

# FINANCIAL SECTION

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JEFFERSON CITY  
COLUMBIA  
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## INDEPENDENT AUDITORS' REPORT

The Board of Trustees  
Public School Retirement System of Missouri  
Non-Teacher School Employee Retirement System of Missouri

We have audited the accompanying statement of plan net assets of the Public School Retirement System of Missouri and the Non-Teacher School Employee Retirement System of Missouri (the System) as of June 30, 2004 and the related statement of changes in plan net assets for the year then ended. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with U.S. generally accepted auditing standards. These 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 audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of the Public School Retirement System of Missouri and the Non-Teacher School Employee Retirement System of Missouri at June 30, 2004 and the changes in plan net assets for the year then ended, in conformity with U.S. generally accepted accounting principles.

The management's discussion and analysis on pages 18 through 22 are not a required part of the basic financial statements but are supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming an opinion on the financial statements taken as a whole. The supplementary schedules of funding progress and employer contributions on pages 35 and 36 are not a required part of the basic financial statements of the System, but are required by the Governmental Accounting Standards Board (GASB). The supplementary information included on pages 37 through 39 is presented for purposes of additional analysis and is not a required part of the basic financial statements of the System. Such information, included on pages 35 through 39, has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

*Williams - Keepers LLC*

September 3, 2004

## Management's Discussion and Analysis

June 30, 2004

This discussion and analysis of the financial position of the Public School Retirement System and the Non-Teacher School Employee Retirement System (collectively referred to as the Systems) provides an overview of the Systems' financial activities for the fiscal year ended June 30, 2004. We encourage you to consider the information presented here in conjunction with additional information presented in the financial statements and required supplementary information.

### Financial Highlights

The following highlights are explained in more detail for each System later in this discussion.

The combined net assets of the Systems at June 30, 2004 were \$24.0 billion. The net assets were up \$2.3 billion from June 30, 2003. This increase was primarily due to the increase in the fair value of investments of \$2.1 billion.

The overall investment return was 12.4% for the Public School Retirement System (PSRS) and 12.1% for the Non-Teacher School Employee Retirement System (NTRS). Our relatively conservative asset allocation provided returns that exceeded our assumed rate of return of 8%, but trailed our peers of large institutional pension systems that took more risk with a more aggressive asset allocation and larger equity exposure.

The Systems' funding objective is to meet long-term benefit obligations through the accumulation of contributions and investment income. This funding shall be carried out in such a way to ensure that the burden of paying retirement costs shall be shared equitably by present and succeeding generations of members and taxpayers.

As of June 30, 2004, the funded ratios were 82.0% for PSRS and 82.7% for NTRS. As of June 30, 2003, the funded ratios were 81.1% for PSRS and 81.9% for NTRS. As of June 30, 2004, we calculated the actuarial value of assets using an asset smoothing method by which investment returns above or below 8% are recognized over a five-year period.

Revenues for the year were \$3.5 billion. This figure is comprised of contribution revenue of \$0.9 billion and investment income of \$2.6 billion.

Expenses increased 10.8% over the prior year from \$1.0 billion to \$1.2 billion. Most of this increase represents increased retirement benefits paid to members. Approximately \$9.7 million was paid to retirees electing the new Partial Lump Sum Option (PLSO). This option allows eligible retirees to elect to have their lifetime monthly benefits actuarially reduced in exchange for the right to also receive a one-time payment at retirement equal to 12, 24, or 36 times the Option 1, Single-Life benefit amount. Since this option was not available until September, this option will have an increased effect on cash flows in fiscal year 2005.

### Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the financial report of the Systems. The financial report consists of: the basic financial statements, comprised of the Statements of Plan Net Assets and the Statements of Changes in Plan Net Assets; the notes to the basic financial statements; and the required and other supplementary information.

The Statements of Plan Net Assets (page 23) present information on the assets and liabilities of the Systems, with the difference between the two reported as net assets. The net assets of the Systems reflect the resources available to pay benefits to members when due. Over time, increases and decreases in net assets measure whether the Systems' financial position is improving or deteriorating.

The Statements of Changes in Plan Net Assets (page 24) present information detailing the changes in net assets that occurred during the current fiscal year. All changes in net assets are reported on an accrual basis. This means that the revenue or expense is recognized as soon as the underlying event giving rise to the change occurs, regardless of when the actual cash is received or paid. Thus, revenues and expenses are reported in this statement for some items that will not result in cash flows until future

fiscal periods. For example, contributions due from a district, even though not yet paid by year end, will be reflected as revenue. Earned vacation accruals will be reflected as an expense, even though they have not been paid to employees.

