of this report.

### **Federal and State Tax Status**

The System is a qualified trust fund under Section 401(a) of the Internal Revenue Code (IRC). As a result of the qualified status, the trust fund is entitled to an exemption, under Section 501(a) of the IRC, from federal income taxation on its investment earnings. Additionally, contributions made on behalf of the active members are tax deferred under Section 414(h) of the IRC. The trust fund and any benefits accruing to the members of PSERS are exempt from Pennsylvania state and municipal taxes.

### **Professional Services**

Professional consultants are appointed by the Board of Trustees to perform services essential to the efficient operation of the System. An annual audit by an independent certified public accounting firm and annual valuation by an actuarial consultant attest to the financial and actuarial soundness of PSERS. The investment performance of the System is reviewed by an investment evaluation firm on a quarterly basis. The consultants providing services to the System are listed in the **Financial Section** and **Investment Section** of this report.

### **Other Information**

In compliance with the Retirement Code, actuarial tables and the computational procedures used by the System in calculating annuities and other benefits were published in the *Pennsylvania Bulletin* (Vol. 31, No.14). This information can be found on the World Wide Web at <http://www.pabulletin.com/secure/data/vol31/31-14/index.html>.

### **System Awards**

#### **Government Finance Officers Association of the United States and Canada Certificate of Achievement for Excellence in Financial Reporting**

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a *Certificate of Achievement for Excellence in Financial Reporting* to PSERS for its *Comprehensive Annual Financial Report* for the fiscal year ended June 30, 2005 (FY 2005). The *Certificate of*

*Achievement* is a prestigious national award recognizing conformance with the highest standards for preparation of state and local government financial reports. To be awarded a *Certificate of Achievement*, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report, whose contents conform to program standards. Such a comprehensive annual financial report must satisfy both generally accepted accounting principles and applicable legal requirements.

A *Certificate of Achievement* is valid for a period of one year only. PSERS has received a *Certificate of Achievement* for 23 consecutive years for FY 1983 to FY 2005. The System believes the current report continues to conform to the *Certificate of Achievement* program requirements and will be submitting this report to GFOA to determine eligibility for the 2006 certificate.

A reproduction of this award appears in this **Introductory Section** of this report. Its attainment represents a significant accomplishment by the System, whose Office of Financial Management holds general responsibility for the compilation and validity of the financial data presented in the *Comprehensive Annual Financial Report*.

### **Public Pension Coordinating Council – Public Pension Standards Award**

The Public Pension Coordinating Council has awarded its Public Pension Standards Award to PSERS for 2006. This award is in recognition of meeting professional standards for plan design and administration as set forth in the Public Pension Standards.

The Public Pension Coordinating Council was formed in 1990 to assist the public employee retirement community. The Council is composed of representatives from three national associations whose members are directly involved in the administration of public employee retirement systems: the National Association of State Retirement Administrators (NASRA); the National Conference on Public Employee Retirement Systems (NCPERS); and the National Council on Teacher Retirement (NCTR).

A reproduction of this award appears in the **Introductory Section**.

### **Acknowledgements**

The preparation of this report reflects the combined efforts of PSERS staff under the direction of the PSERS Board. It is intended to provide complete and reliable information in conformance with accepted standards and to document responsible stewardship of the System's assets.

Respectfully submitted,



Jeffrey B. Clay  
Executive Director



Arthur J. Granito  
Chief Financial Officer

## Administrative Organization PSERS Board of Trustees



Secretary of  
Education  
**Gerald R.  
Zahorchak**  
Acting Secretary  
(*ex officio*)



Executive Director  
Pennsylvania School  
Boards Association  
**Thomas J. Gentzel**  
(*ex officio*)



Treasurer of the  
Commonwealth of  
Pennsylvania  
**Honorable  
Robert P. Casey, Jr.**  
(*ex officio*)



Two members appointed by the Governor  
**Arthur J. Rooney, II** **Tina Byles-Williams**



One member elected  
by retired members  
**Sally J. Turley**



Three members elected by active certified contributors  
**Gerald A. Katona**



**Roger H. May**  
*Chair*



**Melva S. Vogler**



One member elected  
by active noncertified  
contributors  
**Susan L. Clapper**



Two members appointed by the Speaker of the  
Pennsylvania House of Representatives  
**Honorable  
Dwight Evans**



**Honorable  
Steven R. Nickol**  
*Vice-Chair*



One member elected  
by members of  
Pennsylvania Public  
School Boards  
**Richard N. Rose**



Two members appointed by the President  
*Pro Tempore* of the Pennsylvania Senate  
**Honorable  
Vincent J. Fumo**



**Honorable  
Joseph B.  
Scarnati, III**

## PSERS Board of Trustees

as of January 20, 2006

### **Treasurer of the Commonwealth of Pennsylvania (ex officio)**

Honorable Robert P. Casey, Jr.

### **Secretary of Education of the Commonwealth of Pennsylvania (ex officio)**

Dr. Gerald R. Zahorchak, Acting Secretary

### **Executive Director of the Pennsylvania School Boards Association, Inc. (ex officio)**

Mr. Thomas J. Gentzel

### **Two members appointed by the Governor of the Commonwealth of Pennsylvania**

Mr. Arthur J. Rooney, II (term expires 12/31/2006)

Ms. Tina Byles-Williams (term expires 12/31/2008)

### **Three members elected from among the certified contributors of the System for a term of three years**

Mr. Gerald A. Katona, (term expires 12/31/2007)

Mr. Roger H. May, *Chairman* (term expires 12/31/2006)

Ms. Melva S. Vogler (term expires 12/31/2008)

### **One member elected from among the noncertified contributors of the System for a term of three years**

Ms. Susan L. Clapper (term expires 12/31/2006)

### **One member elected from among the annuitants of the System for a term of three years**

Mrs. Sally J. Turley (term expires 12/31/2007)

### **One member elected by the members of Pennsylvania Public School Boards from among their number for a term of three years**

Mr. Richard N. Rose (term expires 12/31/2008)

### **Two members appointed by the Speaker of the House from the Pennsylvania House of Representatives, one representing the Majority Party and one representing the Minority Party**

Honorable Dwight Evans (term expires 02/05/2007)

Honorable Steven R. Nickol, *Vice-Chairman* (term expires 02/05/2007)

### **Two members appointed by the President Pro Tempore of the Pennsylvania Senate, one representing the Majority Party and one representing the Minority Party**

Honorable Vincent J. Fumo (term expires 02/05/2009)

Honorable Joseph B. Scarnati, III (term expires 02/05/2009)



## 2006 Board Committees

as of February 28, 2006

### Appeals / Member Services

Ms. Clapper, Chair  
 Mr. Gentzel  
 Mr. Katona  
 Mr. May  
 Rep. Nickol  
 Mr. Rose  
 Mrs. Turley

### Health Care

Mrs. Turley, Chair  
 Ms. Clapper  
 Mr. Gentzel  
 Mr. Katona  
 Mr. May  
 Rep. Nickol  
 Mr. Rose

### Finance

Ms. Vogler, Chair  
 Committee is comprised  
 of all Board members.

### Elections

Sen. Scarnati, Chair  
 Rep. Evans  
 Mr. Rooney  
 Dr. Zahorchak

### Audit / Budget

Mr. Rose, Chair  
 Rep. Evans  
 Sen. Fumo  
 Mr. Gentzel  
 Mr. Rooney  
 Sen. Scarnati  
 Ms. Vogler

### Personnel

Mr. Gentzel, Chair  
 Ms. Byles-Williams  
 Mr. Casey  
 Ms. Clapper  
 Rep. Evans  
 Mr. May  
 Dr. Zahorchak

### Bylaws / Policy

Rep. Nickol, Chair  
 Ms. Byles-Williams  
 Mr. Casey  
 Rep. Evans  
 Mr. Katona  
 Mrs. Turley  
 Ms. Vogler

### Technology Steering

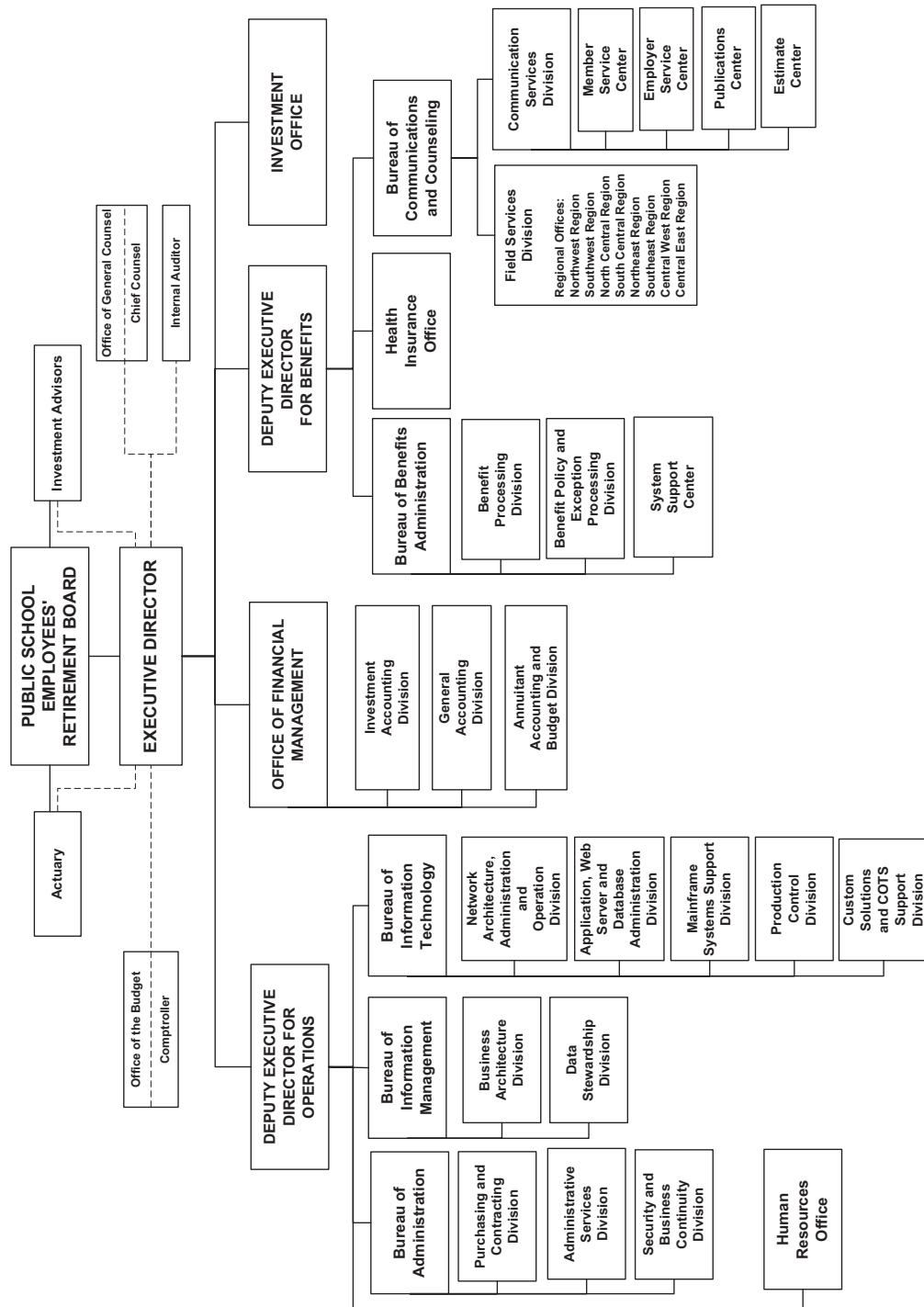
Sen. Fumo, Chair  
 Ms. Byles-Williams  
 Rep. Evans  
 Mr. Katona  
 Sen. Scarnati  
 Ms. Vogler  
 Dr. Zahorchak

### Corporate Governance

Mr. Katona, Chair  
 Ms. Byles-Williams  
 Mr. Casey  
 Rep. Evans  
 Mr. May  
 Mr. Rose  
 Ms. Vogler

NOTE: The chair of the Board of Trustees is a voting *ex-officio* member of all committees.

# Organizational Chart of the Public School Employees' Retirement System



## Organizational Structure of the Public School Employees' Retirement System

### Executive Office

The Executive Office is responsible for the overall management of the Public School Employees' Retirement System (PSERS) to achieve the primary objectives of the Fund as established by the Board of Trustees (Board). Reporting directly to the Executive Director are the Deputy Executive Director for Operations, Deputy Executive Director for Benefits, Chief Investment Officer, Chief Financial Officer, Internal Auditor, Press Secretary, Board Liaison, and Legislative Liaison. The Executive Director serves as chief executive officer responsible for the establishment, installation, and maintenance of modern management techniques to provide an efficient control of funds for and services to the active members and annuitants of the System.

The Executive Office monitors the operation of the investment portfolio and evaluates portfolio performance for consideration by the Board, certifies expenditures of the Fund, and measures performance of professional individuals or firms with whom the Board contracts for specialized services. The Executive Office also apprises the Board of any development that will in any way affect the System and its operation.

### Investment Office

The Investment Office is responsible for the investment activities of the System. In accordance with the investment policy established by the Board, PSERS' investment assets are allocated to numerous external professional investment advisors and internal investment professionals. Refer to the **Investment Section** Pages 81 to 86 for lists of professional investment advisors and Page 64 in the **Financial Section** for a summary of investment expenses.

### Office of Chief Counsel

Legal services are provided by a team of professional personnel under the Governor's

Office of General Counsel. The legal staff is responsible for representing the System in all administrative hearings and other litigation matters and providing counsel on a wide variety of matters including the interpretation of the Retirement Code, the form and legality of all System contracts, corporate governance issues and the structure and implementation of the System's varied financial investments.

### Internal Auditor's Office

The Internal Auditor's Office performs systematic reviews of the various activities of PSERS, testing for compliance with applicable laws, policies and procedures. The Internal Auditor makes recommendations on the improvement of the System's internal control system.

### Office of Financial Management

The Office of Financial Management has responsibility for planning, organizing and directing a complete accounting and financial reporting system in conformance with accounting principles generally accepted in the United States of America. Oversight is provided for new systems development and maintenance of existing systems, and ensuring appropriate accounting controls. The Office is the liaison for other state and federal agencies, reporting units, financial consultants, actuaries, and investment advisors for all accounting matters. The Office is organized into three divisions: General Accounting, Annuitant Accounting and Budget, and Investment Accounting.

### ***General Accounting Division***

The General Accounting Division has the responsibility of recording all financial transactions for the pension and health care operations of the system. It maintains PSERS' General Ledger, audits and processes administrative expenses, and prepares interim and annual financial statements. It bills and collects contributions due to the Fund from its employers. It provides

accounts receivable services to the System for member debts. It also interacts with the other divisions in the Office of Financial Management to assure that the basic financial statements of the System include all financial activity monitored and controlled by those accounting divisions.

### ***Annuitant Accounting and Budget Division***

The Annuitant Accounting and Budget Division analyzes, controls and issues the System's benefit payments to retirees, members and other parties such as beneficiaries and the IRS. The Division also has the responsibility of monitoring and recording Postemployment Healthcare transactions. It reconciles and monitors the financial activities of the third party administrator of the Health Options Program. Additionally, the Division is responsible for developing and monitoring the System's annual budget.

### ***Investment Accounting Division***

The Investment Accounting Division (IAD) has responsibility for processing, monitoring, and recording all investment transactions. It contracts with a third-party application service provider to assist with monitoring the overall internal control structure for investments and assure adequate custody of all investment assets. It serves as intermediary with the custodian bank, the State Treasury Department, brokers, investment managers, the investment evaluator, and investment consultants. It audits and approves investment expenses, prepares monthly investment financial reports and processes all investment funding allocations.

The IAD is also responsible for directing and administering the Class Action Revenue Recovery, the Foreign Cash Overdraft and the Foreign Tax Reclaim Collection programs as part of PSERS' investment activities. It also supports PSERS' Investment Office and the Board in achieving investment objectives and monitoring compliance with investment policy. The Division is comprised of the Public Market Reporting and Analysis, Special Investment Reporting and Analysis, and Treasury and Manager Administration sections.

## **Deputy Executive Director, Operations**

The Deputy Executive Director for Operations administers the facilities, technologies, data and records, policies and procedures, human resource, and procurement activities necessary to support, secure and optimize agency operations. Organizational units overseen by this position include the Bureau of Administration, Bureau of Information Management, Bureau of Information Technology, and the Human Resources Office.

### ***Human Resources Office***

The Human Resources Office is responsible for supporting management and staff to facilitate the accomplishment of the agency's mission. It administers all human resources programs and ensures compliance with labor law and Commonwealth regulations. Programs include position classification, labor relations, recruitment and placement, employee benefits, employee compensation and pay, training and staff development, time and attendance, performance management, organizational development and support, employee transactions, Equal Employment Opportunity and other miscellaneous programs.

### ***Bureau of Administration***

The Bureau of Administration provides facilities, purchasing and contracting, business continuity, automotive, mail, imaging, and other administrative services necessary to support agency functions.

### ***Purchasing and Contracting Division***

The Purchasing and Contracting Division procures materials, supplies, and services needed to support organizational goals and develops, monitors, processes and evaluates contract usage in the agency.

### ***Administrative Services Division***

The Administrative Services Division manages building and grounds for the agency both at headquarters and at the regional locations, provides mail, imaging, and work introduction

services to the agency, asset management, automotive and other administrative services to the agency.

### ***Security and Business Continuity Division***

The Security and Business Continuity Division develops and implements those policies, programs and procedures necessary to ensure that PSERS' human, technology, and capital resources are secure and to ensure that PSERS is prepared to quickly recover and continue critical operations in the event of a disaster.

### **Bureau of Information Management**

PSERS' organization, business processes, data, and information systems are inextricably intertwined with each other. To understand PSERS' business, as it exists, as well as the impact of change and potential for improvements, each of these components must be understood on their own, within the context of each other, and in context of PSERS' mission, vision, values and goals.

The goal of the Bureau of Information Management is to understand, analyze, document, and improve PSERS' organization, business rules, processes, information systems, and data and the relationships among these components so that PSERS is able to:

- conduct its business consistently and according to established rules
- understand each component, its relationship to each of the other components and to PSERS' mission, vision, values and goals
- fully, yet quickly analyze and understand the impact of potential change to one or more of these components on the others
- more effectively identify inefficient, duplicate, or suspect processes, data, or technologies
- account for its organization, business rules and processes, information systems and technologies, and data
- best manage its electronic data records, imaged records, paper and film/fiche records
- understand the meaning and know the

location of its data

- ensure that PSERS' data, information systems, and business processes meet established quality goals
- manage PSERS' forms
- ensure that PSERS' data, forms, information systems, and business processes are in support of its business.

### ***Division of Business Architecture***

The Division of Business Architecture includes analysts who collect, analyze, and document PSERS' organization, business rules, processes, information systems, and data, and perform detailed impact analysis as and when change is proposed. Additionally, staff in this unit confirm that changes have been applied correctly. Staff in this unit also look for opportunities for improvement, lead the development of business requirements and serve as liaisons between PSERS' end-users and Information Technology staff.

This division serves as the repository for PSERS' business knowledge and makes that knowledge available and understandable to agency processing and technology staff.

This division also receives and responds to data queries from agency staff and investigates system, data, or process problems. Finally, this division maintains responsibility for PSERS' records and forms management programs.

### ***Division of Data Stewardship***

PSERS has realized that poor data quality and/or the lack of data can be a significant inhibitor to timely and efficient processing. Staff in the Division of Data Stewardship are the trustees and primary maintainers of PSERS' member and employer data, working to make this data most usable to agency processing staff. Specifically, this group maintains PSERS' member demographic information, affiliate information, and is responsible for correctly applying monetary and non-monetary adjustments to member accounts.

### **Bureau of Information Technology**

The Bureau of Information Technology is responsible for planning, coordinating,

administering, implementing, and supporting information technology resources within PSERS. The Bureau is organized into five Divisions: Network Architecture, Administration, and Operation Division; Application, Web Server, and Database Administration Division; Mainframe Systems Support Division; Production Control Division; and Custom Solutions and COTS Support Division.

### ***Network Architecture, Administration, and Operation Division***

This division provides consultative and technical support in the planning, design, specification, implementation, deployment, operation, support, and troubleshooting of all PSERS' Network Servers, Desktop Systems, Operating Systems and associated Hardware Components.

### ***Application, Web Server, and Database Administration Division***

This division provides consultative and technical support in the planning, design, specification, implementation, deployment, operation, support, and troubleshooting of all PSERS' Database Management systems, Web Application servers and Web servers.

### ***Mainframe Systems Support Division***

The Mainframe Systems Division maintains the legacy COBOL and LINC mainframe business applications and for the development of data migration import and export programs and interface programs resident on the legacy mainframe platform.

### ***Production Control Division***

The Production Control Division develops job control programs, maintains mainframe system batch schedules, and controls the movement of legacy programs into the production environment. This division also manages the agency printing and post-processing operations.

### ***Custom Solution and Commercial off the Shelf (COTS) Division***

The Custom Solution and COTS Division supports PSERS' server-based COTS applications such as E-image and Workflow, Lawson General Ledger, Investment Accounting, etc. and for supporting the use of the Microsoft Office Suite in combination with data access tools such as Open/A. This division also designs, develops, tests and implements customized interfaces necessary to support the interaction between various COTS and custom business applications.

### **Deputy Executive Director, Benefits**

The Deputy Executive Director for Benefits oversees the administration of the benefits programs for all active and retired members of the System and oversees the development and implementation of the communications and counseling programs. Organizational units under the management of the Deputy include the Bureau of Benefits Administration, the Bureau of Communications and Counseling and the Health Insurance Office.

### **Bureau of Benefits Administration**

The Bureau of Benefits Administration provides professional and technical services to all Pennsylvania full-time and part-time public school employees in any of the System's 733 employers. They also provide services to retirees, their beneficiaries and their personal representatives.

### ***Benefits Processing Division***

The Benefits Processing Division handles the high volume of benefit calculations. The staff calculates estimated retirement benefits, creates payroll records, and originates the initial benefit payments and direct rollovers. As the employers report final salary and service data, staff conducts in-depth reviews of accounts and calculates finalized benefits.

This division has responsibility for determining eligibility and calculating the cost to the members

and to the employers for the purchase of additional service credit. The division processes requests to refund contributions and interest from members terminating from the system who are not eligible for retirement benefits. The calculation and payment of death benefits for members who die subsequent to retirement is also performed within this division.

### ***Benefits Policy and Exception Processing Division***

The Benefit Policy and Exception Processing Division has responsibility for creating and writing all benefits policies, procedures, business rules and calculations and presenting policies to the Executive staff and the Board's Appeals/ Members Services Committee; for coordinating all requests for legal analyses and legal opinions; and for working with the System's actuaries regarding benefit calculations and audits. The staff also manages the first level of the member's administrative appeal process.

This division makes determinations relative to membership eligibility, retirement covered compensation and emergency employment where circumstances are suspect or atypical. To insure compliance with the Retirement Code, the division is also responsible for the review and approval of domestic relations orders.

The staff of this division also handles the benefits determinations that are more complex, more time-sensitive or have a significant impact on the agency or the members. This work includes divorce transactions, death benefits for in-service members, frozen annuity calculations, computations that must comply with special IRS regulations, multiple service eligibility and calculations, post finalized benefit adjustments, calculating cost of living increases and processing changes to annuitant or survivor gross benefits.

### ***System Support Center***

The System Support Center's primary responsibility is to work with technical staff in the Bureau of Information Technology to enhance automated business systems and the use of technology within the business areas. Enhancements are the result of changing

technology as well as changes to legislation, court decisions and board policies. Work involves workflow analysis, requirements definition, testing and implementation. The Center is also responsible for reporting and providing assistance to resolve all problems with production, hardware and software.

### **Bureau of Communications & Counseling**

The Bureau of Communications and Counseling is responsible for professionally communicating accurate and timely information. The goal is to promote the understanding of PSERS' benefits and processes to the members, the employers, the Legislature, the Governor's Office, other government organizations, professional organizations and the public.

### ***Field Services Division***

The Field Services Division provides services to both active and retired PSERS' members through eight regional offices located throughout the Commonwealth of Pennsylvania. The regional representatives conduct various meetings and workshops for members and employers and provide counseling services.

### ***Communication Services Division***

The Communication Services Division provides information to the members, employers, and the general public through the telephone, on-site visits, the worldwide web and various publications. There are four centers within this division:

#### **Member Service Center**

This center answers the PSERS' toll-free telephone number, responding to general inquiries about the benefits and processes of the System as well as specific inquiries related to members' accounts.

#### **Employer Service Center**

Staffing of the center includes customer service representatives to answer phone calls and emails,

as well as field representatives to visit employers and conduct workshops, to provide assistance and training for proper reporting to the System.

### **Publications Center**

This center is responsible for the development, production, and distribution of all printed and audiovisual materials for the System. Publications include newsletters, handbooks, pamphlets, annual reports, mass communications to the membership, and presentation material. Staff also responds to general correspondence and email inquiries.

### **Estimate Center**

This center computes a large volume of estimates showing the potential monthly benefits members will receive at retirement through the normal, early, vested or disability benefit.

### **Health Insurance Office**

This office is responsible for all aspects of the PSERS' Health Options Program and administering the annuitants' health insurance premium assistance benefits. HOP is a voluntary statewide plan that provides group health insurance coverage for school retirees, their spouses, and eligible dependents.



## Administrative Staff



**Jeffrey B. Clay**  
Executive Director



**Gerald Gornish**  
Chief Counsel



**Arthur J. Granito**  
Chief  
Financial Officer



**Terrill J. Savidge**  
Deputy Executive  
Director, Operations



**Veronica P. Thomas**  
Deputy Executive  
Director, Benefits



**Alan H. Van Noord**  
Chief  
Investment Officer



**Douglas A. Bonsall**  
Director of  
Communications &  
Counseling



**Deborah L. Garraway**  
Director of Information  
Management



**Donald J. Halke, II**  
Internal Auditor



**Helen D. Hosler**  
Director of Benefits  
Administration



**Maribel La Luz**  
Director of Human  
Resources



**James F. Noone**  
Director of  
Administration



**Mark F. Shafer**  
Director of Health  
Insurance

# PSERS REGIONAL OFFICES

**NORTHWEST**

Penn Wood Center, Suite C  
 464 Allegheny Blvd.  
 Franklin, PA 16323-6210  
 Local (814) 437-9845  
 FAX (814) 437-5826  
**Toll Free 1-888-773-7748 ext. 5175**

**NORTHCENTRAL**

Suite 201  
 300 Bellefonte Avenue  
 Lock Haven, PA 17745-1903  
 Local (570) 893-4410  
 FAX (570) 893-4414  
**Toll Free 1-888-773-7748 ext. 5275**

**NORTHEAST**

Market Street Victorian Square  
 33 S Wilkes Barre Blvd., Suite 20  
 Wilkes Barre, PA 18702-5144  
 Local (570) 826-2003  
 FAX (570) 820-4868  
**Toll Free 1-888-773-7748 ext. 5375**

**SOUTHWEST**

900 Sarah Street, Suite 208  
 Pittsburgh, PA 15203-1106  
 Local (412) 488-2031  
 FAX (412) 488-2338  
**Toll Free 1-888-773-7748 ext. 5775**

**SOUTHEAST**

605 Louis Drive, Suite 500  
 Warminster, PA 18974-2825  
 Local (215) 443-3495  
 FAX (215) 443-3487  
**Toll Free 1-888-773-7748 ext. 5575**



**CENTRALWEST**

636 Scalp Avenue  
 Johnstown, PA 15904-1640  
 Local (814) 262-7715  
 FAX (814) 262-7625  
**Toll Free 1-888-773-7748 ext. 5875**

**SOUTHCENTRAL**

Three Crossgate Drive, Suite 101  
 Mechanicsburg, PA 17050-2459  
 Local (717) 795-9270  
 FAX (717) 795-9281  
**Toll Free 1-888-773-7748 ext. 5675**

**CENTRALEAST**

110 West Arch Street, Suite 204  
 Fleetwood, PA 19522-1321  
 Local (610) 944-9113  
 FAX (610) 944-9275  
**Toll Free 1-888-773-7748 ext. 5475**

## PSERS Headquarters Building



The headquarters of the Public School Employees' Retirement System is located at 5 North Fifth Street in downtown Harrisburg, Pennsylvania within the State Capitol complex. Regional field offices are also maintained in Fleetwood, Franklin, Johnstown, Lock Haven, Mechanicsburg, Pittsburgh, Warminster and Wilkes Barre.

The building was built and first occupied by the Retirement System in 1987 and is its first home built specifically for its use. It is owned by the Five North Fifth Street Corporation, a holding entity formed by PSERS, and is managed by Property Management Inc.

Public School Employees' Retirement System

# Financial Section





### Independent Auditor's Report

The Board of Trustees  
Public School Employees' Retirement System  
Harrisburg, Pennsylvania

We have audited the accompanying basic financial statements of the Public School Employees' Retirement System (PSERS), a component unit of the Commonwealth of Pennsylvania as of and for the years ended June 30, 2006 and 2005, as listed in the table of contents. These financial statements are the responsibility of the PSERS' management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, PSERS' plan net assets as of June 30, 2006 and 2005, and the changes in its plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis and Required Supplemental Schedules of Funding Progress and Employer Contributions (Schedules 1 and 2) are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The Supplemental Schedules 1 through 3 are presented for purposes of additional analysis and are not a required part of the basic financial statements. Supplemental Schedules 1 through 3 have been subjected to the auditing procedures applied in the audit of the basic financial statements, and, in our opinion, are presented fairly, in all material respects, in relation to the basic financial statements taken as a whole.

*Clifton Gunderson LLP*

Baltimore, Maryland  
September 28, 2006

Offices in 15 states and Washington, DC



## Management's Discussion and Analysis

Management's Discussion and Analysis (MD&A) of the Commonwealth of Pennsylvania Public School Employees' Retirement System's (PSERS) for the fiscal year ended June 30, 2006, provides a narrative summary of PSERS' financial position and performance, including highlights and comparative data. The MD&A is presented as required supplemental information to the financial statements and should be read in conjunction with the letter of transmittal, the financial statements, the notes to financial statements and the supplementary schedules.

### Overview of Financial Statements

PSERS is primarily responsible for administering a defined benefit pension plan for public school employees in the Commonwealth of Pennsylvania. PSERS also administers two postemployment healthcare programs, the Health Insurance Premium Assistance Program (Premium Assistance) and the Health Options Program (HOP), for its annuitants. The financial statements present the financial activities for the pension plan and the two postemployment healthcare programs.

The *Statements of Plan Net Assets* provide a snapshot of the financial position of PSERS at June 30, 2006, including comparative amounts for the prior year.

The *Statements of Changes in Plan Net Assets* summarize PSERS' financial activities that occurred during the fiscal period from July 1, 2005 to June 30, 2006, including comparative amounts for the prior year.

The *Notes to Financial Statements* provide additional information that is essential to a full understanding of the financial statements. The notes are an integral part of the financial statements and include detailed information not readily evident in the basic financial statements.

The *Required Supplemental Schedules* immediately following the notes to financial statements provide two schedules showing historical information concerning the funded status of PSERS and the employer contributions.

The remaining supplemental schedules provide additional detailed information concerning the operating expenses, investment expenses and payments to non-investment consultants. All of this supplemental information is considered useful in understanding and evaluating the financial activities of PSERS.

### Financial Highlights

- PSERS' total plan net assets increased by \$5.3 billion from \$52.1 billion at June 30, 2005 to \$57.4 billion at June 30, 2006, the highest fiscal year end total in PSERS' history. The increase is primarily attributable to net investment income and member and employer contributions combined that exceeded the payment of pension benefits and administrative expenses. The increase in plan net assets from \$48.5 billion to \$52.1 billion in the year ended June 30, 2005 was also attributed to net investment income and member and employer contributions combined that exceeded the payment of pension benefits and administrative expenses.

## Management's Discussion and Analysis (Continued)

- The pension plan's funded ratio as of the latest actuarial valuation dated June 30, 2005 decreased from 91.2% at June 30, 2004 to 83.6% at June 30, 2005. The decrease is primarily due to the residual effect of an actuarial asset loss caused by the downturn in the financial markets from 2001 to 2003. The funded ratio for the year ended June 30, 2003 was 97.2%.
- The rate of return on investments was 15.26% for the fiscal year ended June 30, 2006 (FY 2006), 12.87% for the fiscal year ended June 30, 2005 (FY 2005) and 19.67% for the fiscal year ended June 30, 2004 (FY 2004).
- Total member contributions increased from \$955 million in FY 2005 to \$983 million in FY 2006 due to a slight increase in the average member contribution percentage and an increase in the active member payroll. Total member contributions also increased between FY 2004 and FY 2005 because of the same factors.
- Total employer contributions increased from \$458 million in FY 2005 to \$531 million in FY 2006. The net increase is primarily attributable to an increase in the total employer contribution rate from 4.23% in FY 2005 to 4.69% in FY 2006. Total employer contributions increased from FY 2004 to FY 2005 due to an increase in the employer contribution rate from 3.77% to 4.23%.
- Total PSERS' benefit payouts increased by \$200 million from \$3.9 billion in FY 2005 to \$4.1 billion in FY 2006. The increase is primarily attributable to an increase in the number of retirees and beneficiaries currently receiving benefits. Benefit payouts also increased by \$400 million from FY 2004 to FY 2005 due to an increase in the number of retirees added to the payroll.
- Total administrative expenses increased by \$6 million from \$42.6 million in FY 2005 to \$48.6 million in FY 2006 primarily due to the carry-over of expenditures for the New Pension Administration System (NPAS) project and an increase in expenditures for the Health Options Program. Administrative expenses decreased by \$6.6 million between FY 2004 and FY 2005. Administrative expenses were within PSERS' budgeted amounts for each of the fiscal years.

### Funded Status

PSERS uses an actuarial reserve type of funding that is financed by member contributions, employer contributions and earnings from invested assets. An independent actuarial valuation of PSERS' actuarial assets and liabilities is performed annually. As part of this valuation, the progress toward funding pension obligations of PSERS is measured by comparing the actuarial value of assets to the actuarial accrued liability. This measurement is referred to as the funded ratio or funded status. The most recent actuarial valuation reports that PSERS is 83.6% funded as of June 30, 2005. The results of operations for FY 2006 will be reflected in the actuarial valuation for the year ended June 30, 2006. Due to the normal lag time for completion of the actuarial valuation, the resulting funded status will be available at the end of the 2006 calendar year and will be reported in the financial statements for the fiscal year ended June 30, 2007 (FY 2007).



## Management's Discussion and Analysis (Continued)

## Analysis of Plan Net Assets

<b><u>Summary of Plan Net Assets:</u></b>	<b><u>FY 2006</u></b>	<b><u>Increase (Decrease)</u></b>	<b><u>FY 2005</u></b>	<b><u>Increase (Decrease)</u></b>	<b><u>FY 2004</u></b>
<b>Assets:</b>					
Receivables	\$ 1,586,563	\$ 64,569	\$ 1,521,994	\$ 436,885	\$ 1,085,109
Investments	58,719,269	5,781,217	52,938,052	3,906,373	49,031,679
Securities lending collateral pool	6,337,173	(263,511)	6,600,684	2,095,256	4,505,428
Fixed assets	643	(230)	873	(641)	1,514
<b>Total Assets</b>	<b>\$ 66,643,648</b>	<b>5,582,045</b>	<b>61,061,603</b>	<b>6,437,873</b>	<b>54,623,730</b>
<b>Liabilities:</b>					
Payables and other liabilities	2,889,174	539,681	2,349,493	768,290	1,581,203
Obligations under securities lending	6,337,173	(263,511)	6,600,684	2,095,256	4,505,428
<b>Total Liabilities</b>	<b>9,226,347</b>	<b>276,170</b>	<b>8,950,177</b>	<b>2,863,546</b>	<b>6,086,631</b>
<b>Plan Net Assets</b>	<b>\$ 57,417,301</b>	<b>\$ 5,305,875</b>	<b>\$52,111,426</b>	<b>\$ 3,574,327</b>	<b>\$ 48,537,099</b>
<b><u>Summary of Changes in Plan Net Assets:</u></b>					
<b>Additions:</b>					
Contributions	\$ 1,527,730	\$ 114,413	\$ 1,413,317	\$ 62,173	\$ 1,351,144
Net investment income	7,942,639	1,861,142	6,081,497	(2,163,107)	8,244,604
<b>Total Additions</b>	<b>9,470,369</b>	<b>1,975,555</b>	<b>7,494,814</b>	<b>(2,100,934)</b>	<b>9,595,748</b>
<b>Deductions:</b>					
Benefit payments	4,115,865	238,023	3,877,842	380,477	3,497,365
Administrative expenses	48,629	5,984	42,645	(6,557)	49,202
<b>Total Deductions</b>	<b>4,164,494</b>	<b>244,007</b>	<b>3,920,487</b>	<b>373,920</b>	<b>3,546,567</b>
<b>Changes in Plan Net Assets</b>	<b>\$ 5,305,875</b>	<b>\$ 1,731,548</b>	<b>\$ 3,574,327</b>	<b>\$(2,474,854)</b>	<b>\$ 6,049,181</b>

## Investments

PSERS is a long-term investor and manages the pension fund with long-term objectives in mind. A primary element of PSERS' investment philosophy is that diversification among various asset classes is the best way to achieve its goals. PSERS makes estimates of future long-term market returns and establishes an asset allocation plan taking into account the risk associated with each asset class as well as the financial objectives of the Fund.

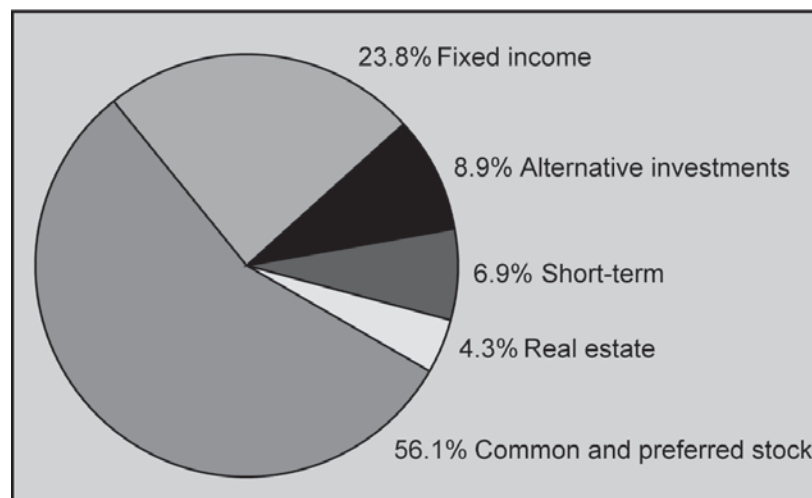
## Management's Discussion and Analysis (Continued)

For FY 2006, PSERS' rate of return on investments was 15.26%. The FY 2006 investment return exceeded PSERS' total fund policy index of 11.96% and placed PSERS' performance in the top ten percent of the Public Fund Universe prepared by the System's investment consultant, Wilshire Associates Inc. (Wilshire). The annualized rate of return over the past three and five-year periods ended June 30, 2006 was 15.90% and 8.67%, respectively. The annualized rate of return for the ten-year period ended June 30, 2006 was 9.47%, gross of fees. PSERS' long-term actuarial investment return assumption is 8.50%.

The asset distribution of PSERS' investment portfolio at June 30, 2006 and June 30, 2005, at fair value, including postemployment healthcare assets, was:

<b><u>Asset Class</u></b>	<b>(Dollar Amounts in Thousands)</b>			
	<b><u>2006</u></b>	<b><u>%</u></b>	<b><u>2005</u></b>	<b><u>%</u></b>
Short-term	\$ 4,061,926	6.9	\$ 4,337,012	8.2
Fixed income	13,962,196	23.8	13,470,565	25.5
Common and preferred stock	32,951,976	56.1	27,859,789	52.6
Real estate	2,542,399	4.3	2,285,617	4.3
Alternative investments	<u>5,200,772</u>	<u>8.9</u>	<u>4,985,069</u>	<u>9.4</u>
<b>Total</b>	<b><u>\$ 58,719,269</u></b>	<b><u>100.0</u></b>	<b><u>\$ 52,938,052</u></b>	<b><u>100.0</u></b>

### Asset Distribution At June 30, 2006



## Management's Discussion and Analysis (Continued)

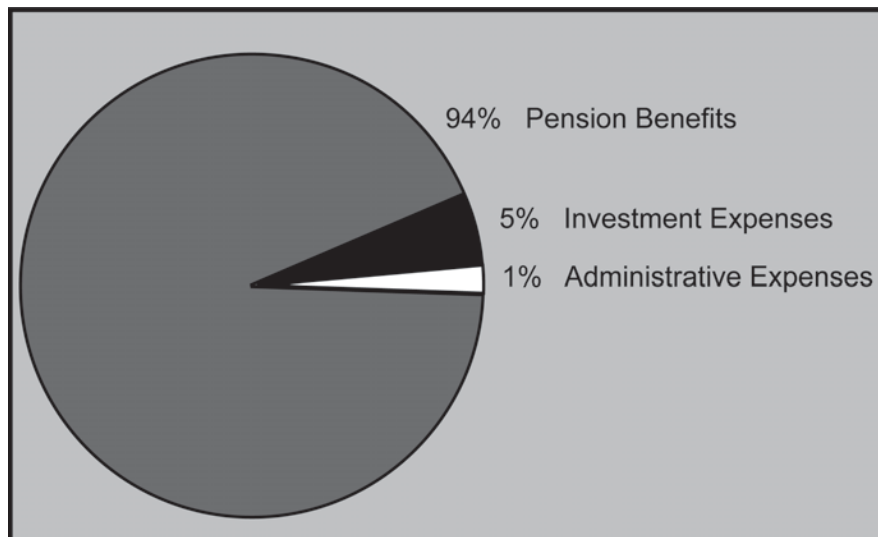
Short-term investments (cash and cash equivalents) at the close of FY 2006 decreased by \$200 million from \$4.3 billion in FY 2005 to \$4.1 billion in FY 2006 due primarily to a decrease in the short-term investments required to support futures contracts and changes in operational cash balances. Fixed income investments increased by \$500 million from \$13.5 billion in FY 2005 to \$14.0 billion in FY 2006 primarily as a result of several investment managers shifting a portion of their short-term investments to fixed income. Common and preferred stock investments increased by \$5.1 billion from \$27.9 billion in FY 2005 to \$33.0 billion in FY 2006. The increase was primarily due to positive returns in the domestic and international equity markets that were partially offset by reductions to the asset class during FY 2006 in accordance with PSERS' asset allocation plan. Real estate investments increased by \$200 million from \$2.3 billion in FY 2005 to \$2.5 billion in FY 2006. Alternative investments increased by \$200 million from \$5.0 billion in FY 2005 to \$5.2 billion in FY 2006 due to the addition of new investment partnerships, drawdowns of commitments to existing partnerships and market value appreciation. Real estate investments remained relatively consistent on a percentage basis over FY 2006.

### Contributions and Investment Income

Employer pension contributions increased by \$110.4 million from \$321.1 million in FY 2004 to \$431.5 million in FY 2005 and by \$25.4 million to \$456.9 million in FY 2006. The increases were attributable to the increase in the employer pension contribution rate from 2.98% in FY 2004 to 4.00% in FY 2005 and 4.00% in FY 2006. Member pension contributions increased by \$4.6 million from \$783.7 million in FY 2004 to \$788.3 million in FY 2005 and by \$39.3 million to \$827.6 million in FY 2006 as a result of the increase in the total participant salary base and the average member contribution percentage increasing from 7.08% in FY 2004 to 7.12% in FY 2005 and to 7.16% in 2006. The employer contributions for health insurance premium assistance increased by \$47.8 million from \$26.3 million in FY 2005 to \$74.1 million in FY 2006 due to the increase in the employer health insurance premium assistance contribution rate from 0.23% in FY 2005 to 0.69% in FY 2006. This followed a decrease in the employer health insurance premium assistance rate from 0.79% in FY 2004 to 0.23% in FY 2005. Contributions from the Centers for Medicare & Medicaid Services (CMS) are those funds received since PSERS became a Prescription Drug Plan (PDP) on January 1, 2006. Net investment income increased by \$1.8 billion from \$6.1 billion in FY 2005 to \$7.9 billion in FY 2006, which correlates to the increase in the investment rate of return from 12.87% for FY 2005 to 15.26% for FY 2006. The 15.26% investment return for FY 2006 placed PSERS' performance in the top ten percent of the Wilshire Public Fund Universe. The annual investment returns for FY 2005 and FY 2004 were also strong at 12.87% and 19.67%, respectively. Net investment income also includes investment expenses as a deduction. The "Total PSERS Benefits and Expenses" section that follows includes an analysis of investment expenses.

**Management's Discussion and Analysis (Continued)****Total PSERS' Benefits and Expenses**

The primary source of expense during FY 2006 was for the payment of benefits totaling \$4.1 billion. This compares to benefit payments of \$3.9 billion during FY 2005 and \$3.5 billion for FY 2004. Investment expenses increased by \$18.6 million from \$192.7 million in FY 2005 to \$211.3 million in FY 2006, consistent with the increase in the total Fund value. Investment expenses increased by \$1.4 million from \$191.3 million during FY 2004 to \$192.7 million during FY 2005. Investment expenses are reported as a reduction in net investment income on the Statement of Changes in Plan Net Assets. Administrative expenses increased by \$6.0 million from \$42.6 million during FY 2005 compared to \$48.6 million during FY 2006. The increase was primarily due to a carry-over of expenditures from FY 2005 to FY 2006 for the NPAS project. Administrative expenses for FY 2004 totaled \$49.2 million.

**Total PSERS' Benefits and Expenses  
Fiscal Year Ended June 30, 2006**

## Statements of Plan Net Assets

June 30, 2006 and 2005  
(Dollar Amounts in Thousands)

	2006			Totals
	Pension	Postemployment Healthcare		
		Premium Assistance	Health Options Program	
<b>Assets:</b>				
Receivables:				
Members	\$ 236,005	\$ 400	\$ 276	\$ 236,681
Employers	164,377	27,733	-	192,110
Investment income	193,699	300	353	194,352
Investment proceeds	960,102	224	-	960,326
Miscellaneous	2,357	737	-	3,094
<b>Total Receivables</b>	<b>1,556,540</b>	<b>29,394</b>	<b>629</b>	<b>1,586,563</b>
Investments, at fair value:				
Short-term	3,880,369	64,706	116,851	4,061,926
Fixed income	13,962,196	-	-	13,962,196
Common and preferred stock	32,951,976	-	-	32,951,976
Real estate	2,542,399	-	-	2,542,399
Alternative investments	5,200,772	-	-	5,200,772
<b>Total Investments</b>	<b>58,537,712</b>	<b>64,706</b>	<b>116,851</b>	<b>58,719,269</b>
Securities lending collateral pool	6,337,173	-	-	6,337,173
Capital assets (net of accumulated depreciation of \$10,402)	643	-	-	643
<b>Total Assets</b>	<b>66,432,068</b>	<b>94,100</b>	<b>117,480</b>	<b>66,643,648</b>
<b>Liabilities:</b>				
Accounts payable and accrued expenses	42,059	325	3,062	45,446
Benefits payable	159,390	811	11,709	171,910
Premium advances	-	-	13,852	13,852
Investment purchases and other liabilities	2,657,779	187	-	2,657,966
Obligations under securities lending	6,337,173	-	-	6,337,173
<b>Total Liabilities</b>	<b>9,196,401</b>	<b>1,323</b>	<b>28,623</b>	<b>9,226,347</b>
<b>Net assets held in trust for pension and postemployment healthcare benefits</b> (A schedule of funding progress is presented on Required Supplemental Schedule 1)	<b>\$57,235,667</b>	<b>\$ 92,777</b>	<b>\$ 88,857</b>	<b>\$57,417,301</b>

These financial statements should be read only in connection with the accompanying notes to financial statements.

## Statements of Plan Net Assets

June 30, 2006 and 2005

(Dollar Amounts in Thousands)

	2005			Totals
	Pension	Postemployment Healthcare		
		Premium Assistance	Health Options Program	
<b>Assets:</b>				
Receivables:				
Members	\$ 214,857	\$ 1,127	\$ 38	\$ 216,022
Employers	140,971	6,939	-	147,910
Investment income	176,712	678	168	177,558
Investment proceeds	974,114	-	-	974,114
Miscellaneous	6,100	281	9	6,390
<b>Total Receivables</b>	<b>1,512,754</b>	<b>9,025</b>	<b>215</b>	<b>1,521,994</b>
Investments, at fair value:				
Short-term	4,154,565	91,769	90,678	4,337,012
Fixed income	13,454,688	-	15,877	13,470,565
Common and preferred stock	27,859,789	-	-	27,859,789
Real estate	2,285,617	-	-	2,285,617
Alternative investments	4,985,069	-	-	4,985,069
<b>Total Investments</b>	<b>52,739,728</b>	<b>91,769</b>	<b>106,555</b>	<b>52,938,052</b>
Securities lending collateral pool	6,600,684	-	-	6,600,684
Capital assets (net of accumulated depreciation of \$10,084)	873	-	-	873
<b>Total Assets</b>	<b>60,854,039</b>	<b>100,794</b>	<b>106,770</b>	<b>61,061,603</b>
<b>Liabilities:</b>				
Accounts payable and accrued expenses	41,262	299	2,000	43,561
Benefits payable	214,634	57	12,756	227,447
Premium advances	-	-	14,122	14,122
Investment purchases and other liabilities	2,061,062	3,301	-	2,064,363
Obligations under securities lending	6,600,684	-	-	6,600,684
<b>Total Liabilities</b>	<b>8,917,642</b>	<b>3,657</b>	<b>28,878</b>	<b>8,950,177</b>
<b>Net assets held in trust for pension and postemployment healthcare benefits</b> (A schedule of funding progress is presented on Required Supplemental Schedule 1)	<b>\$51,936,397</b>	<b>\$ 97,137</b>	<b>\$ 77,892</b>	<b>\$52,111,426</b>

These financial statements should be read only in connection with the accompanying notes to financial statements.

## Statements of Changes in Plan Net Assets

Years ended June 30, 2006 and 2005

(Dollar Amounts in Thousands)

	2006			Totals
	Pension	Postemployment Healthcare Premium Assistance	Health Options Program	
<b>Additions:</b>				
Contributions:				
Members	\$ 827,647	\$ -	\$ 155,199	\$ 982,846
Employers	456,878	74,065	-	530,943
Centers for Medicare & Medicaid Services	-	-	13,941	13,941
Total contributions	<u>1,284,525</u>	<u>74,065</u>	<u>169,140</u>	<u>1,527,730</u>
Investment income:				
From investing activities:				
Net appreciation (depreciation) in fair value of investments	5,969,223	(480)	123	5,968,866
Short-term	129,788	3,362	3,641	136,791
Fixed income	694,449	-	439	694,888
Common and preferred stock	771,276	-	-	771,276
Real estate	285,333	-	-	285,333
Alternative investments	273,808	-	-	273,808
Total investment activity income	<u>8,123,877</u>	<u>2,882</u>	<u>4,203</u>	<u>8,130,962</u>
Investment expenses	(211,247)	(32)	-	(211,279)
Net income from investing activities	<u>7,912,630</u>	<u>2,850</u>	<u>4,203</u>	<u>7,919,683</u>
From securities lending activities:				
Securities lending income	270,447	-	-	270,447
Securities lending expense	(247,491)	-	-	(247,491)
Net income from securities lending activities	<u>22,956</u>	<u>-</u>	<u>-</u>	<u>22,956</u>
Total net investment income	<u>7,935,586</u>	<u>2,850</u>	<u>4,203</u>	<u>7,942,639</u>
<b>Total Additions</b>	<u>9,220,111</u>	<u>76,915</u>	<u>173,343</u>	<u>9,470,369</u>
<b>Deductions:</b>				
Benefits	3,860,658	79,298	151,117	4,091,073
Refunds of contributions	16,330	-	-	16,330
Net transfer to State Employees' Retirement System	8,462	-	-	8,462
Administrative expenses	35,391	1,977	11,261	48,629
<b>Total Deductions</b>	<u>3,920,841</u>	<u>81,275</u>	<u>162,378</u>	<u>4,164,494</u>
<b>Net increase (decrease)</b>	<u>5,299,270</u>	<u>(4,360)</u>	<u>10,965</u>	<u>5,305,875</u>
<b>Net assets held in trust for pension and postemployment healthcare benefits:</b>				
<b>Balance, beginning of year</b>	<u>51,936,397</u>	<u>97,137</u>	<u>77,892</u>	<u>52,111,426</u>
<b>Balance, end of year</b>	<u>\$ 57,235,667</u>	<u>\$ 92,777</u>	<u>\$ 88,857</u>	<u>\$ 57,417,301</u>

These financial statements should be read only in connection with the accompanying notes to financial statements.

## Statements of Changes in Plan Net Assets

Years ended June 30, 2006 and 2005

(Dollar Amounts in Thousands)

	2005			Totals
	Pension	Postemployment Healthcare Premium Assistance	Health Options Program	
<b>Additions:</b>				
Contributions:				
Members	\$ 788,310	\$ -	\$ 167,199	\$ 955,509
Employers	431,556	26,252	-	457,808
Total contributions	1,219,866	26,252	167,199	1,413,317
Investment income:				
From investing activities:				
Net appreciation (depreciation) in fair value of investments	4,463,930	(2,218)	672	4,462,384
Short-term	65,772	4,635	1,389	71,796
Fixed income	594,224	-	585	594,809
Common and preferred stock	676,549	-	-	676,549
Real estate	187,178	-	-	187,178
Alternative investments	265,355	-	-	265,355
Total investment activity income	6,253,008	2,417	2,646	6,258,071
Investment expenses	(192,629)	(48)	-	(192,677)
Net income from investing activities	6,060,379	2,369	2,646	6,065,394
From securities lending activities:				
Securities lending income	125,882	-	-	125,882
Securities lending expense	(109,779)	-	-	(109,779)
Net income from securities lending activities	16,103	-	-	16,103
Total net investment income	6,076,482	2,369	2,646	6,081,497
<b>Total Additions</b>	7,296,348	28,621	169,845	7,494,814
<b>Deductions:</b>				
Benefits	3,639,838	74,465	136,447	3,850,750
Refunds of contributions	16,233	-	-	16,233
Net transfer to State Employees' Retirement System	10,859	-	-	10,859
Administrative expenses	32,670	1,876	8,099	42,645
<b>Total Deductions</b>	3,699,600	76,341	144,546	3,920,487
<b>Net increase (decrease)</b>	3,596,748	(47,720)	25,299	3,574,327
<b>Net assets held in trust for pension and postemployment healthcare benefits:</b>				
<b>Balance, beginning of year</b>	48,339,649	144,857	52,593	48,537,099
<b>Balance, end of year</b>	\$ 51,936,397	\$ 97,137	\$ 77,892	\$ 52,111,426

These financial statements should be read only in connection with the accompanying notes to financial statements.



# Notes To Financial Statements

June 30, 2006 and 2005

## 1. Organization and Description of the System

### (a) Organization

The System was established on July 18, 1917, under the provisions of Pamphlet Law 1043, No. 343 as a governmental cost-sharing multiple-employer plan that provides retirement allowances and other benefits to its members. Membership in the System is mandatory for nearly all qualifying public school employees in the Commonwealth of Pennsylvania (Commonwealth). At June 30, 2006, there were 733 participating employers, generally school districts. Membership as of June 30, 2005, the most recent year for which actual amounts are available, consisted of:

Currently employed members:		
Vested	173,000	
Nonvested	<u>82,000</u>	
<b>Total currently employed members</b>		<b>255,000</b>
Retirees and beneficiaries currently receiving benefits	157,000	
Inactive members and vestees entitled to but not receiving benefits	<u>59,000</u>	
<b>Total retirees and other members</b>		<b><u>216,000</u></b>
<b>Total number of members</b>		<b><u>471,000</u></b>

All members are fully vested in their individual balance in the Members' Savings Account which is described in Note 3.

The System is established by state law as an independent administrative board of the Commonwealth, which is directed by the Public School Employees' Retirement Board (the Board) that exercises control and management of the System, including the investment of its assets. The System's board has fifteen members including the Commonwealth's Secretary of Education, the State Treasurer, the Executive Director of the Pennsylvania School Boards Association, two members appointed by the Governor, six elected members (three from among the System's certified members, one from among the System's non-certified members, one from among the System's annuitants, and one from among school board members in Pennsylvania), two members from the Senate, and two members from the House of Representatives.

The State Treasurer is the custodian of the System's fund. The retirement plan of the System is a contributory defined benefit plan for which the benefit payments to members and contribution provisions by employers and employees are specified in the Pennsylvania Public School Employees' Retirement Code (the Code). Changes in benefit and contribution provisions for the retirement plan must be made by legislation. Pursuant to state law, all legislative bills and amendments proposing to change the System's retirement plan are to be accompanied with an actuarial note prepared by an enrolled pension actuary providing an estimate of the cost and actuarial effect of the proposed change.

## Notes to Financial Statements (Continued)

Based upon the criterion of financial accountability as defined by governmental accounting standards, the System is considered a component unit of the Commonwealth of Pennsylvania financial reporting entity and is included in the Comprehensive Annual Financial Report of the Commonwealth of Pennsylvania.

### (b) Pension Benefits

Under the provisions of the 1975 revision of the Code by the Pennsylvania General Assembly, members are eligible for monthly retirement benefits upon reaching (a) age 62 with at least 1 year of credited service; (b) age 60 with 30 or more years of credited service; or (c) 35 or more years of service regardless of age.

Benefits are generally equal to 2% or 2.5%, depending upon membership class, of the member's final average salary (as defined in the Code) multiplied by the number of years of credited service. In most cases after completion of five years of service, a member's right to the defined benefit is vested and early retirement benefits may be elected. Under certain features of the System, active members may purchase credit for various types of prior school and non-school service on a lump-sum, installment purchase basis, or through an actuarially calculated benefit reduction.

In addition to regular retirement benefits, the System also provides for disability retirement benefits and death benefits. Participants are eligible for disability retirement benefits after completion of five years of credited service. Such benefits are generally equal to 2% or 2.5%, depending upon membership class, of the member's final average salary (as defined in the Code) multiplied by the number of years of credited service, but not less than one-third of such salary nor greater than the benefit the member would have had at normal retirement age. Members over normal retirement age may apply for disability benefits. Certain exceptions apply to normal disability retirements.

Death benefits are payable upon the death of an active member who has reached age 62 or who has at least five years of credited service. Such benefits are actuarially equivalent to the benefit that would have been effective if the member had retired on the day before death.

Members with credited service in the Commonwealth of Pennsylvania State Employees' Retirement System (SERS) may elect to transfer service to the Public School Employees' Retirement System upon commencement of employment in the public school system. Similarly, a member with credited service in the System may transfer such service to SERS upon becoming a member of that system.

Upon termination of a member's employment in the public school sector, the member's accumulated contributions plus interest are refundable from the Members' Savings Account which is described in Note 3.

### (c) Postemployment Healthcare Benefits

The System provides a Health Insurance Premium Assistance Program (premium assistance) for all eligible annuitants who elect to participate. Under this program, employer contribution rates for premium assistance are established to provide reserves in the Health Insurance Account that are sufficient for the payment of premium assistance benefits for each succeeding year. Effective January 1, 2002, under the provisions of Act 9 of 2001, participating eligible annuitants are entitled to receive premium assistance payments equal to the lesser of \$100 per month or

**Notes to Financial Statements (Continued)**

their out-of-pocket monthly health insurance premium. To receive premium assistance, eligible annuitants must obtain their health insurance through either their school employer or the PSERS' Health Options Program (HOP).

The HOP is a PSERS-sponsored voluntary health insurance program for the sole benefit of annuitants of PSERS, spouses of annuitants, survivor annuitants and their dependents. Benefits are provided by managed care providers or by PSERS self-funded fee for service plans. All retirees are eligible to participate in the Enhanced or Basic Options (indemnity plans) regardless of their residence. The managed care plans are available to retirees residing in the plan's service area. The HOP is funded exclusively by the premiums paid by its participants for the benefit coverage they elect. The hospital, medical/surgical and major medical benefits of the Enhanced and Basic Options are self-funded. PSERS uses a third-party administrator to process these claims. An independent actuarial consulting firm sets the rates for the self-funded benefits so that the combination of contributions and the claims fluctuation reserve equal 125% of expected annual incurred claims. The HOP maintains a reserve for claims that are incurred but not reported (IBNR). At June 30, 2006 and 2005, PSERS recorded \$9,151,000 and \$10,300,000, respectively, in IBNR which is included in benefits payable. Effective January 1, 2006, PSERS made significant changes to HOP, in response to the Medicare Modernization Act. PSERS entered into an Employer/Union Entity contract with the Centers for Medicare and Medicaid Services to operate a voluntary Medicare Prescription Drug Plan. Monthly contributions are received from CMS covering the 36,000 participants in the PDP. The PSERS pension fund assets are not available to fund or satisfy obligations of the HOP.

**(d) Contributions**

The Code requires contributions by active members, employers, and the Commonwealth. The Code provides for periodic employer and Commonwealth contributions at actuarially determined rates, expressed as a percentage of annual covered payroll, such that they, along with employee contributions and an actuarially determined rate of investment return, are adequate to accumulate assets to pay retirement benefits when due. Level percentage of payroll employer contribution rates are determined using the entry age normal actuarial funding method. This method determines the amount of contributions necessary to (1) fully fund all current costs, which represents the estimated amount necessary to pay for the benefits earned by the employees during the current service year; and (2) liquidate the prior service cost for service earned prior to the current service year and subsequent benefit increases, which represents the amount necessary to fund accrued liabilities over the appropriate amortization periods.

Contribution rates for active members are set by law (redefined with the provisions of Act 9 of 2001) and are dependent upon members' class. In most cases, the contribution rates based on qualified member compensation are as follows:

Membership Class T-C	Active members hired before July 22, 1983	5.25%
Membership Class T-C	Active members hired on or after July 22, 1983	6.25%
Membership Class T-D	Active members hired before July 22, 1983	6.50%
Membership Class T-D	Active members hired on or after July 22, 1983	7.50%

Active members newly hired after July 1, 2001, the effective date of Act 9 of 2001, are automatically Class T-D. The contribution rates for all members in Membership Class T-D were effective January 1, 2002.

## Notes to Financial Statements (Continued)

The total contribution rate for the employers and the Commonwealth was 4.69% and 4.23% of qualified compensation for the years ended June 30, 2006 and 2005, respectively. According to requirements established in Act 29 of 1994, the Commonwealth reimburses school entity employers a portion of the employer contributions paid to the System. The Commonwealth remits employer contributions for employers other than school entities directly to the System. All contributions from employers and the Commonwealth are shown as employer contributions on the Statements of Changes in Plan Net Assets.

A portion of each employer and Commonwealth contribution to the System is set aside for the funding of the health insurance premium assistance program. The premium assistance contribution rate is set at a level necessary to establish reserves sufficient to provide premium assistance payments for all participating eligible members for the subsequent fiscal year. The portion of the total contribution rate for employers and the Commonwealth used to fund premium assistance was 0.69% and 0.23% for the years ended June 30, 2006 and 2005, respectively.

## 2. Summary of Significant Accounting Policies

### (a) Basis of Accounting

The financial statements of the System are prepared on the accrual basis of accounting under which expenses are recorded when the liability is incurred, revenues are recorded in the accounting period in which they are earned and become measurable, and investment purchases and sales are recorded as of their trade date. Member and employer contributions are recognized in the period for which employees' salaries are reported. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

The accounting and reporting policies of the System conform to accounting principles generally accepted in the United States of America (GAAP). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of additions and deductions in plan net assets during the reporting period. Actual results could differ from those estimates.

### (b) Investments

The System's investments are reported at fair value. Fair value is the amount that the System can reasonably expect to receive for an investment in a current sale between a willing buyer and a willing seller, that is, other than in a forced or liquidation sale. Short-term securities are carried at cost, which approximates fair value, unless they have a published market price or quotation from national security exchanges or securities pricing services, in which case they are valued at the published market price. Fixed income securities and common and preferred stocks are generally valued based on published market prices and quotations from national security exchanges or securities pricing services. Securities which are not traded on a national security exchange are valued by the respective fund manager or other third parties based on similar sales.

**Notes to Financial Statements (Continued)**

Directly-owned real estate investments are primarily valued based on appraisals performed by independent appraisers or, for properties not appraised, at cost or the present value of the projected future net income stream. Real estate owned investments are reported net of related debt borrowed against the market value of the property. As of June 30, 2006 and 2005, \$132,000,000 in line of credit advances were netted against the related property valuation. The line of credit balance is due on March 14, 2009. The line is payable at an interest rate equivalent to the lender's commercial paper rate plus 30 basis points and is collateralized by certain fixed income investments of the System.

Private equity, private debt, venture capital and equity real estate investments are primarily valued based on amounts established by valuation committees. The values for private equity, private debt, venture capital and equity real estate investments are reported on a one-quarter lag (March 31) adjusted for cash flows and significant unrealized losses through June 30. Futures contracts, foreign exchange contracts, and options are marked-to-market daily with changes in market value recognized as part of net appreciation/depreciation in the fair value of investments. Initial margin requirements for such financial instruments are provided by investment securities pledged as collateral or by cash.

Collective trust fund investments (CTF) consist primarily of domestic and international institutional funds. The funds do not pay interest or dividends to shareholders and reinvest all income earned on securities held by the fund. The fair value of CTF is based on the reported share value of the respective fund. CTF are managed by state chartered banks for which various state banking departments have regulatory oversight and investment advisors for which the Securities and Exchange Commission has regulatory oversight.

Investment expenses consist of investment manager fees and those administrative expenses directly related to the System's investment operations. Unsettled investment sales are reported as investment proceeds receivable and unsettled investment purchases are included in investment purchases and other liabilities.

**(c) Capital Assets**

Capital assets, consisting primarily of data processing equipment and software, are recorded at historical cost. The System depreciates capital assets using the straight-line method over an estimated useful life of seven years.

**(d) Benefits Payable**

Benefits payable identifies the obligations of the System, on an accrual basis, for the estimated retirement and death benefits payable to PSERS' members or members' beneficiaries at the end of the fiscal year. It also includes the HOP \$9,151,000 IBNR claims reserve and a \$2,559,000 prescription drug benefit payable at June 30, 2006.