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes can be found on pages 25 through 34. The report also contains required supplementary information in addition to the basic financial statements themselves. The Schedules of Funding Progress (page 35) include historical trend information about the actuarially funded status of each plan from a long-term, ongoing perspective and the progress made in accumulating assets to pay benefits when due.

The Schedules of Employer Contributions (page 36) present historical trend information about the annual required contributions of employers and the actual contributions made by employers.

Other supplementary schedules are also included. The Schedule of Administrative Expenses (page 37) presents the overall cost of administering the Systems. The Schedule of Professional/Consultant Fees (page 39) further details this category of administrative expense.

The Schedule of Investment Expenses (page 38) shows the costs associated with investing the assets of the Systems. These expenses are shown as a reduction of revenue on the Statements of Changes in Plan Net Assets.

### Financial Analysis of the Public School Retirement System

The Public School Retirement System (PSRS) is a mandatory cost-sharing multiple employer retirement system for full-time certificated employees and certain part-time employees of participating employers. PSRS members were required to contribute 10.5% of their annual covered salary during 2004. The employer was required to match that amount. Most PSRS members do not contribute to Social Security, except for employees hired after March 31, 1986 who contribute to Medicare only.

#### Assets

Total assets of PSRS as of June 30, 2004 were \$26.9 billion and were mostly comprised of cash, investments and contributions due from employers. Total assets increased by \$2.6 billion or 10.6% from the prior year primarily due to increased investment earnings.

#### Liabilities

Total liabilities as of June 30, 2004 were \$4.7 billion and were mostly comprised of obligations under security lending arrangements and payables from the purchase of investments. Total liabilities increased by \$.5 billion. This increase was primarily due to increased obligations under security lending arrangements.

#### Net Assets

PSRS assets exceeded liabilities at June 30, 2004 by \$22.2 billion. This was up from 2003 net assets of \$20.0 billion by \$2.2 billion. This increase was a result of improved investment earnings that totaled \$2.4 billion for the year. Benefit payments and other expenses exceeded contribution revenue by \$300.7 million. This trend is a natural progression in a mature defined benefit plan.

### Public School Retirement System Plan Net Assets (000's)

	2004	2003	Change
Cash & investments	\$ 25,421,407	\$ 23,039,370	\$ 2,382,037
Receivables	1,442,099	1,248,772	193,327
Other	9,615	9,561	54
Total assets	<u>26,873,121</u>	<u>24,297,703</u>	<u>2,575,418</u>
Total liabilities	<u>4,722,741</u>	<u>4,249,721</u>	<u>473,020</u>
<b>Plan net assets</b>	<u>\$ 22,150,380</u>	<u>\$ 20,047,982</u>	<u>\$ 2,102,398</u>

### Public School Retirement System Changes in Plan Net Assets (000's)

	<u>2004</u>	<u>2003</u>	<u>Change</u>
<b>Additions</b>			
Members' contributions	\$ 405,614	\$ 378,434	\$ 27,180
Employer contributions	359,762	355,979	3,783
Investment income	2,402,566	873,340	1,529,226
Other	488	351	137
Total additions	<u>3,168,430</u>	<u>1,608,104</u>	<u>1,560,326</u>
<b>Deductions</b>			
Monthly benefits	1,024,740	930,450	94,290
Refunds of contributions	36,018	28,474	7,544
Administrative expenses	5,265	4,674	591
Other	9	1	8
Total deductions	<u>1,066,032</u>	<u>963,599</u>	<u>102,433</u>
<b>Change in plan net assets</b>	<u>\$ 2,102,398</u>	<u>\$ 644,505</u>	<u>\$ 1,457,893</u>

#### Revenues – Additions to Plan Net Assets

The reserves needed to finance retirement benefits are accumulated through the collection of employer and employee contributions and through investment earnings. Total contributions for the year increased by \$31.0 million to \$765.4 million. This was a 4.2% increase over the prior year. Retirement contributions are calculated at 10.5% of retirement salary for each member. The employer matches this amount. Members may also pay contributions to reinstate previously withdrawn service credit or to purchase various types of elective credit.

The net investment gain was \$2.4 billion as compared to a net investment gain of \$873.3 million in 2003. All investment related expenses, such as fees paid to investment managers, are reflected as a reduction in revenue and are accounted for in this net figure.

#### Expenses – Deductions from Plan Net Assets

The primary expenses of PSRS include the payment of pension benefits to members and beneficiaries, refunds of contributions to former members, and the cost of administering the System. Total expenses for fiscal year 2004 were \$1.1 billion, an increase of 10.6% over fiscal year 2003.