**Notes to Financial Statements (Continued)****(e) Compensated Absences**

The System uses the accrual basis of accounting for measuring vacation leave, sick leave, and other compensated absences liabilities. Employees of the System are paid for accumulated vacation leave upon termination or retirement. Retiring employees of the System that meet service, age, or disability requirements are paid between 30% and 100% of sick days available at retirement, up to 163 maximum days paid. As of June 30, 2006 and 2005, \$2,946,000 and \$2,727,000, respectively, was accrued for unused vacation and sick leave for the System's employees and included in "Accounts payable and accrued expenses" on the Statements of Plan Net Assets.

**(f) Premium Advances**

Premium advances in 2006 are for HOP and CMS premiums related to health care and prescription drug coverage to be provided in 2006. Premium advances in 2005 are for HOP premiums related to health care coverage provided in 2005.

**(g) Federal Income Taxes**

The Internal Revenue Service (IRS) issued a determination letter dated March 3, 1978 which stated that the plan and its underlying trust qualify under the provisions of Section 501(a) of the *Internal Revenue Code* (IRC) and therefore are exempt from federal income taxes. The plan has been amended since receiving that determination letter. Additionally, the IRS issued a 1982 ruling which concluded that the fund and the board are integral parts of the Commonwealth, and are therefore not subject to federal income tax. In the opinion of management, the System has operated within the terms of the plan and remains qualified under the applicable provisions of the IRC.

Federal tax legislation was enacted in 2001 that modified the rules for making rollovers to or from pension systems and also established maximum amounts of retirement benefits that can be paid from pension systems. The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) expanded the opportunity for members to roll over funds received from PSERS at retirement to a wider variety of plans including, but not limited to, 403(b) tax sheltered annuities and government sponsored 457 deferred compensation plans. The Act permits the rollover of after-tax contributions from PSERS. EGTRRA provided for periodic increases in the annual compensation limits for qualified retirement plans. The annual compensation limits for 2005 and 2006 were \$210,000 and \$220,000, respectively. EGTRRA also provided for periodic increases in the annual benefit limits for qualified defined benefit plans. The maximum annual defined benefit limits at age 62 for 2005 and 2006 were \$170,000 and \$175,000, respectively.

**(h) Risk Management**

The System is exposed to various liabilities and risks of loss, including, without limitation, the ordinary risks of investment losses, risks related to theft or destruction of assets, liabilities resulting from injuries to employees, and liabilities resulting from court challenges to fiduciary decisions. As an administrative agency of the Commonwealth of Pennsylvania, the System is accorded sovereign immunity. For claims not shielded by sovereign immunity, the System participates in certain Commonwealth pooled insurance programs and requires asset managers to carry certain insurance

**Notes to Financial Statements** (Continued)

coverage for the protection of the System. The System also implemented a self-insurance program for fiduciary and director and officer liability coverage. During the past three fiscal years, insurance settlements did not exceed insurance coverage.

**(i) Reclassifications**

Certain 2005 balances have been reclassified to conform with the 2006 presentation.

**(j) Members Receivables**

Member's receivables include an amount for members' obligations to the System for the purchase of service credit in the amount of \$151,299,000. Members have a variety of options to remit purchase of service payments:

- Remit a lump sum payment.
- Request an installment plan from one to seven years where the member's employer establishes a payroll deduction process. The member's employer then forwards quarterly payments of the withheld amounts to PSERS.
- Accept an actuarial reduction debt through which the amount of the purchase plus accumulated interest will reduce the member's retirement or death benefit.
- Rollover funds from an eligible distribution.

Because members have control over the timing of their remittances to the System, many purchases of service receivables extend beyond one year. An estimated \$127,954,000 of the \$236,005,000 members pension receivables at June 30, 2006 are expected to be collected by the System subsequent to June 30, 2007.

**(k) Adoption of New Accounting Standards**

During the year ended June 30, 2005 the System adopted Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures (an amendment of GASB Statement No. 3)* ("GASB 40"). The adoption of GASB 40 required the System to include a presentation of Deposit and Investment Risk Disclosures in the Notes to Financial Statements. See Note 4 for disclosures required by this Statement.

During the year ended June 30, 2006 the System adopted Governmental Accounting Standards Board Statement No. 44, *Economic Condition Reporting: The Statistical Section (an amendment of NCGA Statement 1)*. The adoption of GASB 44 requires the System to meet reporting standards in the Statistical Section of its CAFR. These standards are designed to enhance the provision of information for the assessment of the financial position and the financial condition of the System.

**3. Description of Accounts**

The Code requires the System to maintain the following accounts which represent reserves held for future and current benefit payments as follows:

**Notes to Financial Statements (Continued)****(a) State Accumulation Account**

The State Accumulation Account is credited with the contributions of the Commonwealth and the employers. Additionally, interest earnings of the System (after crediting the Members' Savings Account with 4% interest and the reserve for retirement with 5.50% statutory interest) are credited to this account. Each year, the necessary amounts, as determined by the actuary for the payment of retirement, disabilities, and death benefits, are transferred from the State Accumulation Account to the Reserve for Retirement Account increasing the reserve credit to the 8.5% valuation assumption rate determined by the actuary. All administrative expenses necessary for the operation of the System, except for premium assistance and HOP expenses, are paid from the State Accumulation Account.

**(b) Members' Savings Account**

The Members' Savings Account is credited with all contributions made by active members of the System. Interest is added to the member's individual account at an annual rate of 4%.

Upon death or retirement of a member, the accumulated contributions plus interest are transferred to the Reserve for Retirement Account for subsequent payment of benefits.

**(c) Reserve for Retirement Account**

The Reserve for Retirement Account represents the amounts transferred from the Members' Savings and State Accumulation Accounts, plus additional contributions made by the Commonwealth and employers for the payment of supplemental annuities and cost-of-living increases. All death, disability, and retirement benefits are paid from this account. Annual interest of 5.50% is credited to the Reserve for Retirement Account.

**(d) Health Insurance Account**

The Health Insurance Account is credited with contributions of the Commonwealth and the employers for the health insurance premium assistance program. Effective January 1, 2002, under the provisions of Act 9 of 2001, participating eligible annuitants are entitled to receive premium assistance payments equal to the lesser of \$100 per month or their out-of-pocket monthly health insurance premium. The Health Insurance Account pays all administrative expenses necessary to operate the health insurance premium assistance program.

**(e) Health Insurance Program Account**

The Health Insurance Program Account is credited with contributions from members of the HOP and from CMS. All benefits related to the HOP (premium payments to the insurance companies and self-funded benefits) are paid from this account. The Health Insurance Program Account pays all administrative expenses necessary to operate the HOP.



## Notes to Financial Statements (Continued)

**(f) Pension and Postemployment Healthcare Net Assets**

Net assets held in trust for pension and postemployment healthcare benefits at June 30 follows:

	<b>(Dollar Amounts in Thousands)</b>	
	<u>2006</u>	<u>2005</u>
Pension:		
State accumulation account	\$ 17,370,947	\$ 14,557,519
Members' savings account	9,571,668	9,116,347
Reserve for retirement account	<u>30,293,052</u>	<u>28,262,531</u>
<b>Total pension</b>	<b><u>\$ 57,235,667</u></b>	<b><u>\$ 51,936,397</u></b>
Postemployment healthcare:		
Health insurance account	\$ 92,777	\$ 97,137
Health insurance program account	<u>88,857</u>	<u>77,892</u>
<b>Total postemployment healthcare</b>	<b><u>\$ 181,634</u></b>	<b><u>\$ 175,029</u></b>

**4. Investments****(a) Summary of Investments**

The Board has the responsibility to invest and reinvest available funds of the System, in accordance with the guidelines and limitations set forth in the Code and other applicable state law. The Board accomplishes the daily management of the System's investments through investment advisors who act as agents for the System and through internal investment managers.

The Board invests the funds of the System using the "prudent investor" standard which requires the Board to consider the probable safety of investments, avoid speculative investments, and invest as people of prudence, discretion, and intelligence would manage their own affairs. The Board has adopted its investment policy to formally document investment objectives and responsibilities. This policy, as well as applicable state law, establishes guidelines for permissible investments of the System.

## Notes to Financial Statements (Continued)

A summary of the fair value of investments at June 30 follows:

	(Dollar Amounts in Thousands)	
	2006	2005
<b>Pension investments:</b>		
<b>Short-term:</b>		
Pennsylvania Treasury Domestic Short-Term Investment Fund	\$ 2,848,280	\$ 1,949,355
Other domestic short-term	683,350	901,088
Collective trust funds	-	1,070,616
International short-term	348,739	233,506
	<b>3,880,369</b>	<b>4,154,565</b>
<b>Fixed income:</b>		
Domestic mortgage-backed securities	5,670,890	4,898,249
U.S. government and agency obligations	3,152,963	2,943,165
Domestic corporate and taxable municipal bonds	2,880,975	3,178,674
Miscellaneous domestic fixed income	170,880	198,656
Collective trust funds	304,949	276,234
International fixed income	1,781,539	1,959,710
	<b>13,962,196</b>	<b>13,454,688</b>
<b>Common and preferred stock:</b>		
Domestic common and preferred stock	13,647,660	17,249,029
Collective trust funds	6,272,121	607,223
International common stock	13,032,195	10,003,537
	<b>32,951,976</b>	<b>27,859,789</b>
<b>Real estate:</b>		
Equity real estate	2,255,291	2,091,392
Directly-owned real estate	287,108	194,225
	<b>2,542,399</b>	<b>2,285,617</b>
<b>Alternative investments:</b>		
Private equity	3,634,938	3,408,590
Private debt	992,673	1,143,928
Venture capital	573,161	432,551
	<b>5,200,772</b>	<b>4,985,069</b>
<b>Pension investments at fair value</b>	<b>\$ 58,537,712</b>	<b>\$ 52,739,728</b>
<b>Postemployment Healthcare investments:</b>		
Premium Assistance:		
Pennsylvania Treasury Domestic Short-Term Investment Fund	\$ 14,563	\$ 10,081
Other domestic short-term	50,143	81,688
	<b>64,706</b>	<b>91,769</b>
Health Options Program:		
Pennsylvania Treasury Domestic Short-Term Investment Fund	72,553	44,245
Other domestic short-term	44,298	46,433
U.S. government and agency obligations	-	15,877
	<b>116,851</b>	<b>106,555</b>
<b>Postemployment Healthcare investments at fair value</b>	<b>\$ 181,557</b>	<b>\$ 198,324</b>

**Notes to Financial Statements (Continued)****(b) Deposit and Investment Risk Disclosures****i. Deposits**

Custodial credit risk for deposits is the risk that, in the event of a financial institution failure, the System would not be able to recover the value of the deposits. The State Treasury Department is the custodian of the System's fund. State Treasury Department deposits must be held in insured depositories approved by the Commonwealth's Board of Finance and Revenue and must be fully collateralized.

The System, through its third party administrator, maintains certain bank deposits for the operation of its voluntary health insurance program. These deposits are not required to be collateralized by statute or policy. These deposits totaled \$44,298,000 and \$46,433,000 at June 30, 2006 and 2005, respectively, and are under the custody of M&T Bank that has an A-1 Deposit/Debt rating by Standard and Poor's and an A2 rating by Moody's.

**ii. Investment Risks**

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

**Concentration of Credit Risk**

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. As of June 30, 2006 and 2005 the System has no single issuer that exceeds 5% of total investments. Investments issued or explicitly guaranteed by the U.S. government and investments in mutual funds, external investment pools, and other pooled investments are excluded.

**Custodial Credit Risk**

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the System would not be able to recover the value of investment or collateral securities that are in the possession of an outside party. In accordance with a contractual relationship between the Commonwealth's Treasury Department and its custodial agent, substantially all investments, where securities are used as evidence of the investment, are held by the custodian in book-entry form in the System's name. Those investments are defined as insured or registered investments for which the securities are held by the System or its agent and, therefore, have very minimal level of custodial credit risk. The remaining investments, which do not have securities that are used as evidence of the investment, are primarily in collective trust funds and limited partnerships, which include real estate and alternative investments.

## Notes to Financial Statements (Continued)

**Credit Risk**

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The credit risk of a debt instrument is measured by nationally recognized statistical rating organizations (NRSRO) such as Fitch Investor Services (Fitch), Moody's Investor Services (Moody's), and Standard and Poor's (S&P). Annually, the Board establishes an asset allocation plan. This plan manages the overall credit risk of the fixed income asset class through a clearly defined long-term asset allocation policy. This policy establishes a long-term target allocation of the fixed income asset class at 22% of the investment portfolio. The fixed income target allocation consists of:

- An allocation of 12.6% of the portfolio has been made to a domestic core plus segment of the fixed income asset class benchmarked to the Lehman Aggregate Bond Index and composed of primarily investment grade, relatively liquid, public domestic bonds with an overall weighted-average NRSRO credit rating of A or better;
- An allocation of 5% of the portfolio has been made to the Treasury Inflation-Protected Securities (TIPS) segment of the fixed income asset class benchmarked to the Lehman U.S. TIPS Index and composed of primarily government issued TIPS with an overall weighted-average NRSRO credit rating of AA or better;
- An allocation of 3.3% of the portfolio has been made to the global core plus fixed income asset class benchmarked to the Lehman Global Aggregate Index composed of primarily investment grade, relatively liquid U.S. and non-U.S. public bonds with an overall weighted-average NRSRO credit rating of A or better; and,
- An allocation of 1.1% of the portfolio has been made to the high yield fixed income asset class benchmarked to the Credit Suisse First Boston High Yield Bond Index that focuses on less liquid public non-investment grade fixed income securities with an overall weighted-average NRSRO credit rating of BB+ or less.

The following table discloses aggregate market value by credit quality rating category. Many securities have ratings from more than one NRSRO and sometimes those ratings differ from one NRSRO to another. The data listed below uses the rating (expressed as S&P equivalent), available from Fitch, Moody's and/or S&P that indicates the greatest degree of risk at June 30, 2006 and 2005.

## Notes to Financial Statements (Continued)

<u>Quality Rating</u>	(Dollar Amounts in Thousands)	
	<u>2006</u> Fair Value	<u>2005</u> Fair Value
AAA	\$ 6,445,960	\$ 5,998,491
AA	1,072,388	958,565
A	1,260,292	1,168,562
BBB	1,152,165	1,034,282
BB and below	854,747	1,179,419
NR*	<u>3,801,658</u>	<u>4,028,098</u>
<b>Total Exposed to Credit Risk</b>	14,587,210	14,367,417
<b>U.S. Government Guaranteed**</b>	<u>3,436,912</u>	<u>3,440,160</u>
<b>Total Fixed Income and Short-Term Investments</b>	<b><u>\$ 18,024,122</u></b>	<b><u>\$ 17,807,577</u></b>

\* Not Rated securities include \$304,949 and \$1,346,850 in collective trust funds at June 30, 2006 and 2005, respectively. Also included are \$2,935,396 and \$2,003,681 at June 30, 2006 and 2005, respectively, in the Pennsylvania (PA) Treasury Domestic Short-Term Investment Fund (STIF), a pooled investment fund for which ratings were unavailable. The STIF pool is comprised of short-term, high credit quality securities which are mainly U.S. Treasuries, agencies or repurchase agreements.

\*\* Composed of U.S. government and agency obligations explicitly guaranteed by the U.S. government and not considered to have credit risk.

### Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of a fixed income investment. The System manages its interest rate risk by diversifying the fixed income portfolio and maintaining the fixed income portfolio at an effective duration range between 65 and 135 percent of the benchmark index.

Duration is a measure of the approximate sensitivity of a bond's value to interest rate changes. The higher the duration, the greater the changes in fair value when interest rates change. For example, a duration of 4.0 would mean that, given a 100-basis point change up/down in rates, a bond's price would move down/up approximately 4.0 percent. PSERS measures interest rate risk using option-adjusted duration, which recognizes the fact that yield changes may change the expected cash flows due to embedded options.

## Notes to Financial Statements (Continued)

At June 30, 2006 and 2005, the System's fixed income portfolio had the following option-adjusted durations by fixed income sector:

Investment Type	(Dollar Amounts in Thousands)			
	2006		2005	
	Option-Adjusted Duration	Fair Value	Option-Adjusted Duration	Fair Value
Domestic mortgage-backed securities	3.1	\$ 5,670,890	1.8	\$ 4,898,249
U.S. government & agency obligations	5.1	3,152,963	6.3	2,959,042
Domestic corporate and taxable municipal bonds	3.4	2,880,975	3.3	3,178,674
Miscellaneous domestic fixed income	1.0	170,880	1.4	198,656
Fixed income collective trust funds	3.8	304,949	5.2	276,234
International fixed income	6.2	1,781,539	7.0	1,959,710
PA Treasury Domestic Short-Term Investment Fund	0.1	<u>2,935,396</u>	0.1	<u>2,003,681</u>
<b>Total fixed income &amp; PA Treasury Domestic Short-Term Investment Fund</b>	<b>3.3*</b>	<b>16,897,592</b>	<b>3.4*</b>	<b>15,474,246</b>
Total adjustment for futures contracts	<u>0.2**</u>	<u>-</u>	<u>1.2**</u>	<u>-</u>
<b>Total fixed income &amp; PA Treasury Domestic Short-Term Investment Fund</b>	<b><u>3.5**</u></b>	<b><u>\$ 16,897,592</u></b>	<b><u>4.6**</u></b>	<b><u>\$ 15,474,246</u></b>

\* The option-adjusted duration of 3.3 and 3.4 at June 30, 2006 and 2005, respectively, for the total fixed income & PA Treasury Domestic Short-Term Investment Fund portfolio is calculated by weighting the option-adjusted duration of each investment type by market value.

\*\* Fixed income investment managers enter into futures contracts to adjust the durations of their portfolios as a whole rather than any particular investment type within the portfolio. In total, the futures contracts have adjusted PSERS' total fixed income & PA Treasury Domestic Short-Term Investment Fund portfolio duration upward by 0.2 and 1.2 at June 30, 2006 and 2005, respectively.

## Notes to Financial Statements (Continued)

## Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. As part of the System's program to manage risk and enhance returns, the System invests in non-U.S. markets. Investment managers in non-U.S. equity and global fixed income may hedge their non-U.S. foreign currency exposure back to U.S. dollars. The System also reduces the exposure to currency risk by hedging up to 30% of MSCI EAFE Index country currencies to the U.S. dollar. At June 30, 2006 and 2005 PSERS had the following non-U.S. currency exposure:

## 2006

(Dollar Amounts in Thousands)

Currency	Equity	Fixed Income	Alternative Investments	Short-Term*	Currency Hedge**	Total Fair Value
Euro	\$ 3,213,586	\$ 796,778	\$ 678,328	\$ (775)	\$ (1,346,075)	\$ 3,341,842
British pound sterling	2,271,685	177,855	66,613	85,278	(792,495)	1,808,936
Japanese yen	2,497,865	132,200	-	20,222	(895,990)	1,754,297
Canadian dollar	680,242	98,029	11,692	39,068	-	829,031
South Korean won	402,962	12,068	-	51,739	-	466,769
Swedish krona	292,826	38,141	-	22,711	-	353,678
Hong Kong dollar	407,870	-	-	2,093	(87,275)	322,688
Swiss franc	706,145	-	-	(74,409)	(314,409)	317,327
Australian dollar	360,776	5,309	-	131,491	(200,827)	296,749
Other non-U.S. currencies	<u>1,349,383</u>	<u>127,742</u>	<u>-</u>	<u>151,258</u>	<u>-</u>	<u>1,628,383</u>
<b>Total</b>	<b>\$ <u>12,183,340</u></b>	<b>\$ <u>1,388,122</u></b>	<b>\$ <u>756,633</u></b>	<b>\$ <u>428,676</u></b>	<b><u>(3,637,071)</u></b>	<b>\$ <u>11,119,700</u></b>

## 2005

(Dollar Amounts in Thousands)

Currency	Equity	Fixed Income	Alternative Investments	Short-Term*	Total Market Value
Euro	\$ 2,456,484	\$ 874,761	\$ 597,765	\$ (215,101)	\$ 3,713,909
British pound sterling	1,826,597	153,178	115,856	44,978	2,140,609
Japanese yen	1,704,872	73,125	-	328,334	2,106,331
Swiss franc	500,899	-	-	2,197	503,096
Canadian dollar	316,574	63,233	7,682	36,096	423,585
South Korean won	373,100	11,397	-	17,122	401,619
Hong Kong dollar	361,620	-	-	2,357	363,977
Australian dollar	299,085	75,856	-	(12,167)	362,774
Swedish krona	238,952	42,191	-	16,814	297,957
Other non-U.S. currencies	<u>1,131,191</u>	<u>214,951</u>	<u>-</u>	<u>(11,297)</u>	<u>1,334,845</u>
<b>Total</b>	<b>\$ <u>9,209,374</u></b>	<b>\$ <u>1,508,692</u></b>	<b>\$ <u>721,303</u></b>	<b>\$ <u>209,333</u></b>	<b>\$ <u>11,648,702</u></b>

\* Includes investment receivables and payables.

\*\* The currency hedge program was not implemented until FY 2006.

**Notes to Financial Statements (Continued)****(c) Securities Lending**

In accordance with a contract between the Commonwealth and its custodial agent, the System participates in a securities lending program. Under this program, the custodian, acting as the lending agent, loans securities (equities, fixed income issues and money market instruments) to independent brokers and dealers in exchange for collateral in an amount not less than 102% of the fair value of any securities loaned except for non-U.S. corporations for which 105% of the fair value is required. For Euro fixed income debt issues, for which the Commonwealth receives Euros as collateral and international fixed income debt issues denominated in U.S. dollars, the collateral required to be exchanged is in an amount not less than 102% of the fair value of any securities loaned. Collateral is marked-to-market daily. If the fair value of the collateral held falls below the minimum guidelines for securities loaned, additional collateral is obtained. In lieu of certain approved securities or cash, the borrower may deliver to the lending agent irrevocable bank letters of credit as collateral. If the collateral obtained consists in whole or in part of cash, the lending agent may use or invest the cash in accordance with reinvestment guidelines approved by the Commonwealth.

As of June 30, 2006 and 2005, the System had no credit risk exposure to borrowers because the amounts the System owed the borrowers exceeded the amounts the borrowers owed the System. Under the securities lending program, the lending agent provides indemnification to the Commonwealth if the same borrowers fail to return the underlying securities (and the collateral is inadequate to replace the loaned securities) or fail to pay income distributions on them. There were no losses during the fiscal years ended June 30, 2006 and 2005 resulting from a default of the borrowers or the lending agent.

All securities loans can be terminated on demand by either the System or the borrower, although the average term of the loan is one day. There were no term loans as of June 30, 2006 and 2005.

Cash collateral is invested in the lending agent's short-term investment pool and is not subject to custodial credit risk. The System's income from securities lending represents its pro-rata share from participating in the program. The weighted-average maturity of the investments in the pool was 31 days and 27 days at June 30, 2006 and 2005, respectively. The relationship between the maturities of the investment pool and the System's loans is affected by the maturities of the securities loans made by other entities that use the lending agent's pool, which the System cannot determine. The System cannot pledge or sell collateral securities received unless the borrower defaults. In the event of a default, the lending agent may use the collateral to replace the loaned securities.

As of June 30, 2006, the fair value of loaned securities was \$7,028,659,000 which includes \$818,469,000 of loaned securities which are collateralized by securities and irrevocable letters of credit that are not included in the Statement of Plan Net Assets. The fair value of the associated collateral was \$7,166,598,000 of which \$6,337,173,000 was cash. As of June 30, 2005, the fair value of loaned securities was \$6,861,398,000 which includes \$473,692,000 of loaned securities which are collateralized by securities and irrevocable letters of credit that are not included in the Statements of Plan Net Assets. The fair value of the associated collateral was \$7,110,014,000 of which \$6,600,684,000 was cash.



## Notes to Financial Statements (Continued)

## 5. Derivative and Other Similar Investments

The System enters into a variety of financial contracts, which include options and futures. The System also enters into foreign exchange positions, such as forward and spot contracts to obtain or hedge foreign currency exposure; collateralized mortgage obligations (CMOs); other forward contracts, and U.S. Treasury strips. The System is not a dealer, but an end-user of these instruments. The contracts are used primarily to enhance performance and reduce the volatility of the portfolio. The System is exposed to credit risk in the event of non-performance by counterparties to financial instruments. As the System generally enters into transactions only with high quality institutions, no losses associated with counterparty nonperformance on derivative financial instruments have been incurred. Legal risk is mitigated through selection of executing brokers and review of all documentation. The System is exposed to market risk, the risk that future changes in market conditions may make an instrument less valuable. Exposure to market risk is managed in accordance with risk limits set by senior management, through buying or selling instruments or entering into offsetting positions.

The notional or contractual amounts of derivatives indicate the extent of the System's involvement in the various types and uses of derivative financial instruments and do not measure the System's exposure to credit or market risks and do not necessarily represent amounts exchanged by the parties. The amounts exchanged are determined by reference to the notional amounts and the other terms of the derivatives.

The following table summarizes the aggregate notional or contractual amounts for the System's derivative financial instruments at June 30, 2006 and 2005 (in thousands):

	2006	2005
Futures contracts – long	<b>\$ 11,547,597</b>	\$ 14,086,616
Futures contracts – short	<b>3,828,194</b>	6,651,721
Foreign exchange forward and spot contracts, gross	<b>10,161,833</b>	5,141,012
Options – calls purchased	<b>25,109</b>	-
Options – puts purchased	-	15,651
Options – calls sold	<b>23,230</b>	70,751
Options – puts sold	<b>53,167</b>	47,946

Futures contracts are contracts in which the buyer agrees to purchase and the seller agrees to make delivery of a specific financial instrument at a predetermined date and price. Gains and losses on futures contracts are settled daily based on a notional (underlying) principal value and do not involve an actual transfer of the specific instrument. Futures contracts are standardized and are traded on exchanges. The exchange assumes the risk that a counterparty will not pay and generally requires margin payments to minimize such risk. In addition, the System enters into short sales, sales of securities it does not presently own, to neutralize the market risk of certain equity positions. Initial margin requirements on futures contracts and collateral for short sales are provided by investment securities pledged as collateral and by cash held by various brokers. Although the System has the right to access individual pledged securities, it must maintain the amount pledged by substituting other securities for those accessed. The value of securities pledged and the amount of cash held at June 30, 2006 and 2005 represent a restriction on the amount of assets available as of year-end for other purposes.

**Notes to Financial Statements (Continued)**

Option contracts provide the option purchaser with the right, but not the obligation, to buy or sell the underlying security at a set price during a period or at a specified date. The option writer is obligated to buy or sell the underlying security if the option purchaser chooses to exercise the option. The System generally uses exchange listed currency, index, stock, and futures options. The System has authorized an investment manager to write covered call stock index option spreads up to a notional amount of \$500,000,000.

Foreign exchange contracts involve an agreement to exchange the currency of one country for the currency of another country at an agreed-upon price and settlement date. The contracts reported above primarily include forwards. The \$10,161,833,000 of foreign currency contracts outstanding at June 30, 2006 consist of “buy” contracts, which represent the U.S. dollar equivalents of commitments to purchase foreign currencies of \$3,869,444,000 and “sell” contracts, which represent U.S. dollar equivalents of commitments to sell foreign currencies of \$6,292,389,000. The \$5,141,012,000 of foreign currency contracts outstanding at June 30, 2005 consist of “buy” contracts of \$3,359,106,000 and “sell” contracts of \$1,781,906,000. The unrealized loss on contracts of \$(52,689,000) and \$(7,825,000) at June 30, 2006 and 2005, respectively, is included in the System’s net assets and represents the fair value of the contracts. The System has authorized an investment manager to manage a currency hedge portfolio consisting of foreign exchange spot and forward contracts, currency futures, and currency options to hedge up to a notional amount of \$5,100,000,000 of the MSCI EAFE Index currencies to U.S. dollars.

The System also invests in mortgage-backed securities (MBS) such as CMOs and MBS forwards to maximize yields. These securities are sensitive to prepayments of mortgages, which may result from a drop in interest rates. The MBS forwards are subject to credit risk in the event of nonperformance by counterparties. The fair value of CMOs at June 30, 2006 and 2005 is \$2,295,764,000 and \$2,357,739,000, respectively.

The System invests in U.S. Treasury strips which essentially act as zero coupon bonds and are subject to market volatility from a rise or drop in interest rates.

Through certain collective trust funds, the System also indirectly holds various derivative financial instruments. The collective trust funds invest in futures and options thereon; forward foreign currency contracts; options; interest rate, currency, equity, index, and total return swaps; interest-only strips; and CMOs, to enhance the performance and reduce the volatility of their portfolios.

Swap agreements are used to modify investment returns or interest rates on investments in the collective trust funds. Swap transactions involve the exchange of investment returns or interest rate payments without the exchange of the underlying principal amounts. These swaps expose the collective trust funds entering into these types of arrangements to credit risk in the event of nonperformance by counterparties.

**Notes to Financial Statements (Continued)****6. Pension Plan for Employees of the System**

The System contributes to the Commonwealth's State Employees' Retirement System (SERS), a cost-sharing multiple-employer defined benefit pension plan. SERS provides retirement, death, and disability benefits to plan members and beneficiaries according to Commonwealth statute. SERS issues a publicly available financial report that can be obtained by writing to SERS, 30 N. Third Street, P. O. Box 1147, Harrisburg, Pennsylvania 17108-1147.

The contribution requirements of plan members and the System are mandated by Commonwealth statute. Most SERS plan members are required to contribute 5% or 6.25% of their annual covered payroll depending upon service class. The System is required to contribute at an actuarially determined rate.

The rates applied to annual covered payroll were 2.37% at June 30, 2006, 1.43% at June 30, 2005, and 0.50% at June 30, 2004. The System's contributions to SERS for the year ending June 30, 2006, 2005 and 2004 were \$418,000, \$233,000 and \$84,000, respectively, which were equal to the required contributions each year.

**7. Litigation and Contingencies**

The System is subject to various threatened and pending lawsuits. These lawsuits include issues related to benefit calculations and eligibility including challenges to amendments to the Public School Employees' Retirement Code which increased retirement benefits for certain active public school employees but did not provide for increased benefits for employees who retired before the effective date of the amendments. It is the opinion of management that the ultimate liability arising from such threatened and pending litigation will not have a material effect on the financial position of the System. The System is exposed to various other liabilities and risks related to fiduciary responsibilities of directors and officers.

## Required Supplemental Schedule 1 Schedule of Funding Progress\*

(Unaudited - see accompanying auditors' report)  
(Dollar Amounts in Millions)

Valuation as of June 30	(1) Actuarial accrued liabilities (AAL)	(2) Actuarial value of assets	(3) (Funded) Unfunded actuarial accrued liabilities (FAAL) or UAAL (1) – (2)	(4) Ratio of assets to AAL (2) / (1)	(5) Covered payroll	(6) (FAAL) or UAAL as a percentage of covered payroll (3) / (5)
2005	# \$61,129.4	\$ 51,122.1	\$ 10,007.3	83.6%	\$ 10,527.7	95.1%
2004	# 56,978.1	51,949.6	5,028.5	91.2%	10,030.7	50.1%
2003	# 54,313.3	52,770.0	1,543.3	97.2%	9,652.9	16.0%
2002	# 51,693.2	54,193.1	(2,499.9)	104.8%	9,378.9	(26.7)%
2001	# 47,870.9	54,783.9	(6,913.0)	114.4%	9,414.9	(73.4)%
2000	39,771.6	49,241.8	(9,470.2)	123.8%	8,939.6	(105.9)%

\* The amounts reported in the Schedule of Funding Progress do not include assets or liabilities for Premium Assistance and HOP.

# Includes the effects of Act 9 of 2001 and Act 38 of 2002.

See accompanying notes to required supplemental schedules.

## Required Supplemental Schedule 2 Schedule of Employer Contributions\*

(Unaudited - see accompanying auditors' report)  
(Dollar Amounts in Thousands)

Year ended June 30	Annual required contributions	Actual Employer contributions	Percentage contributed
2006	\$ 1,328,373	\$ 456,878	34%
2005	945,107	431,556	46%
2004	321,091	321,091	100%
2003	20,831	20,831	100%
2002	539	539	100%
2001	158,193	158,193	100%

The Board adopted all contribution rates as recommended by the Actuary pursuant to the prevailing provisions of the Retirement Code for each year.

\* The amounts reported in the Schedule of Employer Contributions do not include premium assistance contributions.

See accompanying notes to required supplemental schedules.

# Notes to Required Supplemental Schedules

June 30, 2006 and 2005

(Unaudited - see accompanying auditors' report)

## 1. Description of Schedule of Funding Progress

Each time a new benefit is added which applies to service already rendered, an "unfunded accrued liability" is created. The laws governing PSERS require that these additional liabilities be financed systematically over a period of future years. Also, if actual financial experiences are less favorable than assumed financial experiences, the difference is added to unfunded accrued liabilities.

In an inflationary economy, the value of the dollar is decreasing. In this environment, employees pay in greater dollar amounts, resulting in a dollar increase in unfunded accrued liabilities. This occurs at a time when the actual substance of these items may be decreasing. Looking at just the dollar amounts of unfunded accrued liabilities can be misleading. Unfunded accrued liabilities divided by active employee payroll provides an index which clarifies understanding. The smaller the ratio of unfunded liabilities to covered payroll, the stronger the system. Observation of this relative index over a period of years will give an indication of whether the system is becoming financially stronger or weaker.