Benefit expenses increased by \$94.3 million. This was a result of cost-of-living increases applied to the benefits of current retirees and the addition of 2,505 new service and disability retirees. There were no changes to the benefit formula during 2004. Refunds of contributions increased by \$7.6 million to \$36 million.

Administrative expenses increased by \$0.6 million to \$5.3 million. This was a 12.6% increase. This increase is mainly attributable to providing a 3% COLA increase for staff members, conducting a required Trustee election and adding five staff members for Member Services. The cost of these items was charged 60% to PSRS and 40% to NTRS. Because our Board continually strives to manage the Systems in a cost-effective manner, our costs remain below that of comparable public funds. The total cost (including all investment expenses) to administer the Systems in fiscal year 2004 was less than 0.17%. Per the 2003 Cost Effective Measurement Study of U.S. Pension Funds, the average cost to administer public funds is 0.31%.

## FINANCIAL SECTION

### Financial Analysis of the Non-Teacher School Employee Retirement System

The Non-Teacher School Employee Retirement System (NTRS) is a mandatory, cost-sharing, multiple employer retirement system for non-certificated employees and certain part-time certificated employees of participating employers. NTRS members were required to contribute 5% of their annual covered salary during 2004. The employer was required to match that amount. NTRS members also contribute to Social Security.

#### Assets

Total assets of NTRS as of June 30, 2004 were \$2.3 billion and were mostly comprised of cash, investments, and contributions due from employers. Total assets increased by \$0.3 billion or 13% from the prior year primarily due to increased investment returns.

#### Liabilities

Total liabilities as of June 30, 2004 were \$369.6 million and were mostly comprised of obligations under security lending arrangements and payables from the purchase of investments. Total liabilities increased by \$49.3 million. This increase was primarily due to an increased liability for obligations under security lending arrangements.

#### Net Assets

NTRS assets exceeded liabilities at the close of fiscal year 2004 by \$1.9 billion. This was up from 2003 net assets by \$0.2 billion. This increase was a result of improved investment earnings that totaled \$198.4 million for the year. Because NTRS is a much younger plan than PSRS, contribution revenues exceeded benefit payments and other expenses by \$12.1 million.

### Non-Teacher School Employee Retirement System Plan Net Assets (000's)

	2004	2003	Change
Cash & investments	\$ 2,118,407	\$ 1,892,077	\$ 226,330
Receivables	139,426	105,998	33,428
Other	15	-	15
Total assets	<u>2,257,848</u>	<u>1,998,075</u>	<u>259,773</u>
Total liabilities	<u>369,578</u>	<u>320,305</u>	<u>49,273</u>
<b>Plan net assets</b>	<u>\$ 1,888,270</u>	<u>\$ 1,677,770</u>	<u>\$ 210,500</u>

### Non-Teacher School Employee Retirement System Changes in Plan Net Assets (000's)

	2004	2003	Change
<b>Additions</b>			
Members' contributions	\$ 50,625	\$ 48,994	\$ 1,631
Employer contributions	49,977	48,933	1,044
Investment income	198,389	73,188	125,201
Other	10	16	(6)
Total additions	<u>299,001</u>	<u>171,131</u>	<u>127,870</u>
<b>Deductions</b>			
Monthly benefits	74,871	67,399	7,472
Refunds of contributions	10,420	8,033	2,387
Administrative expenses	3,210	2,946	264
Total deductions	<u>88,501</u>	<u>78,378</u>	<u>10,123</u>
<b>Change in plan net assets</b>	<u>\$ 210,500</u>	<u>\$ 92,753</u>	<u>\$ 117,747</u>

### Revenues – Additions to Plan Net Assets

The reserves needed to finance retirement benefits are accumulated through the collection of employer and employee contributions and through investment earnings. Total contributions for the year increased by \$2.7 million to \$100.6 million. This was a 2.7% increase over the prior year. Retirement contributions are calculated at 5% of retirement salary for each member. The employer matches this amount. Members may also pay contributions to reinstate previously withdrawn service credit or to purchase various types of elective credit.

The net investment gain was \$198.4 million as compared to a net investment gain of \$73.2 million in 2003. All investment related expenses, such as fees paid to investment managers, are reflected as a reduction in revenue and are accounted for in this net figure.

### Expenses – Deductions from Plan Net Assets

The primary expenses of NTRS include the payment of pension benefits to members and beneficiaries, refunds of contributions to former members, and the cost of administering the System. Total expenses for fiscal year 2004 were \$88.5 million, an increase of 12.9% over fiscal year 2003.