## 2. Actuarial Assumptions and Methodologies

### (a) Funding Method

An entry-age normal actuarial cost method of valuation is used in determining benefit liabilities and normal cost. The outstanding balance of the June 30, 2001 unfunded accrued liability is being amortized over a closed 10-year period commencing July 1, 2002, with level dollar funding. Changes in the unfunded accrued liability, including actuarial gains and losses, subsequent to June 30, 2001 are being amortized over a closed period of 10 years from the first day of July next following the change, with level dollar funding.

### (b) Asset Valuation Method

For actuarial purposes, assets are valued using a five-year moving market average value that will recognize the 8.5% actuarial expected investment return immediately and spread the difference between actual and expected investment return (beginning with fiscal year ending June 30, 2001) over a period of five years (adopted as of June 30, 2001). Previously, PSERS immediately recognized interest and dividends when earned, and recognized realized and unrealized gains and losses on the market value of assets over a three-year period.

**Notes to Required Supplemental Schedules (Continued)****(c) Actuarial Assumptions**

Significant actuarial assumptions employed by the actuary for funding purposes as of June 30, 2005, the date of the most recent actuarial valuation include:

- Investment return – 8.5%, includes inflation at 3.25%
- Salary increases – 6.00%, which reflects an allowance for inflation of 3.25%, national productivity of 1%, and merit or seniority increases of 1.75%
- Amortization method – level dollar funding
- Remaining amortizations period (closed) – 10 years and 30 years in accordance with Act 40 of 2003
- Benefit payments – no postretirement benefit increases assumed in the future
- Multiple Decrement Tables – mortality, vesting, retirement age, and withdrawal estimates are based upon tables provided by the actuary

The System's actuarial values are calculated separately for retirees and beneficiaries and for active and inactive members.

The actuarial present value of benefits to be paid to retirees and beneficiaries currently receiving benefits and deferred survivor beneficiaries, whose benefits have been determined, is calculated using the assumptions noted above. The Reserve for Retirement Account with interest credited thereon at an annual rate of 5.50% is compared to the actuarial accrued liability for the remaining lifetimes of the retirees and beneficiaries and any deficiency is then funded by a transfer from the State Accumulation Account. Consequently, all such determined benefits are fully funded.

The actuarial accrued liability for active and inactive members is calculated on the projected benefit basis using the entry-age normal actuarial cost method under which the present value of each member's expected benefit payable at retirement or death is determined. The assets of the Members' Savings Account, State Accumulation Account and the fair value adjustment are subtracted from this present value to arrive at the funded or unfunded actuarial accrued liability.

## Supplemental Schedule 1 Schedule of Operating Expenses Fiscal Year Ended June 30, 2006

(Dollar Amounts in Thousands)

	Administrative expenses (1)	Investment expenses (2)	Total
<b>Personnel costs:</b>			
Salaries and wages	\$ 13,714	\$ 2,360	\$ 16,074
Social security contributions	1,063	180	1,243
Retirement contributions	342	76	418
Employees' insurance contributions	3,964	434	4,398
Other employee benefits	49	758	807
<b>Total personnel costs</b>	<b>19,132</b>	<b>3,808</b>	<b>22,940</b>
<b>Operating costs:</b>			
Investment managers' fees	-	202,898	202,898
Custodian fees	-	359	359
Specialized services	17,504	70	17,574
Rental of real estate, electricity	1,632	134	1,766
Consultant and legal fees	1,637	2,222	3,859
Treasury and other Commonwealth services	1,819	111	1,930
Postage	1,839	-	1,839
Contracted maintenance and repair services	353	26	379
Office supplies	484	8	492
Rental of equipment and software	1,107	103	1,210
Printing	1,161	-	1,161
Travel and training	301	8	309
Telecommunications	518	10	528
Equipment (not capitalized)	193	181	374
Miscellaneous expenses	277	1,341	1,618
<b>Total operating expenses</b>	<b>28,825</b>	<b>207,471</b>	<b>236,296</b>
<b>Fixed charges:</b>			
Furniture and fixtures	305	-	305
Depreciation	367	-	367
<b>Total fixed charges</b>	<b>672</b>	<b>-</b>	<b>672</b>
<b>Total operating expenses</b>	<b>\$ 48,629</b>	<b>\$ 211,279</b>	<b>\$ 259,908</b>

- (1) Includes administrative expenses of \$1,977 related to Postemployment Healthcare Premium assistance and \$11,261 related to Postemployment Healthcare Health Options Program for the fiscal year ended June 30, 2006.
- (2) Does not include \$28,205 in capitalized broker commissions for the fiscal year ended June 30, 2006.



## Supplemental Schedule 2 Summary of Investment Expenses Fiscal Year Ended June 30, 2006

(Dollar Amounts in Thousands)

	<u>Assets under management*</u>	<u>Fees</u>
<b>External management</b>		
Short-term **	\$ -	\$ 303
Domestic equity	7,001,000	43,424
International equity	13,139,000	44,730
Fixed income	9,141,000	12,851
Real estate	3,436,000	35,249
Private equity and debt	4,627,000	48,806
Venture capital	573,000	17,535
<b>Total external management</b>	<b>37,917,000</b>	<b>202,898</b>
<b>Total internal management</b>	<b>19,299,000</b>	<b>5,568</b>
<b>Total investment management</b>	<b>\$ 57,216,000</b>	<b>\$ 208,466</b>
Custodian fees		359
Consultant and legal fees		2,222
Miscellaneous expenses		232
<b>Total investment expenses</b>		<b>\$ 211,279</b>

\* Net asset value at June 30, 2006

\*\* Short-term investments with a fair value of \$2,935,000 are included in the other external and internal management assets under management amounts.

### Supplemental Schedule 3

## Schedule of Payments to Non-Investment Consultants

### Fiscal Year Ended June 30, 2006

(Payment amounts greater than \$50,000)

<u>Consultant</u>	<u>Fees</u>	<u>Services Provided</u>
CoreSource, Inc.	\$ 7,587,542	Postemployment healthcare benefits administration and claims adjudication
Tier Technologies, Inc.	4,722,332	NPAS project development
The Segal Company	2,395,189	Actuarial services and consulting for HOP and prescription drug plan
Benecard Services, Inc.	1,939,692	Administration of postemployment healthcare benefits and prescription drug plan
Buck Consultants LLC	1,062,191	Pension benefit actuarial services
L. R. Wechsler Ltd.	413,599	Information technology consulting
Independent Pharmaceutical Consultants, Inc.	294,604	Administration of postemployment healthcare benefits and prescription drug plan
Independent Fiduciary Services, Inc.	223,750	Auditing services
Info Matrix Corporation	87,480	Computer programming/analysis
Clifton Gunderson LLP	84,000	Financial audit of pension system and postemployment healthcare programs
Milliman Inc.	50,000	Actuarial audit



Public School Employees' Retirement System

# Investment Section



**COMMONWEALTH OF PENNSYLVANIA  
PUBLIC SCHOOL EMPLOYEES RETIREMENT SYSTEM**

ALAN H. VAN NOORD, CFA  
Chief Investment Officer

## Investment Overview

### Authority and Fiduciary Standard

The Board has the responsibility to invest funds of the System in accordance with guidelines and limitations set forth in the Code and other applicable state law. As fiduciaries, the members of the Board and Staff must act solely in the interests of the members of the System and for the exclusive benefit of the System's members. In performance of their duties, the members of the Board and Staff delegated with investment authority shall be held to the Prudent Investor Standard.

The Prudent Investor Standard, as articulated in the Code, means "the exercise of that degree of judgment, skill and care under the circumstances then prevailing which persons of prudence, discretion and intelligence who are familiar with such matters exercise in the management of their own affairs not in regard to speculation, but in regard to the permanent disposition of the fund, considering the probable income to be derived therefrom as well as the probable safety of their capital."

The Prudent Investor Standard requires a trustee to act prudently and with caution, discretion, loyalty, and care but does not restrict the assets in which the Board can invest. Under the Prudent Investor Standard, which recognizes modern portfolio theory, the Board's investment and management decisions with respect to individual assets shall be considered in the context of the portfolio as a whole and as part of an overall investment strategy, and not in isolation. No specific investment or course of action, taken alone, shall be considered inherently prudent or imprudent. This Standard recognizes the trade-off between risk and return.

### Policies and Objectives

The Board is responsible for the formulation of investment policies for the System. The overall investment objectives of the System are as follows:

- **Return Objectives** – the overall return objective is to realize a return sufficient to achieve funding adequacy on an inflation-adjusted basis. Funding adequacy is achieved when the actuarial market value of assets is at least equal to the System's projected benefit obligations. The System has a return objective of meeting or exceeding the targeted actuarial rate of return (currently 8.5%) over the long-term. In addition, the Board has the following broad objectives:
  1. The assets of the System shall be invested to maximize the returns for the level of risk taken; and,
  2. The System shall strive to achieve a return that exceeds the Policy Index (the Policy Index is a custom benchmark created based on the Board-established asset allocation structure to generate a return that meets the actuarial rate of return assumption).

- **Risk Objectives**

1. The assets of the System shall be diversified to minimize the risk of losses within any one asset class, investment type, industry or sector distribution, maturity date, or geographic location. Failure to do so could impair the System's ability to achieve its funding and long-term investment goals and objectives; and,
2. The System's assets shall be invested so that the probability of investment losses (as measured by the Policy Index) in excess of 12% in any one year is no greater than 2.5% (or two standard deviations below the expected return).

To achieve these objectives, the Board meets at least once per year to review the overall asset allocation plan and investment policies for the System. Implementation of investment policies is accomplished through the use of external investment management firms who act as agents for the System and through internal investment managers. The Board also retains various investment consultants to assist with the formulation and implementation of investment policies.

## **Operations**

The Board provides oversight of investment activities through the Finance Committee that makes recommendations to the Board. The Finance Committee generally conducts eight meetings per year and may meet more frequently as needed. Investment Office staff, as well as external investment advisors, internal investment managers, and Investment Accounting staff, assist the Board in achieving investment objectives and monitoring compliance with investment policies. For the fiscal year ended June 30, 2006, Wilshire Associates Incorporated (Wilshire) served as the general investment consultant to assist the Board in formalizing investment objectives, establishing an asset allocation plan, conducting investment advisor searches, reviewing performance, and commenting on compliance with investment policies. In addition, the Board utilized Courtland Partners, Ltd. as a real estate consultant and Portfolio Advisors, LLC as an alternative investment consultant. Alternative investments generally consist of investments in private debt, private equity, and venture capital limited partnerships. Investment Office staff implement the investment decisions within the Investment Policy Statement, Objectives and Guidelines regarding asset allocation, security selection, and other objectives directed by the Board.

The Board employs both external investment management firms and internal investment managers to manage the investment portfolio of the System. At year end, 40 external investment management firms were managing \$30.9 billion in assets of the System, \$19.3 billion in assets were managed by the System's internal investment managers, and the remaining \$8.5 billion in assets were managed by numerous developmental, alternative investment, and real estate managers. The performance of each external investment management firm and each internal manager is monitored quarterly against a pre-established benchmark as well as the performance of its peer group.

## **Asset Allocation**

The Board reviews the long-term asset allocation targets of the System at least annually, usually in the first quarter of the calendar year. The Board will consult with its actuary, consultants, Investment Office staff, and other sources of information it deems appropriate in formulating the asset allocation plan. The Board believes that the level of risk assumed by the System is largely determined by the Board's strategic asset allocation plan. The Board, in determining its long-term asset allocation, shall take the following factors into consideration:

- The System's investment time horizon;
- The demographics of the plan participants and beneficiaries;
- The cash flow requirements of the System;
- The actuarial assumptions approved by the Board;
- The funded status of the System;
- The Board's willingness and ability to take risk; and,
- The employers' (Commonwealth and school districts) financial strength.

In establishing the asset allocation for the System, the Board considers capital market expectations for expected return, volatility, and asset class correlations as prepared by its general investment consultant. The current long-term, top-down asset allocation targets of the Board are discussed in the following paragraphs.

The long-term target allocation as of June 30, 2006 included an equity target allocation of **60.0%** consisting of publicly traded stocks. Specific targets have been established for U.S. equity exposure (30.0%) and international equity exposure (30.0%). During the latter half of the fiscal year ending June 30, 2006, the Board approved a change to the U.S. and international equity target allocations eliminating the home country bias. Eliminating the home country bias had the effect of decreasing the target U.S. equity exposure from 40% to 30% and increasing the target international equity exposure from 20% to 30%. Within the U.S. equity target, the portfolios are diversified between large, small and micro capitalization investment managers, and growth and value investment managers. The international equity exposure includes both developed and emerging markets portfolios.

The fixed income target allocation of **22.0%** consisted of U.S. core fixed income exposure (12.6%), Treasury Inflation-Protected Securities exposure (5.0%), specialty fixed income exposure (1.1%), and global fixed income exposure (3.3%). Within these categories, all sectors of the bond market are represented. Specialty fixed income is comprised of a high yield portfolio.

The real estate target allocation of **7.0%** consisted primarily of opportunistic limited partnerships and publicly traded real estate securities.

Alternative investments had a target of **11.0%**. The primary vehicle used to invest funds in this asset class is the limited partnership. The partnerships are established by individual management groups that have been selected by the System for the purpose of investing in and managing private equity and unlisted subordinated debt positions on behalf of PSERS and other limited partners.

Finally, unallocated cash of the System has an asset allocation target of **0.0%** since cash historically represents the lowest returning asset class over time.

## Investment Results

As of June 30, 2006, the fair value of the investment portfolio was \$58.7 billion, an increase of \$5.8 billion over last year's value. This increase came primarily from net investment income (\$7.9 billion) and net changes in other investment assets and liabilities (\$0.5 billion), which were partially offset by benefit payments in excess of member and employer contributions (\$2.6 billion). The investment portfolio, as invested, was composed of 62.4% common and preferred stocks (equity), 21.7% fixed income investments, 6.8% real estate, and 9.1% alternative investments at June 30, 2006. The table on page 74 illustrates a more detailed description of the investment portfolio's asset classes in dollars and as a percentage of the total investment portfolio.

The past fiscal year saw positive market returns across all major asset classes except domestic fixed income securities. Markets that enjoyed particularly strong returns included international equities (developed, small cap, and emerging markets) and real estate. International equities were up 28.40% during the fiscal year according to the Morgan Stanley Capital International (MSCI) All-Country World Index (ACWI) ex. U.S., an international equity index. International small capitalization equities, which are included in PSERS International Stock Portfolios, were up 31.23% according to the S&P/Citigroup Global ex. U.S. Extended Market Index. Emerging market equities, a sub-sector of the MSCI ACWI ex. U.S., were up 35.90% during the fiscal year according to the MSCI Emerging Markets Index. The strength in these markets can be partially attributed to the strength in commodity prices during the past fiscal year, especially oil. In addition, strong economic growth and corporate profits have also driven these markets to higher levels. Publicly traded real estate securities were up 21.87% during the fiscal year according to the Dow Jones (DJ) Wilshire Real Estate Securities Index. Strengthening fundamentals and attractive yields have helped to drive returns in this segment of the market. The DJ Wilshire 5000 Index, a domestic equity index, returned 9.92% for the fiscal year. All of these gains came in the first three quarters of the fiscal year as strong corporate profits flowed through to share prices. However, the markets were down almost 2.00% in the fiscal fourth quarter as rising interest rates and commodity prices outweighed continued strong economic growth, stable consumer confidence, and a falling unemployment rate.

The Lehman Aggregate Bond Index, a domestic bond index, was down 0.81% while the Lehman Global Aggregate Bond Index, a global bond index, was up 0.27%. Returns in these indexes were weak as the Federal Reserve increased rates eight times during the fiscal year increasing the Federal Funds rate from 3.25% to 5.25%.

As a result of the strong positive returns from equities, real estate, and alternative investments, the System was able to generate a total return of 15.26% for the one-year period ended June 30, 2006. This return exceeded the total fund Policy Index return of 11.96% by 330 basis points. Annualized total returns for the three- and five-year periods ended June 30, 2006 were 15.90% and 8.67%, respectively. These returns exceeded the total fund Policy Index returns for the three- and five-year periods ended June 30, 2006 by 299 and 174 basis points, respectively. As of June 30, 2006, the System had posted positive returns in 12 of the past 13 quarters.

Wilshire calculates the total investment return of the System as well as the performance of each external investment management firm and each internal investment manager employed by the Board to invest the System's assets. Performance is calculated using a time-weighted return methodology.

The following table provides the System's total investment return for each major asset class and the total portfolio, including, where applicable and available, respective benchmark indexes used by asset class and median performance by asset class:



	Annualized Total Returns (%) Net of Fees Ended June 30, 2006		
	1 Year	3 Years	5 Years
	<b>PSERS Total Portfolio</b>	<b>15.26</b>	<b>15.90</b>
Total Fund Policy Index	11.96	12.91	6.93
Median Public Defined Benefit Plan (DBP) Fund Universe (Wilshire Database)	10.66	12.35	6.85
<b>PSERS Domestic Stock Portfolios</b>	<b>9.66</b>	<b>13.19</b>	<b>4.74</b>
Dow Jones Wilshire 5000 Index	9.92	12.98	4.02
Median Public DBP Fund Universe - Domestic Equities (Wilshire Database)	9.66	13.16	4.02
<b>PSERS International Stock Portfolios</b>	<b>30.81</b>	<b>26.44</b>	<b>12.41</b>
MSCI All-Country World Index Ex. U.S.	28.40	25.77	11.85
Median Public DBP Fund Universe - International Equities (Wilshire Database)	27.29	24.11	10.84
<b>PSERS Domestic Fixed Income Portfolios</b>	<b>0.14</b>	<b>4.00</b>	<b>6.37</b>
Lehman Brothers Aggregate Index	(0.81)	2.05	4.97
Median Public DBP Fund Universe - Domestic Bonds (Wilshire Database)	0.11	3.26	5.69
<b>PSERS Global Fixed Income Portfolios</b>	<b>1.11</b>	<b>4.75</b>	<b>8.90</b>
Lehman Brothers Global Aggregate Index	0.27	4.09	8.27
Median Public DBP Fund Universe - Global Bonds (Wilshire Database)	0.37	5.52	9.84
<b>PSERS Real Estate*</b>	<b>38.60</b>	<b>29.15</b>	<b>18.86</b>
Blended Real Estate Index**	20.63	17.46	13.35
Median Public DBP Fund Universe - Real Estate (Wilshire Database)	20.40	19.32	14.40
<b>PSERS Alternative Investments*</b>	<b>22.17</b>	<b>22.56</b>	<b>10.66</b>
Venture Economics Median Return, Vintage Year Weighted***	11.78	8.65	2.78
Median Public DBP Fund Universe - Private Equity (Wilshire Database)	26.35	18.69	6.91

\* Returns reported on a one-quarter lag, except for publicly traded real estate security investments.

\*\* Returns presented are a blend of the DJ Wilshire Real Estate Securities Index (20%) and the NCREIF Index (80%). The NCREIF Index is reported on a one-quarter lag.

\*\*\* Returns presented are on a one-quarter lag.

The System also is involved in a securities lending program administered by Mellon Bank N.A. This program provides incremental income to the System by lending securities in the System's portfolio to securities dealers in exchange for either cash collateral, which can be reinvested to generate income, or non-cash collateral plus a cash fee. This program generated \$23.0 million in additional income during the year.

## Accomplishments

The System's returns during the fiscal year ended June 30, 2006 not only exceeded its total fund Policy Index, but also placed the System in the top 10% of all public defined benefit pension funds in the country as measured by Wilshire. Strong returns such as these can be attributed to the combined efforts of the Board, the System's Investment Office and Investment Accounting staff, and its external consultants and investment advisors. Without their efforts, accomplishments such as this would not be possible.

The System continued its multi-year project to implement an independent accounting book of record for the System's investment transactions and holdings. In FY 2006, the System completed its conversion of all public market portfolios to its internal accounting software provided by Financial Control Systems, Inc. and began work on converting its real estate and alternative investment portfolios from an Excel-based accounting system to the internal accounting software. The System expects to complete the conversion of all remaining portfolios and develop various management reports in 2007.

## Summary

The System had a tremendous fiscal year ended June 30, 2006, as the returns generated by the System were in the top 10% of all public defined benefit pension plan returns. Strong returns generated in domestic and international equity markets, real estate, and alternative investments helped produce outstanding results for the System. For the fiscal year ended June 30, 2006, the System exceeded its targeted actuarial rate of return of 8.5% on a one-, three-, and five-year basis. In addition, we continue to believe that the System's asset allocation is structured to generate a long-term return that meets or exceeds the targeted actuarial rate of return assumption of the System for years to come.



Alan H. Van Noord, CFA  
Chief Investment Officer

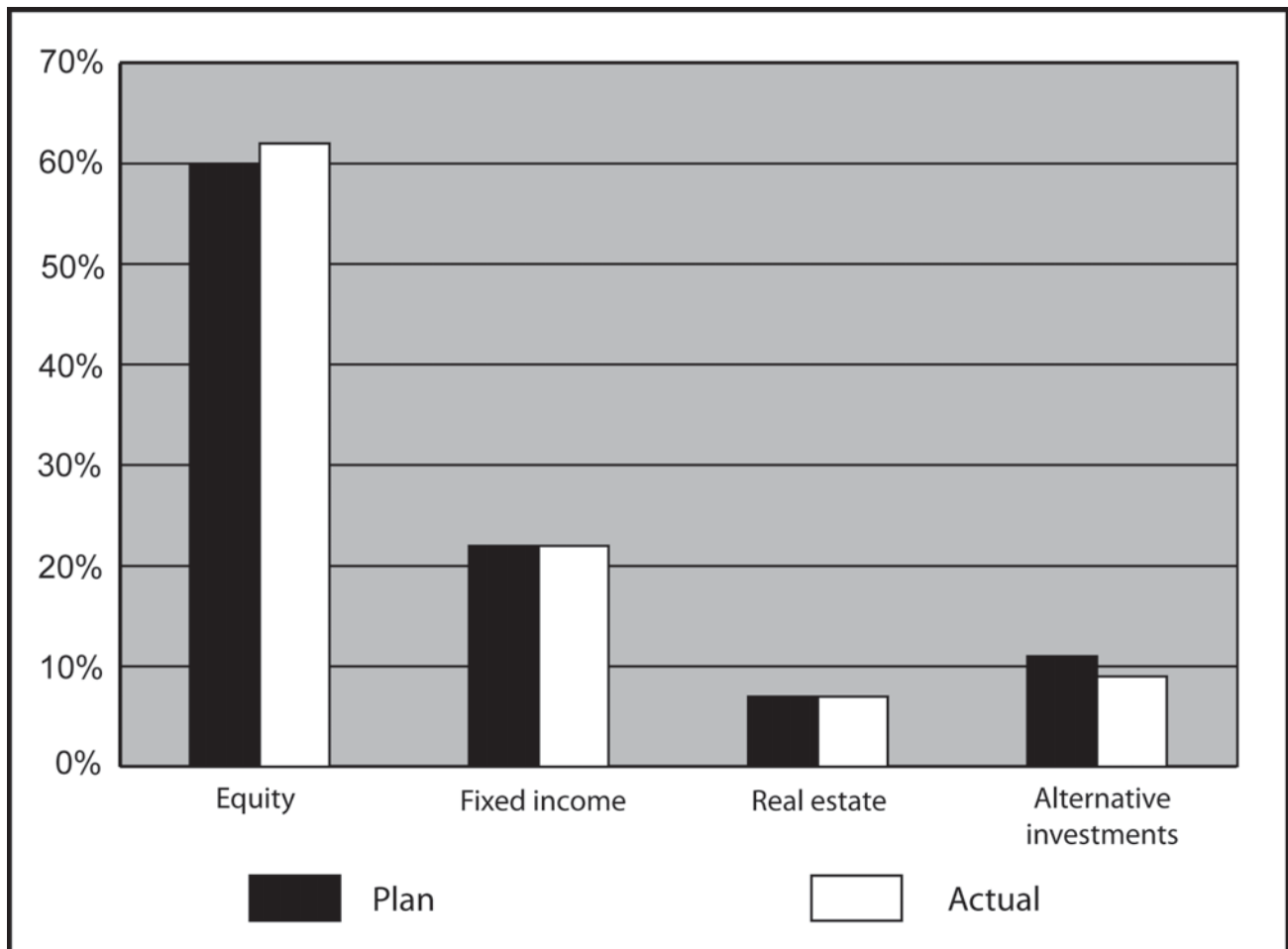
**Portfolio Summary Statistics**  
**Asset Allocation**  
**As of June 30, 2006**  
(Dollar Amounts in Thousands)

<b>Pension investments</b>	<b>Fair Value (\$)</b>	<b>% Fair Value</b>
<b>Common and preferred stock (Equity):</b>		
Domestic common and preferred stock	\$ 13,647,660	24.0%
Collective trust funds	6,272,121	11.0%
International common stock	13,032,195	22.8%
Subtotal per Statement of Plan Net Assets	32,951,976	57.8%
Net Asset Allocation Adjustment*	2,615,444	4.6%
<b>Total Common and preferred stock - Asset Allocation Basis</b>	<b>35,567,420</b>	<b>62.4%</b>
<b>Fixed income:</b>		
Domestic mortgage-backed securities	5,670,890	9.9%
U.S. government and agency obligations	3,152,963	5.5%
Domestic corporate and taxable municipal bonds	2,880,975	5.1%
Miscellaneous domestic fixed income	170,880	0.3%
Collective trust funds	304,949	0.5%
International fixed income	1,781,539	3.1%
Subtotal per Statement of Plan Net Assets	13,962,196	24.4%
Net Asset Allocation Adjustment*	(1,566,567)	(2.7)%
<b>Total Fixed income - Asset Allocation Basis</b>	<b>12,395,629</b>	<b>21.7%</b>
<b>Real estate:</b>		
Equity real estate	2,255,291	4.0%
Directly-owned real estate	287,108	0.5%
Subtotal per Statement of Plan Net Assets	2,542,399	4.5%
Net Asset Allocation Adjustment*	1,327,514	2.3%
<b>Total Real estate - Asset Allocation Basis</b>	<b>3,869,913</b>	<b>6.8%</b>
<b>Alternative investments:</b>		
Private equity	3,634,938	6.4%
Private debt	992,673	1.7%
Venture capital	573,161	1.0%
<b>Total Alternative investments - Asset Allocation Basis</b>	<b>5,200,772</b>	<b>9.1%</b>
<b>Pension investments - Asset Allocation Basis</b>	<b>\$ 57,033,734</b>	<b>100.0%</b>
Pension investment receivables\payables	1,503,978	
<b>Pension investments per Statement of Plan Net Assets</b>	<b>\$ 58,537,712</b>	
<b>Postemployment Healthcare investments</b>	<b>\$ 181,557</b>	<b>100.0%</b>

\* - Includes Short-term investments which are allocated to the asset class of the investment manager which holds them, reclassifications of certain investments between asset classes and investment receivables\payables to adjust the Statement of Plan Net Assets' classification to the basis used to measure Asset Allocation. See the table and graph which follow.

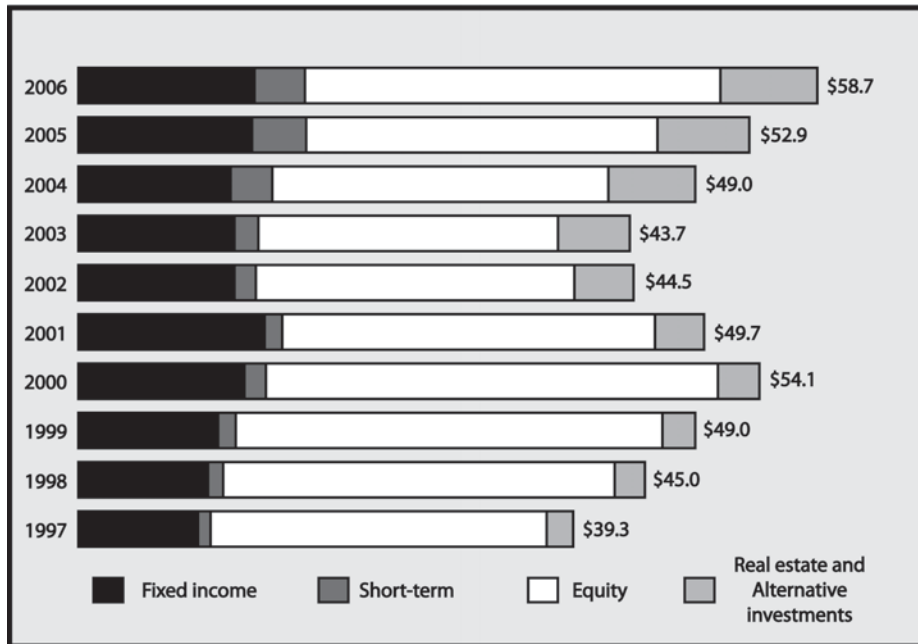
**Comparison of Actual Portfolio Distribution  
to Asset Allocation Plan  
As of June 30, 2006**

<b>Asset Category</b>	<b>Plan</b>	<b>Actual</b>
Common and preferred stock (Equity)	60%	62%
Fixed income	22%	22%
Real estate	7%	7%
Alternative investments	11%	9%
Total	100%	100%



## Portfolio Distribution 10 Year Trend

(Fair Value - Dollar Amounts in Billions)



The following lists of portfolio detail statistics present the ten largest holdings by descending order of fair value for the largest asset classes. Information on the complete holdings of the System is available by writing to the Public School Employees' Retirement System, Office of Financial Management, P. O. Box 125, Harrisburg, PA 17108.

### Domestic Common and Preferred Stock

#### 10 Largest Holdings in Descending Order by Fair Value

As of June 30, 2006

(Dollar Amounts and Shares in Thousands)

Description	No. of Shares	Fair Value (\$)
Security Capital Preferred Growth	9,674	385,298
Exxon Mobil Corporation	4,334	265,878
General Electric Company	7,499	247,176
Citigroup Inc.	3,602	173,776
Bank of America Corporation	3,285	158,032
Microsoft Corporation	6,328	147,437
Johnson & Johnson	2,195	131,539
Procter & Gamble Company	2,335	129,831
Pfizer Inc.	5,278	123,873
ProLogis	2,249	117,237
<b>Total of 10 Largest Holdings</b>		<b>1,880,077</b>
<b>Total System Holdings - Domestic Common and Preferred Stock</b>		<b>13,647,660</b>

## Collective Trust Funds - Common and Preferred Stock

### 10 Largest Holdings in Descending Order by Fair Value

As of June 30, 2006

(Dollar Amounts and Shares in Thousands)

Description	No. of Shares	Fair Value (\$)
Barclays Global Investors EAFE Equity Index	18,227	3,030,398
Bridgewater Pure Alpha Fund II Ltd.	511	570,723
First Quadrant Global Macro Fund Ltd.	5,485	554,296
AQR Offshore Multi-Strategy Fund Ltd.	6	526,775
Barclays Global Ascent Ltd.	500	502,552
Barclays Global Investors MSCI Emerging Markets Index Fund	13,867	376,652
Martin Currie Business Trust Global Emerging Markets Fund	26,008	256,441
Barclays Global Investors Structured Tier Emerging Market Index	6,972	192,700
Barclays Global Investors Canada Alpha Tilts Fund	3,377	95,122
Martin Currie Business Trust Pan European Mid Cap Fund	3,439	65,160
<b>Total of 10 Largest Holdings</b>		<b>6,170,819</b>
<b>Total System Holdings - Collective Trust Funds - Common and Preferred Stock</b>		<b>6,272,121</b>

## International Common Stock

### 10 Largest Holdings in Descending Order by Fair Value

As of June 30, 2006

(Dollar Amounts and Shares in Thousands)

Description	No. of Shares	Fair Value (\$)
Royal Bank of Scotland	4,331	142,432
Glaxosmithkline PLC	4,745	132,614
UBS AG	1,072	117,261
Unicredito Italiano SpA	14,675	114,835
Mitsubishi UFJ Financial Group, Inc.	8	114,701
BP PLC	9,615	112,125
Vodafone Group PLC	49,679	105,896
Sumitomo Mitsui Financial Group, Inc.	10	105,668
ING Groep	2,439	95,838
Takeda Pharmaceutical Company Ltd.	1,532	95,425
<b>Total of 10 Largest Holdings</b>		<b>1,136,795</b>
<b>Total System Holdings - International Common Stock</b>		<b>13,032,195</b>

**Domestic and International Fixed Income**  
**10 Largest Holdings in Descending Order by Fair Value**  
**As of June 30, 2006**  
**(Dollar Amounts and Shares in Thousands)**

Description	Maturity Date	Interest Rate (%)	Par Value(\$) or No. of Shares	Fair Value (\$)
U.S. Treasury - Inflation Index	07/15/13	1.875	287,033	275,741
U.S. Treasury - Inflation Index	07/15/12	3.000	218,405	224,907
U.S. Treasury - Inflation Index	01/15/25	2.375	178,703	173,928
U.S. Treasury - Inflation Index	04/15/28	3.625	133,142	157,986
U.S. Treasury - Inflation Index	04/15/10	0.875	153,561	144,857
U.S. Treasury - Inflation Index	04/15/29	3.875	106,387	131,636
U.S. Treasury - Inflation Index	01/15/15	1.625	140,422	130,906
U.S. Treasury - Inflation Index	01/15/11	3.500	124,423	130,144
U.S. Treasury - Notes	05/15/08	3.750	123,300	120,184
U.S. Treasury - Notes	09/30/06	2.500	117,000	116,245
<b>Total of 10 Largest Holdings</b>				<b>1,606,534</b>
<b>Total System Holdings - Domestic and International Fixed Income</b>				<b>13,962,196</b>

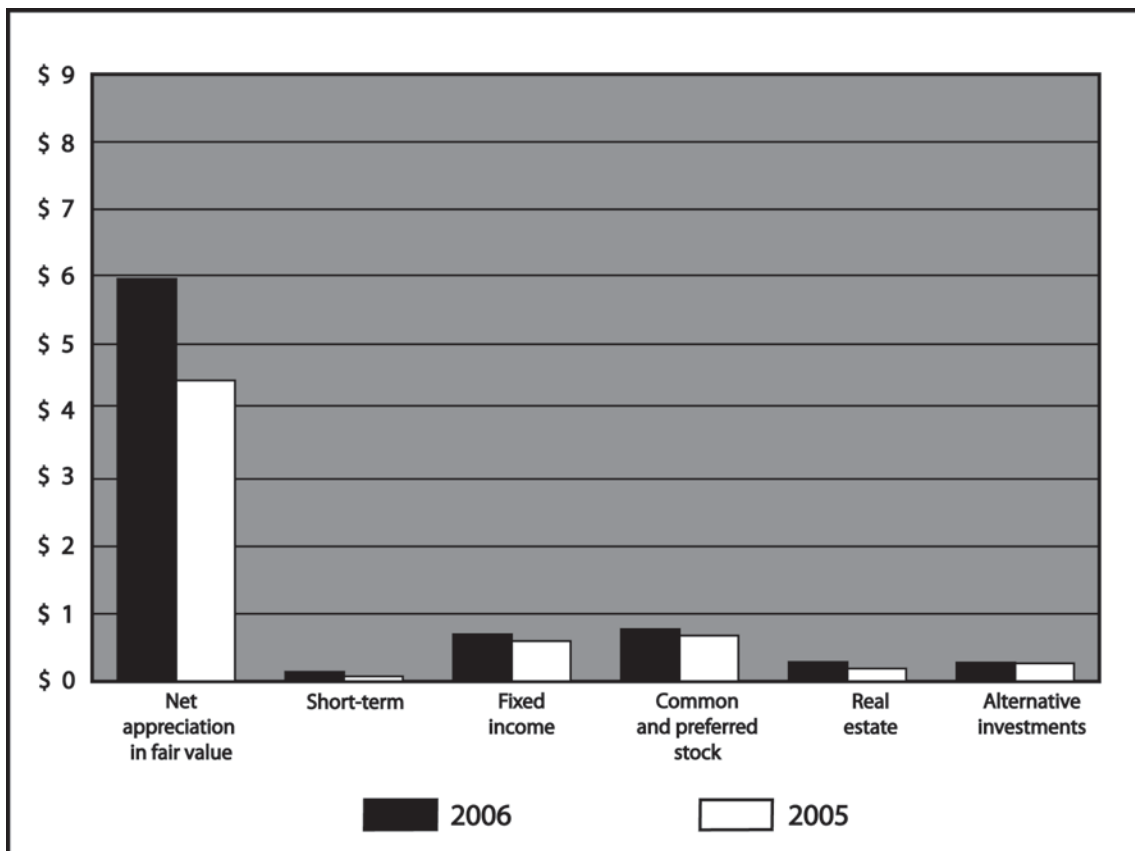
**Postemployment Healthcare Investments**  
**10 Largest Holdings in Descending Order by Fair Value**  
**As of June 30, 2006**  
**(Dollar Amounts in Thousands)**

Description	Maturity Date	Interest Rate (%)	Par Value (\$)	Fair Value (\$)
PA Treasury Short-Term Investment Fund	Various	Various	87,116	87,116
M & T Bank Repurchase Agreement	07/01/06	4.324	14,802	14,802
M & T Bank Repurchase Agreement	07/01/06	4.508	10,922	10,922
FNMA Discount Note	07/21/06	4.814	6,959	6,959
FHLMC Discount Note	07/05/06	4.743	4,970	4,970
FHLMC Discount Note	08/02/06	5.000	4,968	4,968
FNMA Guaranteed REMIC 1994-43 Class PH	09/25/23	6.350	4,064	4,093
FNMA Discount Note	02/09/07	4.150	3,500	3,480
FHLMC Multiclass 2489 Class PD	02/15/31	6.000	3,300	3,298
FNMA Guaranteed REMIC 2002-9 Class C	06/25/30	6.500	2,270	2,272
<b>Total of 10 Largest Holdings</b>				<b>142,880</b>
<b>Total System Holdings - Postemployment Healthcare Investments</b>				<b>181,557</b>

**Comparison of Investment Activity Income**  
**For Fiscal Years Ended June 30, 2006 and 2005**  
(Dollar Amounts in Thousands)

<b>Investing Activities</b>	<b>2006</b>	<b>2005</b>
Net appreciation in fair value of investments	\$ 5,968,866	\$ 4,462,384
Short-term	136,791	71,796
Fixed income	694,888	594,809
Common and preferred stock	771,276	676,549
Real estate	285,333	187,178
Alternative investments	273,808	265,355
<b>Total investment activity income</b>	<b>\$ 8,130,962</b>	<b>\$ 6,258,071</b>

(Dollar Amounts in Billions)





Brokers' fees on equity investment transactions for the fiscal year ended June 30, 2006 were \$28.2 million. The System has commission recapture contracts with several brokers. These contracts generally stipulate that the brokers rebate a percentage of commissions earned on investment transactions directly to the System. During the fiscal year ended June 30, 2006, the System earned \$2.8 million from a commissions recapture program. A list of the brokers receiving fees in excess of \$100,000 during the fiscal year follows.

**Summary Schedule of Brokers' Fees**  
**(Cumulative Fiscal Year Amounts Exceeding \$100,000)**  
**Fiscal Year Ended June 30, 2006**

<b>Broker Name</b>	<b>Fees Paid (\$)</b>	<b>Broker Name</b>	<b>Fees Paid (\$)</b>
Merrill Lynch	2,124,697	Liquidnet Inc.	409,552
UBS Warburg	1,629,570	Credit Lyonnais Securities	391,558
Citigroup/Salomon	1,601,083	Macquarie	367,116
J. P. Morgan, Inc.	1,528,220	Jefferies & Company Inc.	294,076
Credit Suisse First Boston	1,399,238	Cantor, Fitzgerald & Company	288,435
Goldman Sachs & Company	1,387,357	Instinet Corporation	265,938
Morgan Stanley & Company	1,205,709	Daiwa Securities	249,785
Deutsche Bank	1,194,601	Weeden & Company	200,293
Bear, Stearns & Company	1,109,045	UNX	179,538
Lehman Brothers	1,105,654	HSBC Securities Inc.	177,874
Barclays Global Investors	955,896	Susquehanna Financial Group	177,874
Nomura Securities International	734,705	Bank Of America	176,927
Dresdner	688,988	Mizuho Securities	167,352
SG Securities	653,985	Sanford Bernstein & Company	158,979
Jones & Associates	600,701	BNY Brokerage	157,430
ABN AMRO	531,120	Execution Services Incorporated	113,649
Knight Securities	492,441	Cazenove Inc.	108,693
ITG Securities LTD	484,013		

**Professional Consultants  
External Investment Advisors  
As of June 30, 2006**

**Domestic Enhanced Equity Index Managers**

- Acorn Derivatives Management Corporation
- AQR Capital Management, LLC
- Barclays Global Investors
- Bridgewater Associates, Inc.
- First Quadrant, LP
- Pacific Investment Management Company
- Smith Breeden Associates, Inc.

**Domestic Style-Oriented Small Cap Equity Managers**

- Boston Company Asset Management, LLC (The)
- Emerald Advisors, Inc.
- First Pacific Advisors, Inc.
- Mellon Equity Associates
- NorthPointe Capital
- Wellington Management Company, LLP
- William Blair & Company, LLC

**Enhanced Domestic Mid Cap Equity Manager**

- Barclays Global Investors

**Domestic Micro Cap Equity Managers**

- Donald Smith & Company, Inc.
- NorthPointe Capital
- Oberweis Asset Management, Inc.
- Thomson Horstmann & Bryant, Inc.
- Turner Investment Partners

**Publicly Traded Real Estate Securities Managers**

- Morgan Stanley Investment Management, Inc.
- Security Capital Research & Management, Inc.

**Non-U.S. Emerging Market Equity Managers**

- Batterymarch Financial Management, Inc.
- Boston Company Asset Management, LLC (The)
- Templeton Investment Counsel, Inc.
- Wellington Management Company, LLP
- William Blair & Company, LLC

## Professional Consultants (Continued)

### Non-U.S. Large Cap Equity Managers

- AllianceBernstein Institutional Investment Management
- Baillie Gifford Overseas Ltd.
- Barclays Global Investors
- Boston Company Asset Management, LLC (The)
- Marathon Asset Management Limited
- Martin Currie, Inc.
- Mercator Asset Management, LP

### Non-U.S. Small Cap Equity Managers

- Acadian Asset Management
- AXA Rosenberg Investment Management
- Boston Company Asset Management, LLC (The)
- GlobeFlex Capital, LP
- Wasatch Advisors, Inc.

### Currency Hedge Manager

- Pareto Investment Management Limited

### Domestic Fixed Income Managers

- Aberdeen Asset Management, Inc.
- BlackRock Financial Management, Inc.
- Delaware Investment Advisers
- Pacific Investment Management Company
- Western Asset Management Company

### High Yield Fixed Income Manager

- MacKay-Shields Financial Corporation

### Treasury Inflation-Protected Securities Managers

- Bridgewater Associates, Inc.
- Brown Brothers Harriman & Co.

### Global Fixed Income Managers

- Aberdeen Asset Management, Inc.
- Fischer Francis Trees & Watts, Inc.
- Rogge Global Partners

### Real Estate Advisors

- Charter Oak Advisors, Inc.
- GF Management, Inc.

**Professional Consultants (Continued)****Real Estate Advisors (Continued)**

- Grosvenor Investment Management U.S., Inc.
- L&B Realty Advisors, LLP
- Laureate Capital, LLC

**Real Estate Partnerships**

- ARCap Diversified Risk CMBS Fund I & II, LLC
- AvalonBay Value Added Fund, LP
- Berwind Investment Partnership IV, V, & VI
- Blackstone Real Estate Partners V.TE.1, LP
- BPG Co-Investment Partnership, LP
- Carlyle Realty Partners III & IV, LP
- CSFB Strategic Partners II & III RE, LP
- DLJ Real Estate Capital Partners II & III, LP
- Fortress PSERS Investment, LP
- Hines U.S. Office Value Added Fund, LP
- LF Strategic Realty Investors I & II, LP
- Legg Mason Real Estate Capital I & II, Inc.
- Lehman Brothers/PSERS Real Estate, LP
- Lehman Brothers Real Estate Pension Partners II, LP
- Lubert-Adler Real Estate Fund II, III, IV, & V, LP
- Morgan Stanley Real Estate Fund II, LP
- Morgan Stanley Real Estate Fund IV Special Domestic, LP
- Morgan Stanley Real Estate Fund IV & V, Special International, LP
- O'Connor North American Property Partners, LP
- Peabody Global Real Estate Partners, LP
- PRISA
- ProLogis North American Industrial Fund, LP
- Stockbridge Real Estate Fund, LP
- UBS RESA
- Westbrook Real Estate Fund, LP
- Whitehall Street Real Estate, LP III, V, V-S, & VII
- William E. Simon & Sons Realty Partners, LP

**Farmland Advisor**

- Prudential Agricultural Group

**Private Equity/Venture Capital Partnerships**

- ABS Capital Partners II, LP
- Adams Capital Management, LP
- Aisling Capital II, LP
- Allegheny New Mountain Partners, LP
- APA/Fostin Venture Fund I
- Baring Asia Private Equity Fund III, LP
- Bastion Capital Fund, LP

## Professional Consultants (Continued)

## Private Equity/Venture Capital Partnerships (Continued)

- Bear Stearns Merchant Banking Partners II, LP
- BG Media Investors, LP
- Blue Point Capital Partners (B), LP
- Bridgepoint Capital II Partnership, LP
- Bridgepoint Europe IA, IIA, & IIIA, LP
- Bruckmann, Rosser, Sherrill & Company, LP
- Catterton Partners V, LP
- Clarity Partners, LP
- Co-Investment 2000 Fund, LP (The)
- Co-Investment Fund II, LP (The)
- Commonwealth Venture Partners I & II
- Credit Suisse First Boston Equity Partners, LP
- Credit Suisse First Boston International Equity Partners, LP
- Crestview Capital Partners, LP
- Cross Atlantic Technology Fund I & II, LP
- CSFB Strategic Partners II & III-B, & III-VC, LP
- Deutsche European Partners IV, LP
- DLJ Merchant Banking Partners III, LP
- DLJ Strategic Partners, LP
- Dubin Clark Fund II, LP
- Edgewater Growth Capital Partners, LP
- Edgewater Private Equity Fund III, LP
- Edison Venture Fund II & III
- Evergreen Pacific Partners, LP
- Franklin Capital Associates III, LP
- Furman Selz Investors II & III, LP
- Graham Partners Investments (B), LP
- Green Equity Investors II, LP
- Greenwich Street Capital Partners II, LP
- Grotech Partners IV
- GS Mezzanine Partners, LP
- Halifax Capital Partners, LP
- Heritage Fund I, LP
- Jefferies Capital Partners IV, LP
- Jefferson Partners Fund IV (PA), LP
- KBL Partnership, LP
- KRG Capital Fund I, II & III, LP
- Landmark Equity Partners II, III, IV, & V
- Landmark Mezzanine Partners, LP
- Lehman Brothers Communications Investors, LP
- Lehman Brothers Merchant Banking Partners II, LP
- Lehman Brothers Venture Partners 2003-P, LP
- Lexington Capital Partners I, LP
- Lindsay, Goldberg & Bessemer, LP
- LLR Equity Partners I & II, LP
- Milestone Partners II, LP
- Morgan Stanley Dean Witter Capital Partners IV, LP
- NEPA Venture Fund II

**Professional Consultants (Continued)****Private Equity/Venture Capital Partnerships (Continued)**

- New Mountain Partners, LP
- New York Life Capital Partners, I, II & III, LP
- P/A Fund (The)
- PAI Europe III & IV, LP
- Palladium Equity Partners II-A, LP
- Pennsylvania Early Stage Partners I & II, LP
- Perseus-Soros BioPharmaceutical Fund, LP
- Platinum Equity Capital Partners-A, LP
- PNC Equity Partners, LP
- Quadrangle Capital Partners I & II, LP
- Quaker BioVentures, LP
- SCP Private Equity Partners I & II, LP
- Spectrum Equity Investors, LP
- StarVest Partners, LP
- Sterling Capital Partners, LP
- Sterling Venture Partners, LP
- Sunrise Capital Partners, LP
- TDH III, LP
- Technology Leaders, LP
- TL Ventures III, LP
- TPG Partners I, II & V, LP
- U.S. Equity Partners I & II, LP
- Wicks Communications & Media Partners, LP
- Willis Stein & Partners, LP

**Private Debt Partnerships**

- Avenue Special Situations Fund II, III & IV, LP
- Avenue Asia Special Situations Fund II & III, LP
- Cerberus Institutional Partners, LP (Series Two and Three)
- Chrysalis Capital Partners, LP
- Gleacher Mezzanine Fund, LP
- Gold Hill Venture Lending 03-A, LP
- GSC Partners CDO Investors III & IV, LP
- GSC Recovery II & III, LP
- NYLIM Mezzanine Partners Parallel Fund, LP

**Developmental Fund Managers**

- Charter Financial Group, Inc.
- Conestoga Capital Advisors
- Connors Investor Services, Inc.
- Denali Advisors, LLC
- EDMP, Inc.
- Global Capital Management, Inc.
- Hanseatic Management Services, Inc.

## Professional Consultants (Continued)

### Developmental Fund Managers (Continued)

- Hesperides Capital Management, LLC
- John Hsu Capital Group, Inc.
- Opus Capital Management
- Piedmont Investment Advisors
- Piedra Capital, Inc.
- Profit Investment Management
- Pugh Capital Management, Inc.
- Shah Capital Management, Inc.
- Smithbridge Asset Management, Inc.
- Snow Capital Management, LP
- Tucker Hargrove Management, Inc.
- West Chester Capital Advisors

### Alternative Investment Consultant

- Portfolio Advisors, LLC

### Custodian and Securities Lending Agent

- Mellon Bank N.A.

### Investment Accounting Application Service Provider

- Financial Control Systems, Inc.

### Investment Evaluator and General Investment Consultant

- Wilshire Associates Inc.

### Proxy Voting Agent

- Glass, Lewis & Co., LLC

### Real Estate Investments Consultant

- Courtland Partners, Ltd.

Public School Employees' Retirement System

**Actuarial  
Section**





January 28, 2005

The Retirement Board  
Public School Employees'  
Retirement System of Pennsylvania  
P.O. Box 125  
Harrisburg, Pennsylvania 17108

Ladies and Gentlemen:

This report presents the results of the annual actuarial valuation of the Public School Employees' Retirement System of Pennsylvania as of June 30, 2005.

The valuation takes into account all of the promised benefits to which members are entitled as of June 30, 2005, including pension and survivor benefits; and as required by the Retirement Code is the basis for the contribution rate for fiscal year 2006/2007. The fiscal year 2006/2007 employer contribution rate certified by the Board is 6.46%.

The valuation was based on the actuarial assumptions and methods as adopted by the Board of Trustees, including a valuation interest rate of 8½% per annum compounded annually. As a result of the July 1, 2000 – June 30, 2005 experience review the actuarial assumptions and methods used to determine the contribution were changed from last year. Changes adopted by the Board at its December 2005 meeting include a minor change to the actuarial cost method, and changes in the assumptions for post-retirement mortality, death in service, disability retirement, and non-vested withdrawal. The assumed rate of inflation was changed from 3.5% to 3.25%, and the assumed real rate of return on assets was increased from 5% to 5.25%. The interest rate assumption is unchanged at 8.5%, and the salary increase assumption has declined by 25 basis points to a career average of 6%.

### **Assets and Membership Data**

The Retirement System reported the individual data for members of the System as of the valuation date to the actuary. While we did not verify the data at their source, we did perform tests for internal consistency and reasonableness. The amount of assets in the trust fund taken into account in the valuation was based on statements prepared for us by the Retirement System.

### Funding Adequacy

At its December 2005 meeting the Board adopted a package of assumption changes whose fiscal impact had not previously been determined by the actuary. At the meeting the actuary estimated that the required fiscal year 2006/2007 employer contribution rate would be 6.46%, and the Board certified this rate. The actuary subsequently confirmed that the 6.46% rate is adequate for funding future benefits. (The calculated rate, based on the actual package of changes adopted by the Board, would have been 6.41%.) The total funded ratio of the plan (for Pensions and Health Insurance combined) is 83.7% based on the accrued liability and the actuarial value of assets as of June 30, 2005.

### Financial Results and Membership Data

Detailed summaries of the financial results of the valuation and membership data used in preparing the valuation are shown in the valuation report. The actuary prepared supporting schedules included in the Actuarial and Statistical Section of the PSERS Comprehensive Annual Financial Report (CAFR), and also prepared the trend data schedules included in the Financial Section of the CAFR.

Qualified actuaries completed the valuation in accordance with accepted actuarial procedures as prescribed by the Actuarial Standards Board. The qualified actuaries are members of the American Academy of Actuaries and are experienced in performing actuarial valuations of public employee retirement systems. To the best of our knowledge, this report is complete and accurate and has been prepared in accordance with generally accepted actuarial principles and practice.

Respectfully submitted,



Kim M. Nicholl, F.S.A.  
Principal, Consulting Actuary



S. Lynn Hill  
Director, Retirement Consulting

## Executive Summary

This report presents the actuarial valuation as of June 30, 2005 for the Public School Employees' Retirement System of Pennsylvania.

The principal valuation results include:

- The employer contribution rate for fiscal year 2006/2007 which is 6.46%.
- The total funded ratio of the plan determined as of June 30, 2005, which is 83.7% based on the accrued liability and the actuarial value of assets for Pensions and Health Insurance as of that date.
- The determination of the actuarial gain or loss as of June 30, 2004 which is a loss of \$2.9 billion.
- Annual disclosure as of June 30, 2004 as required by Statement No. 25 of the Governmental Accounting Standards Board.

The valuation was completed based upon membership and financial data submitted by the Retirement System. Detailed summaries of the financial results of the valuation and membership data used in preparing the valuation are included in the valuation report. The actuary prepared supporting schedules included in the Actuarial and Statistical Section of the PSERS Comprehensive Annual Financial Report (CAFR), and also prepared the trend data schedules included in the Financial Section of the CAFR.

## Changes Since Last Year

### Legislative and Administrative Changes

There were no legislative or administrative changes since the prior valuation.

The benefit provisions and contribution provisions are summarized in Table 13.

### Actuarial Assumptions and Methods

As a result of the July 1, 2000 – June 30, 2005 experience review the actuarial assumptions and methods used to determine the contribution were changed from last year. The changes are effective for the June 30, 2005 actuarial valuation, and were adopted by the Board at its December, 2005 meeting.

The change in method was a minor change in the Entry Age Normal actuarial cost method. Previously the average normal cost rate was the total of the rates for all active members divided by the number of active members. That is, each active member's normal cost rate had an equal weight in the calculation of the average rate. Individual member normal cost rates are still being determined, but the average rate is now a pay-weighted average. The assumptions for post-retirement mortality, death in service, disability retirement, and non-vested withdrawal were changed to better reflect recent experience, and also to reflect expected future improvements in mortality. The assumed rate of inflation was changed from 3.5% to 3.25%, and the assumed real rate of return on assets was increased from 5% to 5.25%. The interest rate assumption is unchanged at 8.5%, and the salary increase assumption has declined by 25 basis points to a career average of 6%.

The actuarial assumptions and methods are outlined in Table 12.

## Contribution Rates

The results of the valuation as of June 30, 2005 determine the employer contribution rate for fiscal year 2006/2007. At its December 2005 meeting the Board adopted a package of assumption changes whose fiscal impact had not previously been determined by the actuary. At the meeting the actuary estimated that the required fiscal year 2006/2007 employer contribution rate would be 6.46% of payroll, and the Board certified this rate. The actuary subsequently confirmed that the 6.46% rate is adequate for funding future benefits. The calculated rate, based on the actual package of changes adopted by the Board, is 6.41% of payroll, including 5.67% of payroll for pension benefits plus 0.74% of payroll for the health insurance premium assistance program.

The average contribution rate payable by the members is 7.21%. Effective January 1, 2002, the employee contribution rate for members who elected to have prior school service and intervening military service converted to Class T-D service increased by 1.25%. However, anyone who enrolls (or re-enrolls) in PSERS on or after July 1, 2001 is *automatically* a member of Class T-D with regard to all subsequent school service and subsequent intervening military service, with a member rate equal to 7.5%. The average member contribution rate of 7.21% is a pay-weighted average of member rates that vary based on date of hire and based on Class T-D membership.

### Reasons for Change in the Rate

The employer contribution rate calculated by the actuary increased from 4.69% for fiscal year 2005/2006 to 6.41% for fiscal year 2006/2007. The increase of 1.72% is due to the following reasons:

· Decrease due to change in normal rate*	(0.38)
· Increase due to payroll growth*	0.11
· Increase due to actuarial loss on assets*	2.31
· Increase due to actuarial loss on liabilities*	0.66
· Increase due to change in health insurance contribution rate*	0.04
· Impact of the 4% floor on employer contribution rate under Act 40*	(0.67)
· Decrease due to FY 2005 over-contribution*	(0.34)
· Decrease due to assumption and method changes	<u>(0.01)</u>
· Total	1.72%

\* Before assumption and method changes.

## Summary of Principal Results

Summarized below are the principal financial results for the Public School Employees' Retirement System based upon the actuarial valuation as of June 30, 2005. Comparable results from the June 30, 2004 valuation are also shown.

Item	June 30, 2005	June 30, 2004
<b>Demographics</b>		
Active Members		
· Number	255,465	246,700
· Average Annual Pay	\$ 41,210	\$ 40,463
Annuitants		
· Number	156,519	151,552
· Average Annual Benefit Payment	\$ 19,343	\$ 18,464
<b>Contribution Rates (as a Percentage of Payroll)</b>		
	(Fiscal Year 2006/2007)	(Fiscal Year 2005/2006)
Employer Contribution Rate:		
· Total Pension Contribution Rate	5.67%	4.00%
· Health Insurance Contribution Rate	<u>0.74</u>	<u>0.69</u>
· Total Contribution Rate Calculated by Actuary	6.41%	4.69%
· Total Contribution Rate Certified by Board	6.46%	4.69%
Member Average Contribution Rate		
· Total Rate	<u>7.21</u> 13.67%	<u>7.16</u> 11.85%
<b>Actuarial Funded Status*</b>		
· Accrued Liability	\$ 61,226.6 Mil	\$ 57,123.0 Mil
· Actuarial Value of Assets	<u>51,219.3</u>	<u>52,094.5</u>
· Unfunded Accrued Liability	\$ 10,007.3	\$ 5,028.5
· Funded Ratio	83.7 %	91.2 %

\* Pensions and Health Insurance combined

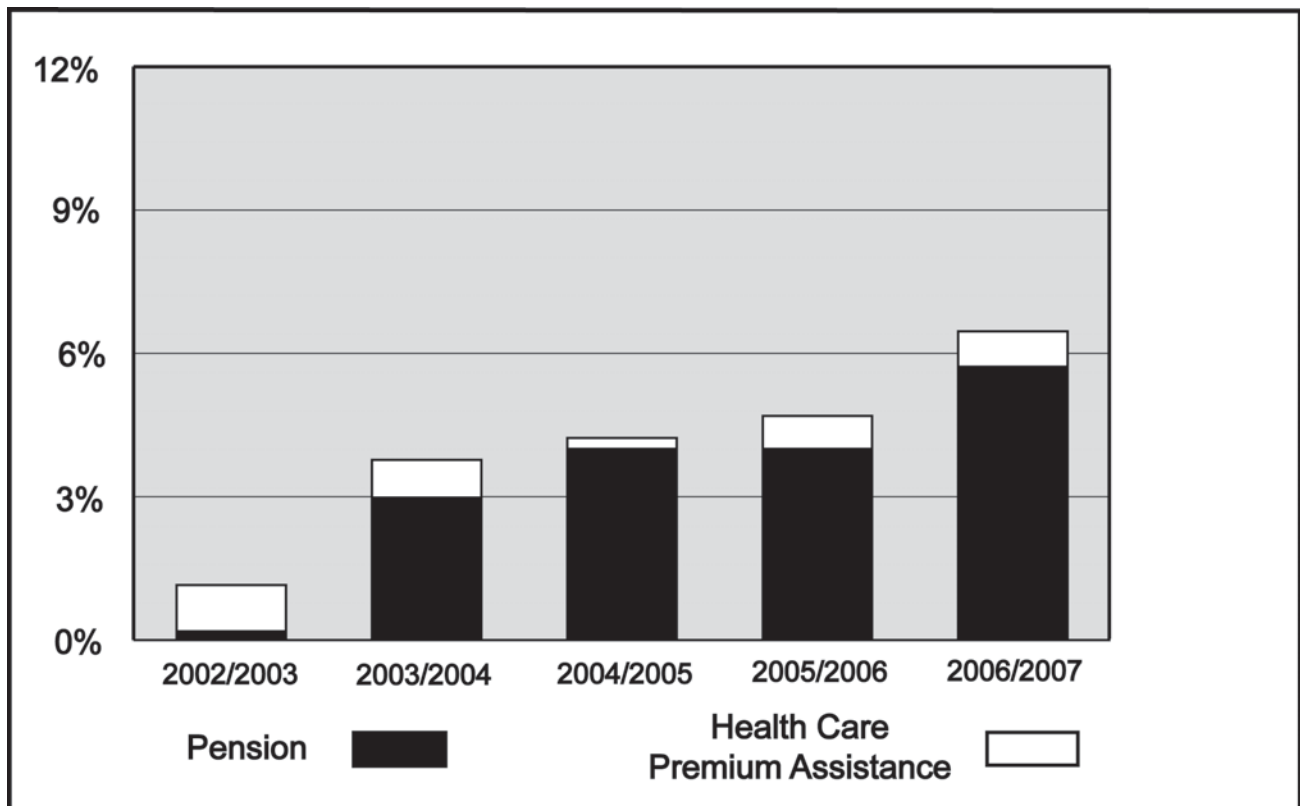
### Five-Year History of Principal Financial Results

#### Five-Year History of Contribution Rates (As a % of Payroll)

Fiscal Year	Member Contributions	Employer Contributions			
		Normal Cost	Unfunded Accrued Liability	Health Care	Total *
2006/2007	7.21%	6.62%	(0.95)%	0.74%	6.46%
2005/2006	7.16	7.61	(4.28)	.69	4.69
2004/2005	7.12	7.48	(7.10)	.23	4.23
2003/2004	7.08	7.25	(4.27)	.79	3.77
2002/2003	7.10	7.20	(10.03)	.97	1.15

\* Certified by the Board.

The following chart shows a five-year history of employer contribution rates:



## Funded Ratio

The financing objective of the System is to:

- Fully fund all current costs based on the normal contribution rate determined under the funding method; and
- Liquidate the unfunded accrued liability based on the amortization schedules as required by the retirement code, i.e., a schedule of 10 or 30 years for each change in the unfunded accrued liability according to Act 40.

The total contribution rate of 6.46% of payroll payable by employers, when taken together with the contributions payable by the members and asset returns, is sufficient to achieve the financing objective.

The System's total funded ratio on the funding basis is measured by comparing the actuarial value of assets (based on a 5-year moving average market value) with the accrued liability. The accrued liability for Pensions is the present value of benefits accumulated to date under the System's funding method and reflects future pay increases for active employees. The accrued liability for Health Insurance equals the assets in the Health Insurance account.

On this basis, the System's total funded ratio (for Pensions and Health Insurance combined) is 83.7% as of June 30, 2005. This funded ratio is based on an actuarial value of assets of \$51.2 billion and an accrued liability of \$61.2 billion. The funded ratio for Pensions alone is 83.6% as of June 30, 2005, based on an actuarial value of assets of \$51.1 billion, and an accrued liability of \$61.1 billion.

### Reasons for Change in the Funded Ratio

The total funded ratio decreased from 91.2% as of June 30, 2004 to 83.7% as of June 30, 2005. The change in assumptions and methods caused the funded ratio to decrease by 0.9%. The remaining decrease is due to the asset and liability losses.