Benefit expenses increased by \$7.5 million. This was a result of cost-of-living increases applied to the benefits of current retirees and the addition of 1,118 new service and disability retirees. There were no changes to the benefit formula during 2004. Refunds of contributions increased by \$2.4 million to \$10.4 million.

Administrative expenses increased by \$0.3 million to \$3.2 million. This was a 9.0% increase. This increase is mainly attributable to providing a 3% COLA increase for staff members, conducting a required

Trustee election and adding five staff members for Member Services. The cost of these items was charged 60% to PSRS and 40% to NTRS. As noted for PSRS, our Board continually strives to manage the Systems in a cost effective manner. The total cost (including all investment expenses) to administer the Systems in fiscal year 2004 was less than 0.17%. Per the 2003 Cost Effective Measurement Study of U.S. Pension Funds, the average cost to administer public funds is 0.31%.

### Summary

Due to the long-term nature of defined benefit pension plans, it is important to look at the financial performance of the Systems over a period of years and not just at this single point in time. Although our earnings exceeded the 8% return assumption in 2004, our long-term financial concerns remain. The current contribution rates are still below the annual required contribution rates of 27.76% for PSRS and 12.56% for NTRS. Unless our investment returns greatly exceed our assumptions and expectations, we can expect contribution rate increases over the next several years. In addition, management will continue to strive to improve the financial position of the Systems through a prudent investment program and long-term strategic planning.

### Requests for Information

This financial report is designed to provide the Board of Trustees, our members, and other users of our financial report with a general overview of the Systems' finances and to demonstrate the Systems' accountability for the money they receive. If you have any questions about this report or need additional financial information, contact the Public School and Non-Teacher School Employee Retirement System, P.O. Box 268, Jefferson City, MO 65102.

## Statements of Plan Net Assets

As of June 30, 2004 with comparative totals for June 30, 2003

	PSRS	NTRS	Totals	
			June 30, 2004	June 30, 2003
<b>ASSETS</b>				
Cash	\$ 56,239,259	\$ 10,966,140	\$ 67,205,399	\$ 80,091,737
Receivables				
Contributions	115,256,048	10,448,208	125,704,256	118,873,551
Accrued interest and dividends	81,821,679	6,982,477	88,804,156	80,138,690
Investment sales	1,244,646,934	121,978,719	1,366,625,653	1,155,538,911
Due from NTRS	150,034	-	150,034	94,105
Other	224,754	16,633	241,387	124,090
Total receivables	1,442,099,449	139,426,037	1,581,525,486	1,354,769,347
Investments, at fair value				
Fixed income	9,244,379,497	790,981,656	10,035,361,153	10,426,208,619
Domestic stocks	8,740,375,111	736,729,209	9,477,104,320	8,103,655,384
International equities	3,848,121,518	326,240,790	4,174,362,308	2,968,338,051
Short term investments	451,558,155	48,688,253	500,246,408	1,101,773,646
Total investments	22,284,434,281	1,902,639,908	24,187,074,189	22,599,975,700
Invested securities lending collateral	3,080,733,856	204,801,001	3,285,534,857	2,251,379,438
Prepaid expenses	379,233	14,666	393,899	191,069
Capital assets, net of accumulated depreciation	9,235,232	-	9,235,232	9,369,445
Total assets	26,873,121,310	2,257,847,752	29,130,969,062	26,295,776,736
<b>LIABILITIES</b>				
Accounts payable	9,002,831	770,853	9,773,684	7,598,656
Interest payable	1,947,252	213,926	2,161,178	1,601,216
Securities lending collateral	3,080,733,856	204,801,001	3,285,534,857	2,251,379,438
Investment purchases	1,630,853,923	163,506,329	1,794,360,252	2,309,029,566
Due to PSRS	-	150,034	150,034	94,105
Lease liability	-	-	-	10,036
Compensated absences	203,543	135,695	339,238	312,537
Total liabilities	4,722,741,405	369,577,838	5,092,319,243	4,570,025,554
<b>NET ASSETS HELD IN TRUST FOR PENSION BENEFITS</b>				
	<u>\$ 22,150,379,905</u>	<u>\$ 1,888,269,914</u>	<u>\$ 24,038,649,819</u>	<u>\$ 21,725,751,182</u>
<i>(Schedules of Funding Progress for the plans are presented on page 35)</i>				

See accompanying Notes to the Financial Statements.