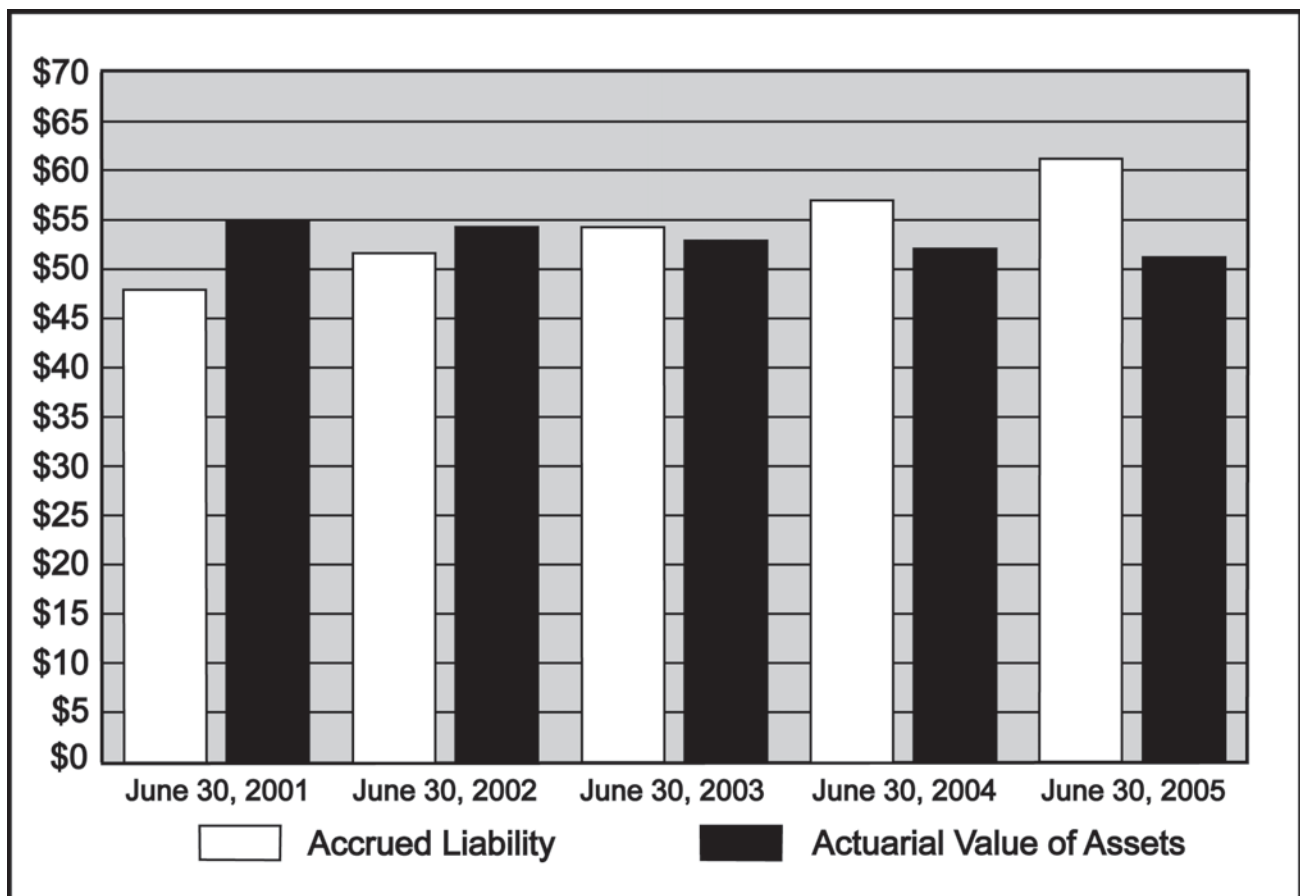
**Five-Year History of  
Total Funded Ratio\***  
(Dollar Amounts in Millions)

Valuation as of June 30	Accrued Liability	Actuarial Value of Assets	Unfunded Accrued Liability	Funded Ratio
2005	\$ 61,226.6	\$ 51,219.3	\$ 10,007.3	83.7%
2004	57,123.0	52,094.5	5,028.5	91.2
2003	54,443.8	52,900.5	1,543.3	97.2
2002	51,796.5	54,296.4	(2,499.9)	104.8
2001	47,917.3	54,830.3	(6,913.0)	114.4

\* For Pensions and Health Insurance

The following chart shows a five-year history of the accrued liability and the actuarial value of assets:

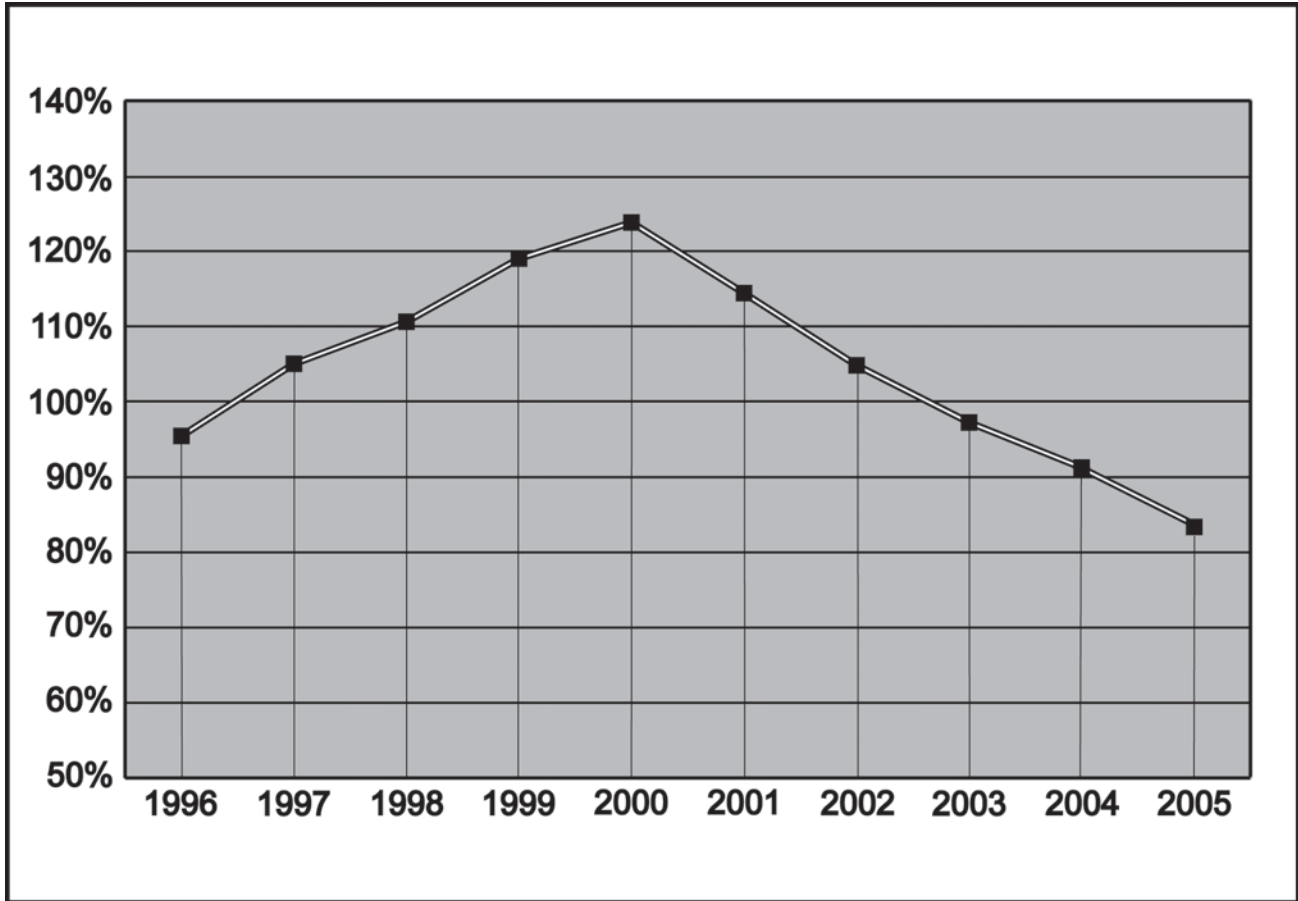
**Five-Year History of Accrued Liability and Actuarial Value of Assets**  
(Dollar Amounts in Billions)





The following chart shows a ten-year history of the total funded ratio for Pensions and Health Insurance:

**Ten-Year History of Funded Ratio  
(1996 - 2005)**



## GASB No. 25 Disclosure

Statement No. 25 of the Governmental Accounting Standards Board established reporting standards for the annual financial reports of defined benefit pension plans. The System complied with Statement No. 25 beginning with the June 30, 1996 valuation. The statement requires disclosure of the “schedule of funding progress” and the “schedule of employer contributions” in the System’s financial statements.

The “schedule of funding progress” shows historical trend information about the System’s actuarial value of pension assets, the actuarial accrued liability for pensions and the unfunded actuarial accrued liability for pensions. The actuarial funded ratio for pensions is measured by comparing the actuarial value of pension assets (based on a 5-year moving average market value) with the accrued liability for pensions. The accrued liability is the present value of pension benefits accumulated to date under the System’s funding method and reflects future pay increases for active employees. On this basis, the System’s funded ratio for pensions is 83.6% as of June 30, 2005. This funded ratio is based on an actuarial value of pension assets of \$51.1 billion and an accrued liability for pensions of \$61.1 billion.

The “schedule of employer contributions” shows historical trend information about the annual required contributions (ARC) for pensions of the employer and the percentage of the ARC contributed to the System. The ARC is equal to the normal cost for pensions plus amortization of the unfunded actuarial accrued liability for pensions. The maximum period of amortizing the unfunded actuarial accrued liability permitted by GASB No. 25 is 40 years. The maximum amortization period decreases to 30 years in 2006. The employer contributions to the System are equal to the normal cost plus a payment towards each change in the unfunded accrued liability, which are amortized over 10 or 30-year periods. The actual employer pension contributions for the five fiscal years ending June 30, 2004 are equal to 100% of the ARC while the actual employer pension contributions for the fiscal year ending June 30, 2005 are 46% of the ARC. Refer to Table 8 for additional detail.

## Rate of Return

The investment return of the trust fund (i.e. total return including both realized and unrealized gains and losses) for fiscal years 2000/2001 through 2004/2005 is shown in the table below. The return based on the actuarial value of assets used for determining annual contribution rates is also shown.

The rate of return on market value reflects the investment earnings on the market value of assets from the beginning of the fiscal year to the end of the fiscal year. The actuarial assets are the assets recognized for valuation purposes. Actuarial assets are based on a smoothed market value that spreads the difference between the actual and expected return (beginning with the 2001/2002 fiscal year) over a period of five years. The rate of return on the actuarial value of assets is a measure of the increase in the actuarial value of assets from the beginning of the fiscal year to the end of the fiscal year.

Fiscal Year	Rate of Return Based on	
	Market Value	Actuarial Value
2004/2005*	12.9%	3.2%
2003/2004*	19.7	2.6
2002/2003*	2.7	1.4
2001/2002*	(5.3)	2.7
2000/2001	(7.4)	14.3

\* Market value rate of return provided by Wilshire Associates Incorporated, the PSERS investment consultant.

**Table 1**  
**Summary of Results of Actuarial Valuation**  
**As of June 30, 2005**  
(Dollar Amounts in Thousands)

Item	Amount
<b>Member Data</b>	
1. Number of Members	
a) Active Members	255,465
b) Inactive Members and Vestees	58,720
c) Annuitants, Beneficiaries and Survivor Annuitants	156,519
d) Total	<u>470,704</u>
2. Annualized Salaries	\$ 10,527,668
3. Annual Annuities	\$ 3,027,550
<b>Valuation Results</b>	
4. Present Value of Future Pension Benefits	
a) Active Members	\$ 47,470,869
b) Inactive Members and Vestees	660,394
c) Annuitants, Beneficiaries and Survivor Annuitants	26,954,108
d) Total	<u>\$ 75,085,371</u>
5. Present Value of Future Pension Normal Cost	
a) Active Members	\$ 7,275,650
b) Employer	6,680,277
c) Total	<u>\$ 13,955,927</u>
6. Pension Accrued Liability	
a) Active Members (4a) - (5c)	\$ 33,514,942
b) Inactive Members and Vestees	660,394
c) Annuitants, Beneficiaries and Survivor Annuitants	26,954,108
d) Total	<u>\$ 61,129,444</u>
7. Health Care Premium Assistance Payments	\$ 97,137
8. Total Accrued Liability (6) + (7)	\$ 61,226,581
9. Actuarial Value of Assets	\$ 51,219,293
10. Funded Status (9) / (8)	83.7 %
11. Unfunded Accrued Liability (8) - (9)	\$ 10,007,288
12. Total Normal Cost Rate	13.83 %
13. Member Contribution Rate	7.21 %
14. Employer Normal Cost Rate (12 - (13)	6.62 %
<b>Employer Annual Funding Requirement for Fiscal 2006/2007</b>	
15. Employer Contribution Rate Calculated by Actuary	
a) Normal	6.62 %
b) Unfunded Accrued Liability	<u>(0.95)</u>
c) Preliminary Pension Rate	5.67 %
d) Preliminary Pension Rate with 4% Floor	5.67
e) Health Insurance Premium Assistance	<u>0.74</u>
f) Total Rate	6.41 %
16. Employer Contribution Rate Certified by Board	6.46 %

**Table 2**  
**Summary of Sources of Employer Contribution Rate**  
**As of June 30, 2005**  
(Dollar Amounts in Thousands)

	Funding Period	Funding Period Beginning July 1	Initial Amount of Liability	Outstanding Balance as of July 1, 2004	Annual Payment	
					Amount	Percent *
1. Amortization of:						
a) July 1, 2001 Fresh Start Unfunded Base	10 Years	2002	\$ (9,137,130)	\$ (7,733,753)	\$ (1,510,937)	(12.78)%
b) Asset Method Change at July 1, 2001 due to Act 38	10 Years	2002	(4,638,306)	(3,925,906)	(767,001)	(6.49)%
c) 2001 Changes	30 Years	2002	7,570,507	6,991,515	668,111	5.65%
d) 2002 Changes	30 Years	2003	3,014,171	3,023,070	286,101	2.41 %
e) 2002 COLA	10 Years	2003	463,795	432,493	76,694	0.65 %
f) 2003 COLA	10 Years	2004	754,524	828,370	135,375	1.15 %
g) 2003 Changes	30 Years	2004	3,229,593	3,475,898	326,059	2.76 %
h) 2004 Changes	30 Years	2005	2,903,093	3,149,856	293,096	2.48 %
i) 2005 Changes	30 Years	2006	3,765,745	3,765,745	380,189	3.22 %
Total Amortization Payments				10,007,288	(112,313)	(0.95)%
2. Employer Normal Cost Rate						6.62 %
3. Preliminary Pension Rate (1) + (2)						5.67 %
4. Preliminary Pension Rate with 4% Floor -- Maximum of (3) and 4%						5.67 %
5. Health Insurance Premium Assistance Rate						0.74 %
6. Final Total Employer Contribution Rate Calculated by Actuary (4) + (5)						6.41 %
7. Final Total Employer Contribution Rate Adopted by Board						6.46 %

\* Based on Estimated Employer Payroll for Fiscal Year Ending 2007 of \$11,821,951.

**Table 3**  
**Determination of Health Insurance Contribution Rate**  
**For Fiscal Year 2006/2007**  
(Dollar Amounts in Thousands)

Item	Amount
1. Estimated Number of Eligible Annuitants in Fiscal Year 2007/2008	112,300
2. Estimated Number of Eligible Annuitants Who Elect Coverage	72,995
3. Estimated Annual Health Insurance Premium Assistance Payments During Fiscal Year 2007/2008 (2) x \$100 x 12	\$ 87,594
4. Estimated Health Insurance Premium Assistance Administrative Expenses During Fiscal Year 2007/2008	2,113
5. Total Estimated Health Insurance Premium Assistance Account Disbursements During Fiscal Year 2007/2008 (3) + (4)	\$ 89,707
6. Estimated Balance in Health Insurance Premium Assistance Account for Prior Fiscal Year	\$ 3,262
7. Estimated Shortfall in Health Insurance Premium Assistance Account (5) - (6)	\$ 86,445
8. Required Health Insurance Premium Assistance Contribution Rate	
(a) Estimated 2006/2007 Payroll	\$ 11,821,951
(b) Required Health Insurance Premium Assistance Contribution Rate (7) / (8a) (rounded up)	0.74%

**Table 4**  
**Summary of Market Value of Plan Assets**  
**As of June 30, 2005**  
(Dollar Amounts in Thousands)

<b>Market Value</b>	
1. Market Value of Assets as of June 30, 2004	\$ 48,484,506
2. Contributions During Fiscal Year 2004/2005	1,246,118
3. Disbursements During Fiscal Year 2004//2005	3,741,395
4. Investment Return During Fiscal Year 2004/2005	
a) Net Investment Return	\$ 6,078,851
b) Administrative Expenses	34,546
c) Investment Return After Expenses (a) - (b)	\$ 6,044,305
5. Market Value of Assets as of June 30, 2005 (1) + (2) - (3) + (4c)	\$ 52,033,534
6. Rate of Return (per Wilshire)	12.87 %
<b>Asset Allocation by Account</b>	
1. Members' Savings Account	\$ 9,116,347
2. Annuity Reserve Account	26,954,108
3. State Accumulation Account	15,865,942
4. Health Care Account	97,137
5. Total (1) + (2) + (3) + (4)	\$ 52,033,534

**Table 5**  
**Derivation of Actuarial Value of Assets**  
**As of June 30, 2005**  
(Dollar Amounts in Thousands)

1. Market Value of Assets as of June 30, 2005					\$ 52,033,534
2. Determination of Deferred Gain (Loss)					
	<u>Return on Assets</u>				
<u>Year</u>	<u>Actual</u>	<u>Expected</u>	<u>Difference</u>	<u>% Deferred</u>	<u>Deferred Amount</u>
2004/2005	\$ 6,044,305	\$ 4,321,981	\$ 1,722,324	80%	\$ 1,377,859
2003/2004	8,201,871	4,404,561	\$ 3,797,310	60%	2,278,386
2002/2003	985,646	4,525,288	(3,539,642)	40%	(1,415,857)
2001/2002	(2,555,630)	4,575,102	(7,130,732)	20%	(1,426,147)
					<u>\$ 814,241</u>
3. Actuarial Value of Assets (1) - (2)					\$ 51,219,293
4. Actuarial Rate of Return *					3.19%

\* The actuarial rate of return is the investment return based on the change in the actuarial value of the assets from the June 30, 2004 valuation to the June 30, 2005 valuation.

**Table 6**  
**Analysis of Change in Unfunded Accrued Liability**  
**As of June 30, 2005**  
(Dollar Amounts in Thousands)

Item	Amount
1. Unfunded Accrued Liability at June 30, 2004	\$ 5,028,521
2. Interest Credit at 8.50% to June 30, 2005	427,424
3. Contributions toward Unfunded Accrued Liability	(785,598)
4. Change due to FY 2005 Over-Contribution	(400,366)
5. Expected Unfunded Accrued Liability at June 30, 2005 (1) + (2) - (3) + (4)	\$ 5,841,177
6. Actual Unfunded Accrued Liability at June 30, 2005	\$ 10,007,288
7. Increase (Decrease) from Expected (6) - (5)	\$ 4,166,111
9. Reasons for Increase (Decrease)	
(a) Experience (Gains) Losses	
(i) Loss from Investment Return on Actuarial Value of Assets	\$ 2,701,891
(ii) Gain from Salary Increases Less than Expected	(118,605)
(iii) Gain from Retirement and Other Separation Experience	766,982
(iv) Loss from Annuitants' Mortality Experience	122,856
Subtotal	\$ 3,473,124
(b) Change in Assumptions and Funding Method	692,987
(c) Grand Total	\$ 4,166,111



**Table 7**  
**Schedule of Funding Progress**  
**GASB Statement No. 25 Disclosure**  
(Dollar Amounts in Thousands)

Valuation as of June 30	Actuarial Value of Assets	Actuarial Accrued Liability	Funded (Unfunded) Actuarial Accrued Liability	Funded Ratio	Covered Payroll	Unfunded Accrued Liability as a Percentage of Covered Payroll
2005	\$ 51,122,156	\$ 61,129,444	\$ (10,007,288)	83.6	\$ 10,527,668	(95.1) %
2004	51,949,622	56,978,143	(5,028,521)	91.2	10,030,705	(50.1)
2003	52,770,018	54,313,328	(1,543,310)	97.2	9,652,881	(16.0)
2002	54,193,064	51,693,207	2,499,857	104.8	9,378,944	26.7
2001	54,783,928	47,870,922	6,913,006	114.4	9,414,884	73.4
2000	49,241,819	39,771,604	9,470,215	123.8	8,939,598	105.9

\* The amounts reported do not include assets or liabilities for Health Insurance. In previous valuations, the amounts reported did include assets and liabilities for Health Insurance.

**Table 8**  
**Schedule of Employer Contributions**  
**GASB Statement No. 25 Disclosure**  
(Dollar Amounts in Thousands)

Fiscal Year Ended June 30	Annual Required Contribution	Actual Employer Contribution	Percentage Contributed
2005	\$ 945,107	\$ 431,556	46 %
2004	321,901	321,091	100 %
2003	20,831	20,831	100 %
2002	539	539	100 %
2001	158,193	158,193	100 %
2000	390,504	390,504	100 %

The information presented above was determined as part of the actuarial valuation as of two years prior to the dates indicated (i.e. the contribution determined by the valuation completed as of June 30, 2002 was contributed in the fiscal year ending June 30, 2004).

Additional information as of the latest actuarial valuation follows:

Valuation Date:	6/30/2005
Actuarial Cost Method:	Entry Age
Amortization Method:	Level percent closed
Remaining Amortization Period:	40 years
Asset Valuation Method:	5-year smoothed market

Actuarial Assumptions:	
- Investment Rate of Return *	8.50%
- Projected Salaried Increases *	6.25%

* Includes Inflation at:	3.50%
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**Table 9**  
**Solvency Test**  
**Comparative Summary of Accrued Liability**  
**and Actuarial Value of Assets\***  
(Dollar Amounts in Thousands)

Valuation as of June 30	(1) Active Member Contributions	(2) Retirees and Beneficiaries	(3) Active Member Employer Financed	Actuarial Value of Assets	Portion of Accrued Liability Covered by Valuation Assets		
					(1)	(2)	(3)
2005	\$ 9,116,347	\$ 27,051,245	\$ 25,058,989	\$ 51,219,293	100%	100%	60%
2004	8,755,109	24,482,234	23,885,657	52,094,479	100%	100%	79%
2003	8,282,753	22,094,109	24,066,913	52,900,465	100%	100%	94%
2002	7,780,370	19,978,567	24,037,574	54,296,368	100%	100%	100%
2001	7,464,404	15,802,140	24,650,750	54,830,300	100%	100%	100%
2000	6,775,934	16,036,880	17,010,018	49,293,047	100%	100%	100%

\*The amounts reported include assets and liabilities for Pensions and Health Insurance.

**Table 10**  
**History and Projection of**  
**Contribution Rates and Funded Ratios \***

Fiscal Year	Employer Payroll	Contribution Rates						Funded Ratio
		Member	Employer Normal Cost Rate	Unfunded Liability Rate	Preliminary Employer Pension Rate	Health Insurance Rate	Total Employer Rate	
1997/1998	\$ 8,091,481	5.65 %	6.44 %	2.17 %	8.61 %	0.15 %	8.76 %	110.6 %
1998/1999	8,247,602	5.69	6.33	(0.44)	5.89	0.15	6.04	119.0
1999/2000	8,939,598	5.72	6.40	(2.04)	4.36	0.25	4.61	123.8
2000/2001	9,414,884	5.77	6.29	(4.65)	1.64	0.30	1.94	114.4
2001/2002	9,378,944	6.43	5.63	(6.05)	(0.42)	1.09	1.09	104.8
2002/2003	9,652,881	7.10	7.20	(10.03)	1.00	0.97	1.15	97.2
2003/2004	10,030,705	7.08	7.25	(4.27)	2.98	0.79	3.77	91.2
2004/2005	11,062,589	7.12	7.48	(7.10)	4.00	0.23	4.23	83.7
2005/2006	11,505,093	7.16	7.61	(4.28)	4.00	0.69	4.69	80.9
2006/2007	<b>11,821,951</b>	<b>7.21</b>	<b>6.62</b>	<b>(0.95)</b>	<b>5.67</b>	<b>0.74</b>	<b>6.46 **</b>	<b>80.7</b>
2007/2008	12,015,696	7.23	6.60	(0.21)	6.39	0.76	7.15	81.6
2008/2009	12,272,752	7.25	6.58	(0.57)	6.01	0.77	6.78	81.3
2009/2010	12,526,362	7.27	6.57	(1.51)	5.06	0.77	5.83	80.3
2010/2011	12,778,938	7.30	6.54	(1.82)	4.72	0.78	5.50	79.1
2011/2012	13,039,623	7.32	6.53	(1.85)	4.68	0.78	5.46	77.9
2012/2013	13,315,696	7.35	6.51	15.24	21.75	0.77	22.52	79.2
2013/2014	13,611,415	7.37	6.49	14.31	20.80	0.77	21.57	80.4
2014/2015	13,928,825	7.39	6.48	13.00	19.48	0.76	20.24	81.5
2015/2016	14,283,124	7.41	6.46	12.67	19.13	0.76	19.89	82.5
2016/2017	14,675,532	7.43	6.45	12.33	18.78	0.74	19.52	83.5

\* The projection of contribution rates is based on the assumption that there are no changes in demographics or economic assumptions, no changes in benefit provisions, and no actuarial gains or losses other than gains or losses on the actuarial value of assets that result from recognizing currently deferred gains or losses on the market value of assets.

\*\* 6.46% total employer contribution rate for fiscal year 2006/2007 adopted by Board on December 9, 2005.

**Table 11**  
**History and Projection of Annuitants, Beneficiaries,**  
**Survivor Annuitants and Active Members**

Valuation as of June 30	New Annuitants During the Year	Annuitant Deaths During the Year	Annuitants at End of Year	Beneficiaries and Survivor Annuitants at End of Year	Total Annuitants, Beneficiaries and Survivor Annuitants	Active Members
1996			113,007	5,719	118,726	213,906
1997			118,137	5,987	124,124	215,077
1998			120,665	6,149	126,814	220,703
1999			126,448	6,421	132,869	223,495
2000			127,404	6,654	134,058	234,210
2001			125,880	6,836	132,716	243,311
2002			134,300	7,114	141,414	242,616
2003			138,383	7,310	145,693	246,700
2004			143,997	7,555	151,552	247,901
2005			<b>148,727</b>	<b>7,792</b>	<b>156,519</b>	<b>255,465</b>
2006	12,442	4,080	157,089	8,209	165,298	255,465
2007	11,351	4,228	164,212	8,600	172,812	255,465
2008	11,712	4,405	171,519	8,959	180,478	255,465
2009	12,056	4,585	178,990	9,298	188,288	255,465
2010	12,096	4,759	186,327	9,620	195,947	255,465
2011	11,651	4,931	193,047	9,925	202,972	255,465
2012	11,732	5,114	199,665	10,225	209,890	255,465
2013	11,693	5,289	206,069	10,523	216,592	255,465
2014	11,527	5,465	212,131	10,816	222,947	255,465
2015	11,379	5,646	217,864	11,110	228,974	255,465

**Table 12**  
**Description of Actuarial Assumptions and Methods**

**ASSUMPTIONS**

**Interest Rate:** 8½% per annum, compounded annually (adopted as of June 30, 1990). The components are 3.25% for inflation and 5.25% for the real rate of return (both adopted as of June 30, 2005). Actuarial equivalent benefits are determined based on 4% (since 1960).

**Separation From Service:** Illustrative rates of assumed separation from service are shown in the following table. (Rates of non-vested withdrawal, of death, and of disability were adopted as of June 30, 2005; other rates were adopted as of June 30, 2000):

Age	Annual Rate of:						
	Non-Vested Withdrawal	Vested Withdrawal*		Death	Disability	Early Retirement**	Superannuation Retirement
		Less than 10 Years of Service	10 or More Years of Service				
<b>Males</b>							
25	12.40 %	5.50 %	1.40 %	.042 %	.024 %		
30	10.00	3.00	1.40	.057	.024		
35	11.00	3.00	1.10	.062	.100		
40	11.00	3.00	.80	.072	.180		
45	11.00	3.00	.50	.100	.180		
50	11.00	3.00	1.78	.152	.280		24.00 %
55	10.50	3.00	3.50	.252	.430	10.00 %	24.00
60	9.00	2.40	4.50	.467	.580	10.00	28.00
65				.870	.100		20.00
69				1.335	.100		20.00
<b>Females</b>							
25	14.10 %	9.50 %	4.00 %	.019 %	.040 %		
30	14.10	7.50	4.00	.023	.040		
35	14.10	5.50	2.00	.031	.080		
40	10.90	3.50	1.00	.043	.130		
45	10.90	3.00	.55	.061	.180		
50	10.90	3.00	1.50	.085	.250		10.00 %
55	10.90	3.00	3.00	.146	.480	10.00	10.00
60	10.90	3.50	5.90	.284	.480	15.00	25.00
65				.561	.160		28.00
69				.866	.160		20.00

\* Vested Withdrawal - At least 5 years service but not eligible for Early or Superannuation retirement.

\*\* Early Retirement - Age 55 with 25 years service, but not eligible for Superannuation retirement.

Description of Actuarial Assumptions and Methods (Continued)

**Death After Retirement:** The Uninsured Pensioners 1994 Mortality Table (UP94) with mortality improvements projected 10 years, and with age set back one year for males and females, adopted in 2005, are used to project mortality for healthy annuitants and for dependent beneficiaries. Special mortality tables based on PSERS' experience are used for disability retirements. (The 1995 George B. Buck Mortality Tables, rated forward one year for males and unadjusted for females, adopted in 2000, are used to determine actuarial equivalent benefits.)

**Salary Increase:** Effective average of 6% per annum, compounded annually (adopted as of June 30, 2005). The components are 3.25% for inflation, 1% for real wage growth and 1.75% for merit or seniority increases (adopted as of June 30, 2000). Representative values are as follows:

Age	Annual Rate of Salary Increase
20	12.00 %
30	9.00
40	7.00
50	4.75
55	4.50
60	4.25
65	4.25
69	4.25

**MISCELLANEOUS**

**Option 4 Elections:** 100% of members are assumed to elect a refund of contributions and a reduced annuity.

**Withdrawal Annuity:** 90% of members are assumed to commence payment immediately and 10% are assumed to defer payment to superannuation age.

**METHODS**

**Calculations:** The actuarial calculations were performed by qualified actuaries in accordance with accepted actuarial procedures, based on the current provisions of the retirement system, and on actuarial assumptions that are internally consistent and reasonably based on the actual experience of the System.

**Actuarial Cost Method:** Entry Age Normal Cost Method (modified slightly as of June 30, 2005 to use a pay-weighted average normal contribution rate). The results of each June 30 valuation normally determine the employer contribution rate for the second succeeding fiscal year. The outstanding balance of the unfunded accrued liability as of June 30, 2001 and the decrease in the unfunded accrued liability due to the actuarial asset method change provided by Act 38 continue to be amortized over a 10-year period, with level dollar funding, beginning July 1 2002. The increases in the unfunded

## Description of Actuarial Assumptions and Methods (Continued)

accrued liability due to the July 1, 2002 and July 1, 2003 cost-of-living adjustments provided by Act 38 were both recognized at June 30, 2002 and continue to be amortized over a 10-year period, with level dollar funding starting on July 1, 2003 and July 1, 2004, respectively. All other changes in the unfunded accrued liability at June 30, 2002 – including the Act 9 benefit changes – are amortized over a 30-year period, with level dollar funding starting on July 1, 2003. Post June 30, 2002 benefit improvements for active members and retirees are amortized over a 10-year period with level dollar funding. Post June 30, 2002 gains and losses, and changes in the unfunded accrued liability resulting from changes in actuarial assumptions and methods, are amortized over a 30-year period with level dollar funding. Act 40 also provided a 4.00% floor on the employer pension rate.

**Asset Valuation Method:** A five-year moving market average value of assets that recognizes the 8.5% actuarial expected investment return immediately and spreads the difference between the actual and expected return (beginning with the 2000/2001 fiscal year) over a period of five years (adopted as of June 30, 2001).

**Determination of Health Care Contribution Rate:** This is the rate necessary to establish reserves sufficient to provide premium assistance payments to all participating eligible annuitants during the fiscal year that immediately follows the year the employer contribution is made.

**DATA**

**Census and Assets:** The valuation was based on members of the System as of June 30, 2005 and does not take into account future members. All census data was supplied by the System and was subject to reasonable consistency checks. The actuary adjusts the data to account for service and pay earned by members on or before the valuation that is not reported by the System until after the actuarial valuation is performed. Asset data was supplied by the System.



## Table 13

### Summary of Benefit and Contribution Provisions

#### MEMBERSHIP

For valuation purposes, all employees are considered to be full coverage. All employees who become members on and after January 1, 1966 are members of the dual coverage group. Dual coverage members contribute to both PSERS and to Social Security.

#### BENEFITS

##### Superannuation Annuity

Eligibility	Age 62, or age 60 with 30 years of service, or 35 years of service regardless of age.
Amount	2.5% of final average salary times years of school service and intervening military service. 2% of final average salary for non-school service and for members who do not elect Class T-D coverage. Minimum of \$100 per year of service. "Final average salary" means the highest average annual salary for any 3 years of service.  Annual salary is subject to a limit of \$200,000, as adjusted under Section 401(a)(17).  For members who elect coverage under Class T-D, the maximum benefit is equal to the limit established by Section 415 of the Internal Revenue Code.

##### Early Retirement Annuity

Eligibility	Age 55 with 25 years of service.
Amount	Accrued benefit as of date of retirement, reduced 1/4% for each month by which commencement of payments precedes Superannuation Age.  For members who elect coverage under Class T-D, the maximum benefit is equal to the limit established by Section 415 of the Internal Revenue Code.

##### Withdrawal Annuity

Eligibility	5 years of service.
Amount	Accrued benefit deferred to superannuation retirement age or an actuarially reduced benefit payable immediately. Actuarially equivalent benefits are based on 4% interest and the 1995 George B. Buck mortality tables, rated forward one year for males and unadjusted for females.

## Summary of Benefit and Contribution Provisions (Continued)

**Disability Annuity**

Eligibility	5 years of service.
Amount	The standard single life annuity if the total number of credited service is greater than 16.667, otherwise the standard single life annuity multiplied by the lesser of the following ratios: $(Y^*/Y)$ or $(16.667/Y)$ where Y is the number of years of credited service and Y* is the total years of credited service if the member were to continue as a school employee until superannuation retirement age (or at current age, if later). Minimum of \$100 per year of service.

**Return of Contributions**

Eligibility	Death or separation from service and member does not qualify for other benefits.
Amount	Refund of accumulated deductions includes interest (less annuity payments received prior to death in the case of a retired member).

**Death Benefit**

Eligibility	Death of an active member or vestee who was eligible to receive an annuity.
Amount	The present value of the annuity which would have been effective if the member retired on the day before death. Option 1 (see below) assumed payable if no other option elected.

**Normal and Optional Forms of Benefits**

Normal Form:	Life annuity with a guaranteed payment equal to member contributions with interest.
Option 1:	Reduced benefit with refund of balance of present value of annuity at retirement over payments received. If balance is less than \$5,000, benefit is paid in lump sum; otherwise, beneficiary may elect annuity and/or lump sum.
Option 2:	Joint and 100% survivorship annuity.
Option 3:	Joint and 50% survivorship annuity.
Option 4:	Benefit of equivalent actuarial value, including lump sum payment of member contributions.

## Summary of Benefit and Contribution Provisions (Continued)

**Postemployment Health Care Insurance Premium Assistance**

Eligibility	Retired members who: <ul style="list-style-type: none"> <li>(a) have 24½ or more years of service, or</li> <li>(b) are disability annuitants, or</li> <li>(c) have 15 or more years of service and who both terminated school service and retired after attaining superannuation age and</li> <li>(d) participate in the PSERS Health Options Program or in an employer-sponsored health insurance program.</li> </ul>
Amount	Participating eligible annuitants receive health insurance premium assistance payments from the Health Insurance Account equal to the lesser of \$100 per month or the actual monthly premium. All administrative expenses necessary to operate the health insurance premium assistance program are to be funded by the Health Insurance Account. The Health Insurance Account is credited with contributions of the Commonwealth and the employers.

**CONTRIBUTIONS**

By Members	Members who elected coverage under Class T-D and who were most recently enrolled prior to July 22, 1983 contribute at a rate of 6½% of compensation, while members who elected coverage under Class T-D and who were most recently enrolled on or after July 22, 1983 contribute at a rate of 7½% of compensation. Members who did not elect coverage under Class T-D and who were most recently enrolled prior to July 22, 1983 contribute at a rate of 5¼% of compensation, while members who did not elect coverage under Class T-D and who were most recently enrolled on or after July 22, 1983 and prior to July 1, 2001 contribute at a rate of 6¼% of compensation. Anyone who enrolls or re-enrolls on or after July 1, 2001 automatically has coverage under class T-D for subsequent school service and subsequent intervening military service, and must contribute at a rate of 7½% of compensation. Reduction in rate for a joint coverage member: 40% of Social Security tax, exclusive of disability and medical coverage portion.
By Commonwealth and employers	Balance of required contribution determined as normal contribution, accrued liability contribution, supplemental annuity contribution, experience adjustment factor and premium assistance contribution, is funded by the Commonwealth and the employers.

**Table 14**  
**Summary of Membership Data**  
**As of June 30, 2005**  
(Dollar Amounts in Thousands)

**Active Members \***

<b>Item</b>	<b>Male</b>	<b>Female</b>	<b>Total</b>
Number of Members	70,774	184,691	255,465
Annual Salaries **	\$ 3,355,836	\$ 7,171,833	\$ 10,527,668
Average Age	44.9	45.0	45.0
Average Service	12.6	11.0	11.5

\* Excludes 58,720 inactive members and vestees.

\*\* These salaries shown in the table above represent a rate of pay for members who were in active service on June 30, 2005.

**Annuitants and Beneficiaries**

<b>Item</b>	<b>Number</b>	<b>Annual Annuities</b>	<b>Average Annuities</b>	<b>Average Age</b>
Annuitants (Normal, Early and Withdrawal)	141,763	\$ 2,855,901	\$ 20,146	69.8
Survivors and Beneficiaries	7,792	65,406	8,394	75.8
Disabled Annuitants	6,964	106,243	15,256	62.3
<b>Total</b>	<b>156,519</b>	<b>\$ 3,027,550</b>	<b>19,343</b>	<b>69.8</b>

**Exhibit I**  
**Active Membership Data as of June 30, 2005**  
**Number and Average Annual Salary**

Age	Years of Service									Total
	0 - 4	5 - 9	10 - 14	15 - 19	20 - 24	25 - 29	30 - 34	35 - 39	40 +	
<b>Under 25</b>	6,922	84								7,006
	\$26,535	\$25,554								\$26,523
<b>25 - 29</b>	17,823	5,173	26							23,022
	\$33,149	\$43,263	\$35,472							\$35,424
<b>30 - 34</b>	9,595	13,158	2,667	67						25,487
	\$29,826	\$44,945	\$52,923	\$37,430						\$40,068
<b>35 - 39</b>	9,077	7,884	7,333	2,185	70					26,549
	\$23,724	\$41,541	\$54,783	\$57,562	\$39,061					\$40,419
<b>40 - 44</b>	11,418	7,640	4,542	5,341	1,858	158				30,957
	\$19,724	\$32,371	\$47,758	\$59,433	\$58,412	\$37,619				\$36,222
<b>45 - 49</b>	10,783	9,493	5,601	4,683	4,745	3,473	202			38,980
	\$19,622	\$29,636	\$40,648	\$53,739	\$62,974	\$64,502	\$40,662			\$38,566
<b>50 - 54</b>	7,438	7,674	6,552	6,151	4,187	9,303	7,968	109		49,382
	\$21,561	\$30,920	\$40,332	\$50,151	\$59,641	\$68,924	\$71,410	\$45,251		\$49,314
<b>55 - 59</b>	4,757	4,040	4,118	4,842	3,697	3,794	7,860	2,062	21	35,191
	\$21,529	\$29,487	\$36,826	\$45,191	\$53,694	\$61,997	\$72,180	\$76,011	\$54,685	\$49,756
<b>60 - 64</b>	2,489	1,799	1,659	2,031	1,634	1,529	909	637	176	12,863
	\$18,574	\$25,505	\$30,938	\$37,980	\$42,747	\$49,223	\$58,522	\$75,205	\$74,249	\$37,305
<b>Over 64</b>	1,802	1,039	791	753	512	479	361	161	130	6,028
	\$12,718	\$18,046	\$21,862	\$27,205	\$29,823	\$34,348	\$37,221	\$48,282	\$68,972	\$23,448
<b>Total</b>	82,104	57,984	33,289	26,053	16,703	18,736	17,300	2,969	327	255,465
	\$24,904	\$36,122	\$44,246	\$50,754	\$56,482	\$63,946	\$70,010	\$73,205	\$70,895	\$41,210

**Exhibit II**  
**The Number and Average Annual Annuity**  
**As of June 30, 2005**

**Retired on Account of Superannuation, Early Retirement and**  
**Those in Receipt of Withdrawal Annuities**

Age	Years of Service									Total
	0 - 4	5 - 9	10 - 14	15 - 19	20 - 24	25 - 29	30 - 34	35 - 39	40 +	
<b>Under 50</b>	11	1,182	1,351	436	137	27	4			3,148
	\$2,857	\$754	\$1,485	\$3,748	\$8,844	\$13,497	\$21,417			\$1,978
<b>50-54</b>	5	232	1,366	537	329	360	287	15		3,131
	\$4,275	\$1,465	\$1,414	\$4,085	\$9,152	\$20,268	\$31,892	\$31,674		\$7,800
<b>55-59</b>	10	250	2,552	1,301	754	1,461	8,233	3,555	6	18,122
	\$29,665	\$1,972	\$1,714	\$4,953	\$10,196	\$25,029	\$39,992	\$51,661	\$56,756	\$31,404
<b>60-64</b>	125	422	2,431	2,001	1,642	2,507	9,509	5,857	235	24,729
	\$1,946	\$2,871	\$2,980	\$7,079	\$13,644	\$24,656	\$35,753	\$48,951	\$53,474	\$30,180
<b>65-69</b>	441	729	2,576	2,652	2,870	3,333	5,579	4,640	766	23,586
	\$869	\$2,516	\$3,686	\$7,481	\$12,358	\$20,443	\$30,124	\$38,520	\$49,699	\$22,048
<b>70-74</b>	543	960	2,728	2,691	2,960	3,205	3,982	2,643	1,810	21,522
	\$590	\$2,003	\$3,435	\$6,293	\$10,816	\$17,148	\$25,767	\$34,519	\$41,730	\$17,884
<b>75-79</b>	611	1,159	2,748	2,809	3,050	3,059	2,868	2,101	1,186	19,591
	\$512	\$1,736	\$3,321	\$6,068	\$10,619	\$16,241	\$22,651	\$29,972	\$39,768	\$14,581
<b>80-84</b>	473	1,029	2,307	2,418	2,198	2,029	1,549	1,480	592	14,075
	\$523	\$1,571	\$3,283	\$5,972	\$10,032	\$14,612	\$19,711	\$24,484	\$35,004	\$11,585
<b>85-89</b>	288	695	1,623	1,419	1,230	1,057	827	938	389	8,466
	\$602	\$1,703	\$3,478	\$6,051	\$9,417	\$13,298	\$18,229	\$22,385	\$27,652	\$10,401
<b>Over 89</b>	147	459	741	758	657	694	564	742	631	5,393
	\$690	\$2,248	\$4,203	\$7,228	\$10,666	\$13,791	\$18,059	\$21,439	\$24,905	\$12,630
<b>Total</b>	2,654	7,117	20,423	17,022	15,827	17,732	33,402	21,971	5,615	141,763
	\$803	\$1,761	\$2,932	\$6,272	\$11,046	\$18,728	\$32,031	\$39,913	\$39,335	\$20,146

**Exhibit III**  
**The Number and Average Annual Annuity**  
**As of June 30, 2005**

**Beneficiaries and Survivor Annuitants**

Age	Years of Service									Total
	0 - 4	5 - 9	10 - 14	15 - 19	20 - 24	25 - 29	30 - 34	35 - 39	40 +	
<b>Under 50</b>	1	18	53	43	49	33	28	18	16	259
	\$240	\$1,707	\$1,753	\$2,875	\$5,462	\$7,612	\$14,746	\$14,304	\$10,652	\$6,205
<b>50 - 54</b>	1	10	14	19	29	32	41	20	10	176
	\$217	\$1,056	\$2,681	\$4,067	\$6,276	\$11,270	\$12,451	\$12,552	\$9,197	\$8,646
<b>55 - 59</b>	2	8	33	28	42	53	113	90	21	390
	\$291	\$2,473	\$2,340	\$3,031	\$6,705	\$12,085	\$15,280	\$15,919	\$13,240	\$11,646
<b>60 - 64</b>	2	15	42	53	44	59	146	130	31	522
	\$381	\$1,402	\$2,464	\$4,778	\$6,275	\$10,845	\$17,185	\$19,940	\$14,123	\$13,091
<b>65 - 69</b>	10	21	94	84	81	74	141	157	54	716
	\$591	\$1,738	\$3,185	\$4,381	\$6,647	\$10,611	\$13,149	\$18,404	\$18,518	\$10,862
<b>70 - 74</b>	8	39	119	119	108	101	194	162	101	951
	\$577	\$1,675	\$2,730	\$4,432	\$6,683	\$9,001	\$12,665	\$15,045	\$18,876	\$9,836
<b>75 - 79</b>	23	53	168	167	160	186	205	239	121	1,322
	\$634	\$1,416	\$2,614	\$3,790	\$6,471	\$8,334	\$11,640	\$12,362	\$15,934	\$8,333
<b>80 - 84</b>	21	96	202	184	174	206	216	307	108	1,514
	\$584	\$1,233	\$2,443	\$3,537	\$5,863	\$7,471	\$9,350	\$10,769	\$14,126	\$7,058
<b>85 - 89</b>	10	98	172	126	127	108	152	225	156	1,174
	\$507	\$1,125	\$2,039	\$3,529	\$4,902	\$7,084	\$7,931	\$9,810	\$10,502	\$6,260
<b>Over 89</b>	1	42	79	58	62	61	86	182	196	767
	\$514	\$1,008	\$2,103	\$3,013	\$4,246	\$5,412	\$6,716	\$7,725	\$8,976	\$6,154
<b>Total</b>	79	400	976	881	876	913	1,322	1,530	814	7,791
	\$567	\$1,325	\$2,443	\$3,788	\$5,946	\$8,511	\$11,845	\$12,898	\$13,189	\$8,395

**Exhibit IV**  
**The Number and Average Annual Annuity**  
**As of June 30, 2005**

**Retired on Account of Disability**

Age	Years of Service									Total
	0 - 4	5 - 9	10 - 14	15 - 19	20 - 24	25 - 29	30 - 34	35 - 39	40 +	
<b>Under 50</b>	2	226	185	105	57	15				590
	\$10,868	\$9,872	\$11,938	\$16,424	\$20,111	\$25,249				\$13,069
<b>50 - 54</b>	1	166	198	146	165	200	42			918
	\$20,265	\$8,401	\$11,147	\$15,720	\$22,505	\$36,091	\$46,178			\$20,466
<b>55 - 59</b>	4	218	296	250	260	377	203	3		1,611
	\$14,367	\$8,009	\$10,404	\$13,541	\$21,167	\$31,798	\$44,653	\$49,560		\$21,709
<b>60 - 64</b>		219	285	249	280	232	45	2		1,312
		\$5,925	\$8,151	\$11,512	\$18,341	\$27,200	\$38,253	\$46,868		\$15,052
<b>65 - 69</b>		161	238	199	170	115	16	2		901
		\$5,157	\$7,377	\$9,730	\$14,592	\$23,933	\$27,256	\$42,997		\$11,407
<b>70 - 74</b>		133	173	147	127	67	13	1		661
		\$4,050	\$6,505	\$8,640	\$12,810	\$19,445	\$26,193	\$43,179		\$9,451
<b>75 - 79</b>		96	146	88	90	56	6	1	1	484
		\$3,407	\$5,719	\$8,613	\$13,016	\$17,880	\$23,576	\$24,751	\$54,601	\$8,912
<b>80 - 84</b>	1	72	63	47	54	34	14	1		286
	\$25,382	\$3,615	\$5,858	\$7,157	\$10,542	\$15,570	\$21,209	\$29,135		\$8,447
<b>85 - 89</b>		26	39	27	21	11	16			140
		\$3,107	\$5,827	\$8,135	\$10,849	\$15,996	\$21,045			\$9,059
<b>Over 89</b>		4	18	23	8	6	2			61
		\$3,045	\$5,999	\$8,176	\$9,306	\$14,460	\$16,133			\$8,224
<b>Total</b>	8	1,321	1,641	1,281	1,232	1,113	357	10	1	6,964
	\$15,606	\$6,600	\$8,677	\$11,694	\$17,572	\$28,521	\$40,082	\$42,547	\$54,601	\$15,256



**Exhibit V**  
**The Number and Average Annual Annuity**  
**As of June 30, 2005**

**Those in Receipt of a Refund Annuity**

Age	Years of Service									Total
	0 - 4	5 - 9	10 - 14	15 - 19	20 - 24	25 - 29	30 - 34	35 - 39	40 +	
Under 50										
50 - 54										
55 - 59										
60 - 64										
65 - 69										
70 - 74										
75 - 79										
80 - 84										
85 - 89										
Over 89	1 \$ 66									1 \$ 66
<b>Total</b>	1 \$ 66									1 \$ 66

**Exhibit VI**  
**Annuitant and Beneficiary Membership Data**  
**As of June 30, 2005**

**Number and Average Annual Benefit**  
**Excludes Partial Lump Sum Payments**

Age Last Birthday	Number	Annual Benefit (Dollars in Thousands)	Average Annual Benefit (Dollars)
<b>Annuitants</b> (Normal, Early and Withdrawal)			
Under 60	24,401	\$ 599,759	\$ 24,579
60 - 64	24,729	746,327	30,180
65 - 69	23,586	520,023	22,048
70 - 74	21,522	384,894	17,884
75 - 79	19,591	285,663	14,581
Over 79	27,934	319,235	11,428
Total	141,763	\$ 2,855,901	\$ 20,146
<b>Survivors and Beneficiaries</b>			
Under 60	825	7,671	9,298
60 - 64	522	6,833	13,090
65 - 69	716	7,777	10,862
70 - 74	951	9,354	9,836
75 - 79	1,322	11,016	8,333
Over 79	3,456	22,755	6,584
Total	7,792	\$ 65,406	\$ 8,394
<b>Disabled Annuitants</b>			
Under 60	3,119	\$ 61,471	\$ 19,709
60 - 64	1,312	19,748	15,052
65 - 69	901	10,277	11,406
70 - 74	661	6,247	9,451
75 - 79	484	4,314	8,913
Over 79	487	4,186	8,595
Total	6,964	\$ 106,243	\$ 15,256
<b>Grand Total</b> <b>Average Annual Benefit</b>		156,519	\$ 3,027,550
		\$ 3,027,550	\$ 19,343

**Exhibit VII****10 Year History of Membership Data****Active Members**

<b>Valuation as of June 30</b>	<b>Number of Active Members</b>	<b>Percentage Change in Membership</b>	<b>Total Annual Payroll (Dollars in Thousands)</b>	<b>Percentage Change in Payroll</b>
2005	255,465	3.05%	\$ 10,527,668	4.95%
2004	247,901	0.49%	10,030,705	3.91%
2003	246,700	1.68%	9,652,881	2.92%
2002	242,616	(0.29%)	9,378,944	(0.38%)
2001	243,311	3.89%	9,414,884	5.32%
2000	234,210	4.79%	8,939,598	8.39%
1999	223,495	1.27%	8,247,602	1.93%
1998	220,703	2.62%	8,091,481	4.47%
1997	215,077	0.55%	7,745,001	1.69%
1996	213,906	1.48%	7,616,585	3.23%

**Annuitant and Survivor Annuitant Members**

<b>Year Ended June 30</b>	<b>Number on roll</b>	<b>Additions</b>	<b>Deletions</b>	<b>Percentage Change in Membership</b>	<b>Annual Annuities (Dollars in Millions)</b>	<b>Percentage Change in Annuities</b>
2005	156,519	10,050	5,083	3.28%	\$ 3,027.6	8.20%
2004	151,552	10,526	4,667	4.02%	2,798.2	9.94%
2003	145,693	9,079	4,800	3.03%	2,545.1	13.20%
2002	141,414	13,003	4,305	6.55%	2,248.3	20.10%
2001	132,716	3,140	4,482	(1.00)%	1,872.0	0.00%
2000	134,058	5,923	4,734	0.89%	1,880.6	2.73%
1999	132,869	10,609	4,554	4.77%	1,830.6	10.77%
1998	126,814	7,132	4,442	2.17%	1,652.6	14.21%
1997	124,124	9,787	4,389	4.55%	1,447.0	11.74%
1996	118,726	7,047	4,281	2.39%	1,295.0	6.05%

Public School Employees' Retirement System

# Statistical Section



## Statistical Section Narrative

To assist readers in the assessment of the System's economic condition, The Statistical Section of this Comprehensive Annual Financial Report presents information to add historical perspective, context, and detail to the financial statements, notes to financial statements, and required supplementary information presented in the preceding sections. To provide historical perspective and a sense of trend, the exhibits in this Section are presented in multiple-year formats. The information is categorized into four topical groups: *Financial Trends, Revenue Capacity, Demographic and Economic Information, and Operating Information.*

### Financial Trends

The ***Schedule of Trend Data*** provides key financial, actuarial, and demographic information for a ten-year period ending June 30, 2006.

The ***Schedule of Total Changes in Plan Net Assets*** shows the historical combined effects of the additions and deductions of plan net assets over the ten-year period ending June 30, 2006.

The schedule of ***Additions to Plan Net Assets*** provides tabular and visual details of the additions to the System's plan net assets over the ten-year period ending June 30, 2006.

The schedule of ***Deductions from Plan Net Assets*** provides tabular and visual details of the deductions from the System's plan net assets over the ten-year period ending June 30, 2006.

### Revenue Capacity

The ***Schedule of Investment Income*** provides a ten-year perspective on the System's largest source of revenue - Net Investment Income.

### Demographic and Economic Information

The ***Schedule of Summary Membership Data*** provides general populations and statistics relating to the System's active membership over the ten-year period ending June 30, 2006.

The ***Schedule of Summary Annuity Data*** provides general populations and statistics relating to the System's annuitants over the ten-year period ending June 30, 2006.

The schedule of ***Components of Total Contribution Rate*** provides a long-term historical perspective of the actuarially required contribution rates to the System's members and employers.

The ***Schedule of Retired Members by Type of Benefit*** provides summary statistics relating to the PSERS annuitants' receipt of annuities over the ten-year period ending June 30, 2006.

### Operating Information

The list of ***Ten Largest Employers*** shows the System's ten largest employers in terms of reported members. Due to the stable comparable populations of school employees in PSERS' employers over the years, a single presentation provides perspective for a ten-year period.

The ***Schedule of Employers*** provides the full list of PSERS' employers.

Schedule of Trend Data\*

For years ending June 30,	2006	2005	2004	2003	2002	2001	2000	1999	1998	1997
<b>Contribution Rates: %</b>										
<b>Total Employer</b>	4.69	4.23	3.77	1.15	1.09	1.94	4.61	6.04	8.76	10.60
<b>Health Care Premium Insurance</b>	.69	.23	.79	.97	1.09	.30	.25	.15	.15	.60
<b>Average Member</b>	7.16	7.12	7.08	7.10	6.43	5.77	5.72	5.69	5.65	5.62
<b>Contributions:</b>										
<b>Employer \$</b>	530,943	457,808	406,722	116,456	109,450	185,716	412,783	526,960	731,131	844,599
<b>Member \$</b>	982,846	955,509	944,422	897,307	805,567	721,725	680,040	646,507	578,322	559,070
<b>Average Annual Member Compensation \$</b>	43,361	41,210	40,463	39,128	38,658	38,695	38,169	36,903	36,662	36,010
<b>Market Value of Assets \$</b>	57,328,000	52,033,534	48,484,506	42,446,826	43,576,553	48,143,327	53,412,950	48,971,751	44,851,838	39,386,330
<b>Actuarial Value of Assets \$</b>	52,558,000	51,219,300	52,094,500	52,900,500	54,296,400	54,830,300	49,293,047	44,606,526	39,968,957	34,872,643
<b>Accrued Actuarial Liability \$</b>	64,720,000	61,129,444	56,978,143	54,313,328	51,693,207	47,870,922	39,771,604	37,499,115	36,136,163	33,209,493
<b>Funded Ratio %</b>	81.2	83.7	91.2	97.2	104.8	114.4	123.8	119.0	110.6	105.0
<b>Total Benefits &amp; Refunds \$</b>	4,115,865	3,877,842	3,497,365	3,102,684	2,913,163	2,297,332	2,382,277	2,456,383	2,015,309	1,859,119
<b>Average Pension \$</b>	20,236	19,343	18,464	17,469	15,899	14,105	14,029	13,777	13,032	11,658
<b>Annuityants &amp; Beneficiaries</b>	162,813	156,519	151,552	145,693	141,414	132,716	134,058	132,869	126,814	124,124
<b>Active Members</b>	263,350	255,465	247,901	246,700	242,616	243,311	234,210	223,495	220,703	215,077

\* All dollar amounts are in thousands, except Average Annual Member Compensation and Average Pension.

## Schedule of Total Changes in Plan Net Assets 10 Year Trend (Dollar Amounts in Thousands)

Year Ending June 30,	Additions to Plan Net Assets				Deductions from Plan Net Assets						Net Increase / (Decrease)
	Member Contributions	Employer Contributions	Net Investment Income	Total Additions	Benefits	Lump-Sum and Instalment	Refunds of Contributions	Administrative	Net Transfers	Total Deductions	
2006	\$ 982,846	\$ 544,884	\$ 7,942,639	\$ 9,470,369	\$ 3,260,712	\$ 830,361	\$ 16,330	\$ 48,629	\$ 8,462	\$ 4,164,494	\$ 5,305,875
2005	955,509	457,808	6,081,497	7,494,814	3,158,661	692,089	16,233	42,645	10,859	3,920,487	3,574,327
2004	944,422	406,722	8,244,604	9,595,748	2,906,344	559,939	14,767	49,202	16,315	3,546,567	6,049,181
2003	897,307	116,456	1,022,467	2,036,230	2,591,130	485,495	13,943	42,278	12,116	3,144,962	(1,108,732)
2002	805,567	109,450	(2,523,025)	(1,608,008)	2,293,687	595,184	14,858	35,373	9,434	2,948,536	(4,556,544)
2001	721,725	185,716	(3,843,713)	(2,936,272)	2,087,868	176,228	22,369	34,854	10,867	2,332,186	(5,268,458)
2000	680,040	412,783	5,765,133	6,857,956	2,048,792	306,329	22,446	29,333	4,710	2,411,610	4,446,346
1999	646,507	526,960	5,428,659	6,602,126	1,834,494	591,532	20,110	27,786	10,247	2,484,169	4,117,957
1998	578,322	731,131	6,195,893	7,505,346	1,611,137	376,575	20,503	29,947	7,094	2,045,256	5,460,090
1997	559,070	844,599	6,147,462	7,551,131	1,445,515	384,234	17,296	26,940	12,074	1,886,059	5,665,072

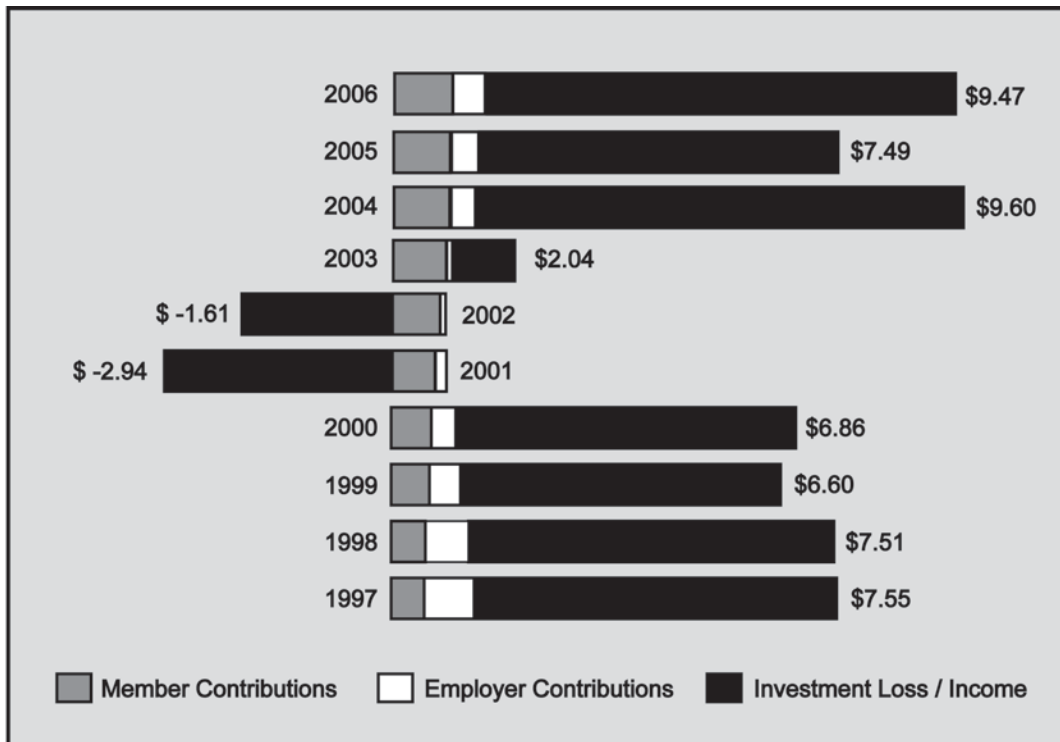


## Additions to Plan Net Assets 10 Year Trend

(Dollar Amounts in Thousands)

Fiscal Year	Members Contributions	Employers, Commonwealth, & CMS Contributions		Net Investment Income / (Loss)	Total Additions
		Dollar Amount	Percentage of Covered Payroll		
2006	\$ 982,846	\$ 544,884	4.69 %	\$ 7,942,639	\$ 9,470,369
2005	955,509	457,808	4.23	6,081,497	7,494,814
2004	944,422	406,722	3.77	8,244,604	9,595,748
2003	897,307	116,456	1.15	1,022,467	2,036,230
2002	805,567	109,450	1.09	(2,523,025)	(1,608,008)
2001	721,725	185,716	1.94	(3,843,713)	(2,936,272)
2000	680,040	412,783	4.61	5,765,133	6,857,956
1999	646,507	526,960	6.04	5,428,659	6,602,126
1998	578,322	731,131	8.76	6,195,893	7,505,346
1997	559,070	844,599	10.60	6,147,462	7,551,131

(Dollar Amounts in Billions)



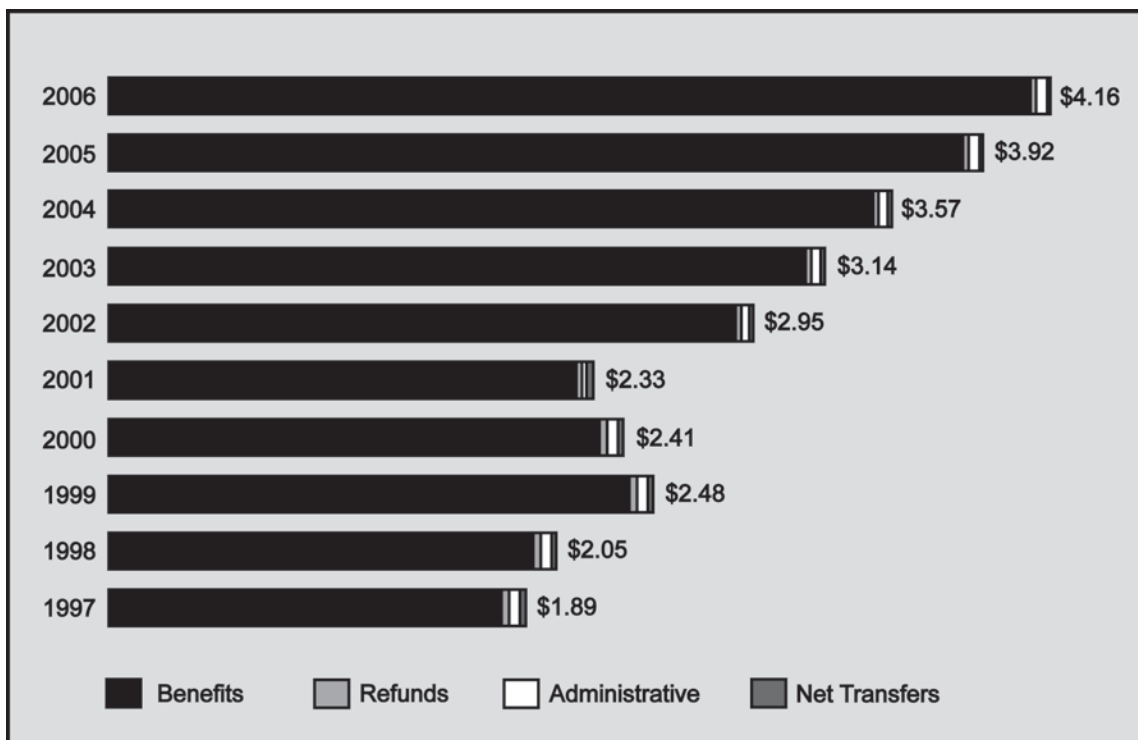
## Deductions from Plan Net Assets 10 Year Trend

(Dollar Amounts in Thousands)

Fiscal Year	Benefits	Lump-Sum and Installment	Refunds	Administrative	Net Transfers*	Total Deductions
2006	\$ 3,260,712	\$ 830,361	\$ 16,330	\$ 48,629	\$ 8,462	\$ 4,164,494
2005	3,158,661	692,089	16,233	42,645	10,859	3,920,487
2004	2,906,344	559,939	14,767	49,202	16,315	3,546,567
2003	2,591,130	485,495	13,943	42,278	12,116	3,144,962
2002	2,293,687	595,184	14,858	35,373	9,434	2,948,536
2001	2,087,868	176,228	22,369	34,854	10,867	2,332,186
2000	2,048,792	306,329	22,446	29,333	4,710	2,411,610
1999	1,834,494	591,532	20,110	27,786	10,247	2,484,169
1998	1,611,137	376,575	20,503	29,947	7,094	2,045,256
1997	1,445,515	384,234	17,296	26,940	12,074	1,886,059

\* Net transfers to the Commonwealth of Pennsylvania, State Employees' Retirement System.

(Dollar Amounts in Billions)



## Schedule of Investment Income 10 Year Trend (Dollar Amounts in Thousands)

For years ending June 30,	2006	2005	2004	2003	2002	2001	2000	1999	1998	1997
<b>Investment income:</b>										
From investing activities:										
Net appreciation (depreciation) in fair value of investments	\$ 5,968,866	\$ 4,462,384	\$ 6,871,417	\$ (172,506)	\$ (3,826,705)	\$ (5,137,619)	\$ 4,129,236	\$ 4,068,463	\$ 4,893,203	4,862,236
Investment income	2,162,096	1,795,687	1,549,791	1,358,997	1,450,203	1,413,964	1,739,049	1,431,399	1,371,511	1,341,086
Total investment activity income (loss)	8,130,962	6,258,071	8,421,208	1,186,491	(2,376,502)	(3,723,655)	5,868,285	5,499,862	6,264,714	6,203,322
Investment expenses	(211,279)	(192,677)	(191,300)	(179,056)	(162,777)	(143,685)	(124,576)	(88,929)	(88,816)	(73,998)
Net income (loss) from investing activities	7,919,683	6,065,394	8,229,908	1,007,435	(2,539,279)	(3,867,340)	5,743,709	5,410,933	6,175,898	6,129,324
From securities lending activities:										
Securities lending income	270,447	125,882	46,075	43,870	57,391	147,852	161,416	163,445	319,903	278,279
Securities lending expense	(247,491)	(109,779)	(31,379)	(28,838)	(41,137)	(124,225)	(139,992)	(145,719)	(299,908)	(260,141)
Net income from securities lending activities	22,956	16,103	14,696	15,032	16,254	23,627	21,424	17,726	19,995	18,138
Total net investment income (loss)	7,942,639	6,081,497	8,244,604	1,022,467	(2,523,025)	(3,843,713)	5,765,133	5,428,659	6,195,893	6,147,462

## Schedule of Summary Membership Data 10 Year Trend

(Dollar Amounts in Thousands)

For year ended June 30,	Male			Female			Total Number of Active Members
	Average Age	Average Service	Average Annual Salaries	Average Age	Average Service	Average Annual Salaries	
2006	44.6	12.0	49,153	44.7	10.7	41,155	263,350
2005	44.9	12.6	47,416	45.0	11.0	38,832	255,465
2004	45.1	13.0	47,103	45.1	11.1	37,901	247,901
2003	45.1	13.5	45,947	45.0	11.2	36,465	246,700
2002	45.2	14.0	45,182	44.9	11.3	36,073	242,616
2001	45.5	14.6	45,686	44.9	11.6	35,852	243,311
2000	45.2	14.4	45,049	44.6	11.3	35,331	234,210
1999	45.2	14.6	43,498	44.7	11.5	34,132	223,495
1998	45.4	15.2	43,239	44.7	11.7	33,799	220,703
1997	45.2	15.4	42,512	44.7	11.8	33,125	215,077

## Schedule of Summary Annuity Data 10 Year Trend

For year ended June 30,	Number of Annuitants & Beneficiaries	Total Annual Annuities	Average Annual Annuity
2006	161,813	\$ 3,274,000	\$ 20,236
2005	156,519	3,027,550	19,343
2004	151,552	2,798,211	18,464
2003	145,693	2,545,135	17,469
2002	141,414	2,248,291	15,899
2001	132,716	1,871,995	14,105
2000	134,058	1,880,644	14,029
1999	132,869	1,830,582	13,777
1998	126,814	1,652,645	13,032
1997	124,124	1,447,037	11,658

Total Annual Annuities dollars expressed in Millions.

## Components of Total Contribution Rate

(In Percentages)

Employer Year	Employer Payroll	Member Contribution (Average)	Employer Contribution					Grand Total Contribution Rate
			Normal Requirement (A)	(Funded) / Unfunded Accrued Liability (B)	Preliminary Employer Pension Rate	Health Insurance Premium Assistance Contribution (C)	Total Employer Rate	
2006-2007	11,821,951	7.21	6.62	(0.95)	5.67	.74	6.46	13.67
2005-2006	11,505,093	7.16	7.61	(4.28)	4.00	.69	4.69	11.85
2004-2005	11,062,589	7.12	7.48	(7.10)	4.00	.23	4.23	11.35
2003-2004	10,030,705	7.08	7.25	(4.27)	2.98	.79	3.77	10.85
2002-2003	9,652,881	7.10	7.20	(10.03)	1.00	.97	1.15	8.25
2001-2002	9,378,944	6.43	5.63	(6.05)	(0.42)	1.09	1.09	6.89
2000-2001	9,414,884	5.77	6.29	(4.65)	1.64	.30	1.94	7.71
1999-2000	8,939,598	5.72	6.40	(2.04)	4.36	.25	4.61	10.33
1998-1999	8,247,602	5.69	6.33	(0.44)	5.89	.15	6.04	11.73
1997-1998	8,091,481	5.65	6.44	2.17	8.61	.15	8.76	14.41
1996-1997	7,745,001	5.62	6.44	3.56	10.00	.60	10.60	16.22
1995-1996	7,616,585	5.59	6.43	4.67	11.10	.62	11.72	17.31
1994-1995	7,378,342	5.55	6.43	4.18	10.61	.45	11.06	16.61
1993-1994	6,885,337	5.51	7.34	5.58	12.92	.25	13.17	18.68
1992-1993	6,348,565	5.48	7.90	5.84	13.74	.50	14.24	19.72
1991-1992	6,098,222	5.46	8.00	6.40	14.40	.50	14.90	20.36
1990-1991	5,744,798	5.69	8.28	10.90	19.18		19.18	24.87
1989-1990	5,363,535	5.53	8.44	11.24	19.68		19.68	25.21
1988-1989	5,055,793	5.37	8.63	10.64	19.27		19.27	24.64
1987-1988	4,586,367	5.34	8.72	10.82	19.54		19.54	24.88
1986-1987	4,415,102	5.29	9.13	10.77	19.90		19.90	25.19
1985-1986	4,066,471	5.27	9.16	10.88	20.04		20.04	25.31

The total contribution rate is the total of the employer and member rates actuarially required for the funding of PSERS' pension and postemployment health insurance premium assistance benefits.

The total employer rate is comprised of a normal requirement, an accrued liability requirement and a postemployment healthcare insurance premium assistance requirement.

- (A) The normal requirement portion is the percentage of compensation necessary to fund any prospective pension benefits payable to the member.
- (B) The total funded / unfunded accrued liability portion is the percentage of compensation necessary to fund past pension benefit enhancements, cost-of-living adjustments and other actuarial gains and losses.
- (C) The postemployment healthcare insurance premium assistance portion is the percentage of compensation necessary to fund the postemployment health insurance premium assistance program established under the provisions of Act 23 - 1991.

## Schedule of Retired Members by Type of Benefit

Year	Retirement Type**	Option M*		Option 1*		Option 2, 3*	
		Number of Retirees	Average Mo. Benefit	Number of Retirees	Average Mo. Benefit	Number of Retirees	Average Mo. Benefit
2006	S	49,831	\$1,813	11,081	\$1,514	19,085	\$2,067
	W	43,328	1,656	10,948	1,269	11,477	1,872
	D	5,544	1,244	8	629	1,569	1,571
	R	1	5	0	0	0	0
	B	473	951	1	1,675	6,785	728
		<b>99,177</b>		<b>22,038</b>		<b>38,916</b>	
2005	S	49,508	\$1,737	10,385	\$1,420	18,206	\$1,965
	W	42,096	1,611	9,754	1,187	10,492	1,778
	D	5,455	1,198	9	656	1,450	1,539
	R	1	5	0	0	0	0
	B	405	908	1	1,072	6,646	690
		<b>97,465</b>		<b>20,149</b>		<b>36,794</b>	
2004	S	49,424	\$1,648	9,706	\$1,312	17,321	\$1,842
	W	40,944	1,556	8,582	1,073	9,551	1,669
	D	5,327	1,154	9	656	1,304	1,508
	R	1	5	0	0	0	0
	B	324	899	2	1,072	6,502	648
		<b>96,020</b>		<b>18,299</b>		<b>34,678</b>	
2003	S	49,231	\$1,560	8,999	\$1,186	16,408	\$1,725
	W	39,707	1,494	7,541	964	8,696	1,569
	D	5,170	1,105	9	656	1,156	1,459
	R	1	5	0	0	0	0
	B	258	881	11	542	6,348	614
		<b>94,367</b>		<b>16,560</b>		<b>32,608</b>	
2002	S	49,368	\$1,431	8,422	\$1,064	15,695	\$1,572
	W	38,679	1,389	6,696	820	7,948	1,415
	D	5,049	1,017	11	700	1,015	1,305
	R	1	5	0	0	0	0
	B	232	814	11	557	6,206	586
		<b>93,329</b>		<b>15,140</b>		<b>30,864</b>	
2001	S	47,982	\$1,241	7,681	\$857	14,453	\$1,334
	W	36,628	1,287	5,656	653	7,051	1,275
	D	4,864	909	13	567	895	1,167
	R	1	4	0	0	0	0
	B	175	790	7	426	6,029	562
		<b>89,650</b>		<b>13,357</b>		<b>28,428</b>	
2000	S	49,367	\$1,225	7,923	\$860	14,768	\$1,326
	W	36,620	1,288	5,623	660	7,063	1,281
	D	4,740	886	14	545	847	1,141
	R	1	4	0	0	0	0
	B	144	762	3	435	5,879	544
		<b>90,872</b>		<b>13,563</b>		<b>28,557</b>	
1999	S	49,255	\$1,183	8,046	\$ 855	14,641	\$1,309
	W	36,002	1,281	5,514	670	6,958	1,278
	D	4,587	854	14	545	782	1,105
	R	1	4	0	0	0	0
	B	120	754	1	1,160	5,655	519
		<b>89,965</b>		<b>13,575</b>		<b>28,036</b>	
1998	S	49,081	\$1,151	8,134	\$ 858	14,558	\$1,293
	W	31,568	1,131	5,253	636	6,300	1,209
	D	4,439	828	15	541	724	1,074
	R	1	4	0	0	0	0
	B	84	792	1	1,160	5,421	493
		<b>85,173</b>		<b>13,403</b>		<b>27,003</b>	
1997	S	48,869	\$1,011	8,185	\$ 773	14,406	\$1,162
	W	29,931	1,025	5,115	585	6,050	1,106
	D	4,334	733	16	439	694	974
	R	1	4	0	0	0	0
	B	54	766	1	1,160	5,275	475
		<b>83,189</b>		<b>13,317</b>		<b>26,425</b>	

**\* OPTIONS:**

- M - Maximum Option - Highest monthly allowance with guarantee of accumulated deductions only
- 1 - Option 1 - Maximum allowance reduced for Death Benefit protection
- 2, 3 - Option 2 & 3 - Joint and survivor annuities
- SO - Special Option - Plan approved by actuary
- BO - Beneficiary options - Life, 5 and 10 year certain annuity plans

## Schedule of Retired Members by Type of Benefit (Continued)

Year	Retirement Type**	Option SO*		Option BO*		Total Retirees	% Increase of Retirees
		Number of Retirees	Average Mo. Benefit	Number of Retirees	Average Mo. Benefit		
2006	S	849	\$3,324	0	\$ 0	80,846	4.8%
	W	418	2,761	0	0	66,171	11.4%
	D	12	1,785	0	0	7,133	7.3%
	R	0	0	0	0	1	0.0%
	B	162	865	534	688	7,955	6.3%
		<b>1,441</b>		<b>534</b>		<b>162,106</b>	<b>7.6%</b>
2005	S	740	\$3,306	0	\$ 0	78,839	2.2%
	W	355	2,710	0	0	62,697	5.6%
	D	8	1,513	0	0	6,922	4.1%
	R	0	0	0	0	1	0.0%
	B	157	804	526	657	7,735	3.3%
		<b>1,260</b>		<b>526</b>		<b>156,194</b>	<b>3.7%</b>
2004	S	675	\$3,135	0	\$ 0	77,126	2.5%
	W	313	2,622	0	0	59,390	5.7%
	D	7	1,482	0	0	6,647	4.9%
	R	0	0	0	0	1	0.0%
	B	144	694	514	622	7,486	3.2%
		<b>1,139</b>		<b>514</b>		<b>150,650</b>	<b>3.9%</b>
2003	S	613	\$2,984	0	\$ 0	75,261	1.6%
	W	266	2,494	1	336	56,210	5.0%
	D	3	2,211	0	0	6,338	4.3%
	R	0	0	0	0	1	0.0%
	B	146	637	489	517	7,252	2.6%
		<b>1,028</b>		<b>490</b>		<b>145,062</b>	<b>6.0%</b>
2002	S	562	\$2,727	0	\$ 0	74,047	4.9%
	W	235	2,312	0	0	53,558	8.1%
	D	3	2,099	0	0	6,078	5.3%
	R	0	0	0	0	1	0.0%
	B	148	559	475	553	7,072	3.5%
		<b>948</b>		<b>475</b>		<b>140,756</b>	<b>6.0%</b>
2001	S	473	\$2,412	0	\$ 0	70,589	-2.7%
	W	202	2,186	1	336	49,538	0.1%
	D	2	2,151	0	0	5,774	3.1%
	R	0	0	0	0	1	0.0%
	B	149	513	476	517	6,836	2.6%
		<b>826</b>		<b>477</b>		<b>132,738</b>	<b>-1.2%</b>
2000	S	480	\$2,389	0	\$ 0	72,538	0.2%
	W	207	2,180	1	336	49,514	1.7%
	D	2	2,151	0	0	5,603	4.1%
	R	0	0	0	0	1	0.0%
	B	146	481	488	500	6,660	3.8%
		<b>835</b>		<b>489</b>		<b>134,316</b>	<b>1.1%</b>
1999	S	444	\$2,379	0	\$ 0	72,386	0.3%
	W	207	2,167	0	0	48,681	12.5%
	D	1	1,109	0	0	5,384	4.0%
	R	0	0	0	0	1	0.0%
	B	142	427	496	475	6,414	4.5%
		<b>794</b>		<b>496</b>		<b>132,866</b>	<b>4.8%</b>
1998	S	433	\$2,365	0	\$ 0	72,206	0.5%
	W	163	2,063	0	0	43,284	4.9%
	D	0	0	0	0	5,178	2.7%
	R	0	0	0	0	1	0.0%
	B	146	392	487	426	6,139	2.7%
		<b>742</b>		<b>487</b>		<b>126,808</b>	<b>2.2%</b>
1997	S	392	\$2,125	0	\$ 0	71,852	0.7%
	W	149	1,979	0	0	41,245	12.1%
	D	0	0	0	0	5,044	4.1%
	R	0	0	0	0	1	0.0%
	B	153	329	495	419	5,978	4.7%
		<b>694</b>		<b>495</b>		<b>124,120</b>	<b>4.6%</b>

**\*\* RETIREMENT TYPE:**

- S - Superannuation or Normal Retirement
- W - Withdrawal or Early Retirement
- D - Disability Benefit
- R - Refund Annuity
- B - Beneficiaries Receiving Annuities



## Ten Largest Employers

(Based on count of reported members)

		Percentage of Total Active Members
1.	City of Philadelphia School District	10.5 %
2.	Pittsburgh School District	2.2
3.	Central Bucks School District	.9
4.	Reading School District	.8
5.	Allentown City School District	.8
6.	North Penn School District	.7
7.	Bethlehem Area School District	.7
8.	Pocono Mountain School District	.6
9.	Erie City School District	.6
10.	Pennsbury School District	.6

The top ten employers in PSERS through the years has not varied significantly. Philadelphia School District and Pittsburgh School District each year represent the largest portion of reported members from the employer population. After these two employers, the remainder of the more than 700 employers of the System each comprise less than 1% of the total active membership in PSERS.

## Schedule of Employers School Districts

### A

Abington  
Abington Heights  
Albert Gallatin  
Aliquippa  
Allegheny-Clarion Valley  
Allegheny Valley  
Allentown City  
Altoona Area  
Ambridge Area  
Annville-Cleona  
Antietam  
Apollo-Ridge  
Armstrong  
Athens Area  
Austin Area  
Avella Area  
Avon Grove  
Avonworth

### B

Bald Eagle Area  
Baldwin-Whitehall  
Bangor Area  
Beaver Area  
Bedford Area  
Belle Vernon Area  
Bellefonte Area  
Bellwood-Antis  
Bensalem Township  
Benton Area  
Bentworth  
Berlin Brothers Valley  
Bermudian Springs  
Berwick Area  
Bethel Park  
Bethlehem Area  
Bethlehem-Center  
Big Beaver Falls Area  
Big Spring  
Blackhawk  
Blacklick Valley  
Blairsville-Saltsburg  
Bloomsburg Area  
Blue Mountain  
Blue Ridge  
Boyertown Area  
Bradford Area  
Brandywine Heights Area  
Brentwood Boro  
Bristol Boro  
Bristol Township  
Brockway Area  
Brookville Area  
Brownsville Area  
Burgettstown Area

Burrell  
Butler Area

### C

California Area  
Cambria Heights  
Cameron County  
Camp Hill  
Cannon-McMillan  
Canton Area  
Carbondale Area  
Carlisle Area  
Carlynton  
Carmichaels Area  
Catasauqua  
Centennial  
Center Area  
Central Bucks  
Central Cambria  
Central Columbia  
Central Dauphin  
Central Fulton  
Central Greene  
Central York  
Chambersburg Area  
Charleroi Area  
Chartiers-Houston  
Chartiers Valley  
Cheltenham Township  
Chester-Upland  
Chestnut Ridge  
Chichester  
Clairton  
Clarion Area  
Clarion-Limestone Area  
Claysburg-Kimmel  
Clearfield Area  
Coatesville Area  
Cocalico  
Colonial  
Columbia Boro  
Commodore Perry  
Conemaugh Township Area  
Conemaugh Valley  
Conestoga Valley  
Conewago Valley  
Conneaut  
Connellsville Area  
Conrad Weiser Area  
Cornell  
Cornwall-Lebanon  
Corry Area  
Coudersport Area  
Council Rock  
Cranberry Area  
Crawford Central  
Crestwood  
Cumberland Valley

Curwensville Area

Dallas  
Dallastown Area  
Daniel Boone Area  
Danville Area  
Deer Lakes  
Delaware Valley  
Derry Area  
Derry Township  
Donegal  
Dover Area  
Downingtown Area  
DuBois Area  
Dunmore  
Duquesne City

### E

East Allegheny  
East Lycoming  
East Penn  
East Pennsboro Area  
East Stroudsburg  
Eastern Lancaster County  
Eastern Lebanon County  
Eastern York  
Easton Area  
Elizabeth Forward  
Elizabethtown Area  
Elk Lake  
Ellwood City Area  
Ephrata Area  
Erie City  
Everett Area  
Exeter Township

### F

Fairfield Area  
Fairview  
Fannett-Metal  
Farrell Area  
Ferndale Area  
Fleetwood Area  
Forbes Road  
Forest Area  
Forest City Regional  
Forest Hills  
Fort Cherry  
Fort Le Boeuf  
Fox Chapel Area  
Franklin Area  
Franklin Regional  
Frazier  
Freedom Area  
Freeport Area

Schedule of Employers (Continued)

G

Galeton Area  
 Garnet Valley  
 Gateway  
 General McLane  
 Gettysburg Area  
 Girard  
 Glendale  
 Governor Mifflin  
 Great Valley  
 Greater Johnstown  
 Greater Latrobe  
 Greater Nanticoke Area  
 Greencastle-Antrim  
 Greensburg Salem  
 Greenville Area  
 Greenwood  
 Grove City Area

H

Halifax Area  
 Hamburg Area  
 Hampton Township  
 Hanover Area  
 Hanover Public  
 Harbor Creek  
 Harmony  
 Harrisburg City  
 Hatboro-Horsham  
 Haverford Township  
 Hazleton Area  
 Hempfield  
 Hempfield Area  
 Hermitage  
 Highlands  
 Hollidaysburg Area  
 Homer Center  
 Hopewell Area  
 Huntingdon Area

I

Indiana Area  
 Interboro  
 Iroquois

J

Jamestown Area  
 Jeannette City  
 Jefferson-Morgan  
 Jenkintown  
 Jersey Shore Area  
 Jim Thorpe Area  
 Johnsonburg Area  
 Juniata County  
 Juniata Valley

K

Kane Area  
 Karns City Area  
 Kennett Consolidated  
 Keystone  
 Keystone Central  
 Keystone Oaks  
 Kiski Area  
 Kutztown Area

L

Lackawanna Trail  
 Lake Lehman  
 Lakeland  
 Lakeview  
 Lampeter-Strasburg  
 Lancaster City  
 Laurel  
 Laurel Highlands  
 Lebanon  
 Leechburg Area  
 Lehigh Area  
 Lewisburg Area  
 Ligonier Valley  
 Line Mountain  
 Littlestown  
 Lower Dauphin  
 Lower Merion  
 Lower Moreland  
 Loyalsock Township

M

Mahanoy Area  
 Manheim Central  
 Manheim Township  
 Marion Center Area  
 Marple Newtown  
 Mars Area  
 McGuffey  
 McKeesport Area  
 Mechanicsburg Area  
 Mercer Area  
 Methacton  
 Meyersdale Area  
 Mid Valley  
 Middle-West  
 Middletown Area  
 Midland Boro  
 Mifflin County  
 Mifflinburg Area  
 Millcreek Township  
 Millersburg Area  
 Millville Area  
 Milton Area  
 Minersville Area  
 Mohawk Area  
 Monaca

Monessen  
 Moniteau  
 Montgomery Area  
 Montour  
 Montoursville Area  
 Montrose Area  
 Moon Area  
 Morrisville Boro  
 Moshannon Valley  
 Mount Carmel Area  
 Mount Lebanon  
 Mount Pleasant Area  
 Mount Union Area  
 Mountain View  
 Muhlenberg  
 Muncy

N

Nazareth Area  
 Neshaminy  
 Neshannock Township  
 New Brighton Area  
 New Castle Area  
 New Hope-Solebury  
 New Kensington-Arnold  
 Newport  
 Norristown Area  
 North Allegheny  
 North Clarion County  
 North East  
 North Hills  
 North Penn  
 North Pocono  
 North Schuylkill  
 North Star  
 Northampton Area  
 Northeast Bradford  
 Northeastern York County  
 Northern Bedford County  
 Northern Cambria  
 Northern Lebanon  
 Northern Lehigh  
 Northern Potter  
 Northern Tioga  
 Northern York County  
 Northgate  
 Northwest Area  
 Northwestern  
 Northwestern Lehigh  
 Norwin

O

Octorara Area  
 Oil City Area  
 Old Forge  
 Oley Valley

Schedule of Employers (Continued)

Oswayo Valley  
 Otto Eldred  
 Owen J. Roberts  
 Oxford Area

Ringgold  
 Riverside  
 Riverside Beaver County  
 Riverview  
 Rochester Area  
 Rockwood Area  
 Rose Tree Media

Steel Valley  
 Steelton-Highspire  
 Sto-Rox  
 Stroudsburg Area  
 Sullivan County  
 Susquehanna Community  
 Susquehanna Township  
 Susquenita

P

Palisades  
 Palmerton Area  
 Palmyra Area  
 Panther Valley  
 Parkland  
 Pen Argyl Area  
 Penn Cambria  
 Penn Crest  
 Penn Delco  
 Penn Hills  
 Penn Manor  
 Penn Trafford  
 Pennridge  
 Penns Manor  
 Penns Valley Area  
 Pennsbury  
 Pequea Valley  
 Perkiomen Valley  
 Peters Township  
 Philadelphia  
 Philipsburg-Osceola  
 Phoenixville Area  
 Pine Grove Area  
 Pine-Richland  
 Pittsburgh  
 Pittston Area  
 Pleasant Valley  
 Plum Boro  
 Pocono Mountain  
 Port Allegany  
 Portage Area  
 Pottsgrove  
 Pottstown  
 Pottsville Area  
 Punxsutawney Area  
 Purchase Line

S

Saint Clair Area  
 Saint Marys Area  
 Salisbury-Elk Lick  
 Salisbury Township  
 Saucon Valley  
 Sayre Area  
 Schuylkill Haven Area  
 Schuylkill Valley  
 Scranton City  
 Selinsgrove Area  
 Seneca Valley  
 Shade-Central City  
 Shaler Area  
 Shamokin Area  
 Shanksville-Stonycreek  
 Sharon City  
 Sharpsville Area  
 Shenandoah Valley  
 Shenango Area  
 Shikellamy  
 Shippensburg Area  
 Slippery Rock Area  
 Smethport Area  
 Solanco  
 Somerset Area  
 Souderton Area  
 South Allegheny  
 South Butler County  
 South Eastern  
 South Fayette Township  
 South Middleton  
 South Park  
 South Side Area  
 South Western  
 South Williamsport Area  
 Southeast Delco  
 Southeastern Greene  
 Southern Columbia Area  
 Southern Fulton  
 Southern Huntingdon  
 Southern Lehigh  
 Southern Tioga  
 Southern York County  
 Southmoreland  
 Spring Cove  
 Spring-Ford Area  
 Spring Grove Area  
 Springfield  
 Springfield Township  
 State College Area

T

Tamaqua Area  
 Titusville Area  
 Towanda Area  
 Tredyffrin-Easttown  
 Tri-Valley  
 Trinity Area  
 Troy Area  
 Tulpehocken Area  
 Tunkhannock Area  
 Turkeyfoot Valley  
 Tuscarora  
 Tussey Mountain  
 Twin Valley  
 Tyrone Area

U

Union  
 Union Area  
 Union City Area  
 Uniontown Area  
 Unionville-Chadds Ford  
 United  
 Upper Adams  
 Upper Darby  
 Upper Dauphin Area  
 Upper Dublin  
 Upper Merion Area  
 Upper Moreland  
 Upper Perkiomen  
 Upper Saint Clair

Q

Quaker Valley  
 Quakertown Community

R

Radnor Township  
 Reading  
 Red Lion Area  
 Redbank Valley  
 Reynolds  
 Richland  
 Ridgway Area  
 Ridley

V

Valley Grove  
 Valley View

W

Wallenpaupack Area  
 Wallingford Swarthmore  
 Warren County  
 Warrior Run  
 Warwick  
 Washington  
 Wattsburg Area  
 Wayne Highlands

Schedule of Employers (Continued)

Waynesboro Area	Woodland Hills
Weatherly Area	Wyalusing Area
Wellsboro Area	Wyoming Area
West Allegheny	Wyoming Valley West
West Branch Area	Wyomissing Area
West Chester Area	
West Greene	
West Jefferson Hills	
West Middlesex Area	Y
West Mifflin Area	York
West Perry	York Suburban
West Shore	Yough
West York Area	
Western Beaver County	
Western Wayne	
Westmont Hilltop	
Whitehall-Coplay	
Wilkes-Barre Area	
Wilkesburg	
William Penn	
Williams Valley	
Williamsburg Community	
Williamsport Area	
Wilmington Area	
Wilson	
Wilson Area	
Windber Area	
Wissahickon	

Area Vocational Technical Schools

A. W. Beattie Career Center	Eastern Westmoreland CTC	Mon Valley CTC
Admiral Peary AVTS	Erie County Technical School	Monroe County AVTS
Beaver County AVTS	Fayette County AVTS	Northern Tier Career Center
Bedford County Technical Center	Forbes Road Career and Technology Center	North Fayette County AVTS
Berks Career and Technical Center	Franklin County CTC	North Montco Technical Career Center
Bethlehem AVTS	Fulton County AVTS	North Westmoreland County AVTS
Bucks County AVTS	Greater Altoona CTC	Northumberland County AVTS
Butler County AVTS	Greater Johnstown AVTS	Parkway West AVTS
Carbon County AVTS	Greene County AVTS	Reading-Muhlenberg AVTS
Career Institute of Technology	Huntingdon County CTC	Schuylkill County AVTS
Central Montgomery County CTCS	Indiana County Technology Center	Somerset County Technology Center
Central Westmoreland CTC	Jefferson County-DuBois AVTS	Steel Center AVTS
Central PA Institute for Science and Technology	Juniata - Mifflin County AVTS	SUN Area CTC
Clarion County Career Center	Lancaster County CTC	Susquehanna County CTC
Clearfield County CTC	Lawrence County AVTS	Upper Bucks County AVTS
Columbia-Montour AVTS	Lebanon County AVTS	Venango Technology Center
Crawford County AVTS	Lehigh Career and Technical Institute	West Side AVTS
CTC of Lackawanna County	LENAPE AVTS	Western Area CTC
Cumberland-Perry AVTS	Lycoming County Career Consortium	Western Center for Technical Studies
Dauphin County Technical School	Mercer County AVTS	Wilkes-Barre AVTS
Delaware County AVTS	Middle Bucks Institute of Technology	York County AVTS
Eastern Center for Arts and Technology		

## Schedule of Employers (Continued)

## Intermediate Units

Allegheny #3	Chester County #24	Pittsburgh Mt. Oliver #2
Appalachia #8	Colonial Northampton #20	Riverview #6
Arin #28	Delaware County #25	Schuylkill #29
Beaver Valley #27	Intermediate Unit #1	Seneca Highlands #9
Berks County #14	Lancaster Lebanon #13	Tuscarora #11
Blast #17	Lincoln #12	Westmoreland #7
Bucks County #22	Luzerne #18	
Capital Area #15	Midwestern #4	
Carbon Lehigh #21	Montgomery County #23	
Central #10	Northeastern Education #19	
Central Susquehanna #16	Northwest Tri County #5	

## Colleges / Universities

State System of Higher Education	Bucks County Community College
Bloomsburg University	Butler County Community College
California University	Community College of Allegheny County
Cheyney University	Community College of Beaver County
Clarion University	Community College of Delaware County
East Stroudsburg University	Community College of Philadelphia
Education Resource	Harrisburg Area Community College
Edinboro University	Lehigh Carbon Community College
Indiana University	Luzerne County Community College
Kutztown University	Montgomery County Community College
Lock Haven University	Northampton County Area Community College
Mansfield University	Pennsylvania College of Technology
Millersville University	Pennsylvania State University
Shippensburg University	Reading Area Community College
Slippery Rock University	Westmoreland County Community College
West Chester University	

## Other

Berks County Earned Income Tax Bureau	Pennsylvania School for the Deaf
Department of Corrections - Commonwealth of Pennsylvania	Scotland School for Veterans Children
Department of Education - Commonwealth of Pennsylvania	Thaddeus Stevens School of Technology
Lancaster County Academy	Washington County Alternative School
Overbrook School for the Blind	Western Pennsylvania School for the Blind
Pennsylvania School Boards Association	Western Pennsylvania School for the Deaf
	York County High

## Schedule of Employers (Continued)

## Charter Schools (C.S.)

21st Century Cyber C.S.  
 Achievement House C.S.  
 Ad Prima C.S.  
 Agora Cyber C.S.  
 Alliance for Progress C.S.  
 Architecture & Design C.S.  
 Avon Grove C.S.  
 Bear Creek Community C.S.  
 Beaver Area Academic C.S.  
 Belmont C.S.  
 Bucks County Montessori C.S.  
 Career Connections C.S.  
 Center for Student Learning C.S. at Pennsbury  
 Central PA Digital Learning Foundation C.S.  
 Centre Learning Community C.S.  
 Chester County Family Academy C.S.  
 Christopher Columbus C.S.  
 City Charter High School  
 Collegium C.S.  
 Commonwealth Connections Academy C.S.  
 Crispus Attucks Youthbuild C.S.  
 Delaware Valley C.S.  
 Discovery C. S.  
 Evergreen Community C.S.  
 Erin Dudley Forbes C.S.  
 Eugenio Maria de Hostos Community Bilingual C.S.  
 Family C.S.  
 Fell C.S.  
 First Philadelphia C.S. for Literacy  
 Folk Arts - Cultural Treasures C.S.  
 Franklin Towne C.S.  
 Freire C.S.  
 GECAC Community C.S.  
 Germantown Settlement C.S.  
 Graystone Academy C.S.  
 Green Woods C.S.  
 Hope C.S.  
 Imani Education Circle C.S.  
 IMHOTEP Institute C.S.  
 Independence C.S.  
 Infinity C.S.  
 Keystone Education Center C.S.  
 Khepera C.S.  
 KIPP Academy C.S.  
 La Academia: The Partnership C.S.  
 Laboratory C.S.  
 Leadership Learning Partners C.S.  
 Lehigh Valley Academy Regional C.S.  
 Lehigh Valley C.S. for the Performing Arts  
 Lincoln C.S.  
 Manchester Academic C.S.  
 Mariana Bracetti Academy C.S.  
 Maritime Academy C.S.  
 Mastery Charter High School  
 MaST Community C.S.  
 Math, Civics & Sciences C.S.  
 Montessori Regional C.S.  
 Multi-Cultural Academy  
 New Foundations C.S.  
 New Media Technology C.S.  
 Nittany Valley C.S.  
 Northside Urban Pathways C.S.  
 Northwest PA Collegiate Academy C.S.  
 Northwood Academy C.S.  
 Nueva Esperanza Academy C.S.  
 PA Distance Learning C.S.  
 PA Learners Online Regional Cyber C.S.  
 Pennsylvania Cyber C.S.  
 Pennsylvania Leadership C.S.  
 Pennsylvania Virtual C.S.  
 People for People C.S.  
 Perseus House C.S. of Excellence  
 Philadelphia Academy C.S.  
 Philadelphia Community Academy of PA C.S.  
 Philadelphia Electrical & Technology Charter High School  
 Philadelphia Harambee Institute of Science and  
 Technology C.S.  
 Philadelphia Montessori C.S.  
 Philadelphia Performing Arts C.S.  
 Pocono Mountain C.S.  
 Preparatory Charter of Mathematics, Science, Technology  
 and Careers School  
 Propel C.S. - East  
 Propel C.S. - Homestead  
 Propel C.S. - McKeesport  
 Raising Horizons Quest C.S.  
 RAPA - Edison C.S.  
 Renaissance C.S.  
 Renaissance Advantage C.S.  
 Renaissance Academy - Edison C.S.  
 Richard Allen Preparatory C.S.  
 Ridgeview Academy C.S.  
 Roberto Clemente C.S.  
 Ronald H. Brown C.S.  
 Russell Byers C.S.  
 Sankofa Academy C.S.  
 School Lane C.S.  
 Souderton C.S. Collaborative  
 Spectrum C.S.  
 Sugar Valley C.S.  
 SUSQ-CYBER C.S.  
 Sylvan Heights Science C.S.  
 Tidioute Community C.S.  
 Tuscarora Blended Learning C.S.  
 Universal Institute C.S.  
 Urban League of Pittsburgh C.S.  
 Village C.S. of Chester-Upland  
 Wakisha C.S.  
 West Oak Lane C.S.  
 West Philadelphia Achievement Charter Elementary  
 School  
 Wissahickon C.S.  
 Wonderland C.S.  
 World Communications C.S.  
 Young Scholars C.S.  
 Young Scholars of Central PA C.S.

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