## Statements of Changes in Plan Net Assets

For the year ended June 30, 2004 with comparative totals for the year ended June 30, 2003

	Totals Year Ended			
	PSRS	NTRS	2004	2003
<b>ADDITIONS</b>				
<b>Contributions</b>				
Employer	\$ 359,762,556	\$ 49,976,898	\$ 409,739,454	\$ 404,912,353
Member	405,614,103	50,625,153	456,239,256	427,428,136
Total contributions	<u>765,376,659</u>	<u>100,602,051</u>	<u>865,978,710</u>	<u>832,340,489</u>
<b>Investment income</b>				
<i>From investing activities:</i>				
Net appreciation in fair value of investments	1,985,675,475	163,386,408	2,149,061,883	495,108,666
Interest from investments	279,862,927	23,927,227	303,790,154	322,567,429
Interest from bank deposits	62,438	2,624	65,062	92,014
Dividends	158,216,208	13,144,066	171,360,274	144,155,474
Total investment income	<u>2,423,817,048</u>	<u>200,460,325</u>	<u>2,624,277,373</u>	<u>961,923,583</u>
Less investment expenses	31,832,929	2,907,038	34,739,967	28,514,808
Net income from investing activities	<u>2,391,984,119</u>	<u>197,553,287</u>	<u>2,589,537,406</u>	<u>933,408,775</u>
<i>From security lending activities:</i>				
Security lending gross income	35,870,940	2,746,093	38,617,033	51,564,081
Less security lending activity expenses:				
Agent fees	2,140,864	166,117	2,306,981	3,488,537
Broker rebates	23,148,361	1,743,953	24,892,314	34,957,235
Total security lending expenses	<u>25,289,225</u>	<u>1,910,070</u>	<u>27,199,295</u>	<u>38,445,772</u>
Net income from security lending activity	<u>10,581,715</u>	<u>836,023</u>	<u>11,417,738</u>	<u>13,118,309</u>
Total net investment income	<u>2,402,565,834</u>	<u>198,389,310</u>	<u>2,600,955,144</u>	<u>946,527,084</u>
<b>Other income</b>				
NTRS capital asset charge	309,557	-	309,557	240,353
Miscellaneous income	178,621	9,695	188,316	127,039
Total other income	<u>488,178</u>	<u>9,695</u>	<u>497,873</u>	<u>367,392</u>
Total additions	<u>3,168,430,671</u>	<u>299,001,056</u>	<u>3,467,431,727</u>	<u>1,779,234,965</u>
<b>DEDUCTIONS</b>				
Monthly benefits	1,024,739,904	74,870,838	1,099,610,742	997,848,298
Refunds of contributions	36,018,258	10,419,660	46,437,918	36,507,823
Administrative expenses	5,265,259	3,210,161	8,475,420	7,620,021
Other expenses	8,882	128	9,010	1,761
Total deductions	<u>1,066,032,303</u>	<u>88,500,787</u>	<u>1,154,533,090</u>	<u>1,041,977,903</u>
Net increase	2,102,398,368	210,500,269	2,312,898,637	737,257,062
<b>NET ASSETS HELD IN TRUST FOR PENSION BENEFITS</b>				
Beginning of year	20,047,981,537	1,677,769,645	21,725,751,182	20,988,494,120
End of year	<u>\$ 22,150,379,905</u>	<u>\$ 1,888,269,914</u>	<u>\$ 24,038,649,819</u>	<u>\$ 21,725,751,182</u>

See accompanying Notes to the Financial Statements.

## Notes to the Financial Statements

June 30, 2004

(with comparative information for June 30, 2003)

### Note 1 – Plan Descriptions

The Board of Trustees of the Public School Retirement System administers two separate retirement systems, the Public School Retirement System (PSRS) and the Non-Teacher School Employee Retirement System (NTRS). The Board of Trustees consists of seven members, three of whom are elected PSRS active members, one an elected active member of NTRS and three persons appointed by the governor, one of whom must be a retired member of either PSRS or NTRS.

The funds of the two Systems are invested in conjunction with each other but each System retains title to its own investments. Each System's assets may be used only for the payment of benefits to the members of the separate System in accordance with the statutes governing that System as well as expenses required to administer the System.

#### The Public School Retirement System

The Public School Retirement System of Missouri (PSRS) is a mandatory cost-sharing multiple employer retirement system for all full-time certificated employees and certain part-time certificated employees of all public school districts in Missouri (except the school districts of St. Louis and Kansas City) and all public community colleges. The System also includes certificated employees of PSRS, Missouri State Teachers' Association, Missouri State High School Activities Association, and certain employees of the state of Missouri who elected to remain covered by PSRS under legislation enacted in 1986, 1987 and 1989.

PSRS was established as an independent trust fund by an Act of the Missouri General Assembly effective August 1, 1945. Statutes governing the Retirement System are found in Sections 169.010-169.141 and Sections 169.560-169.595, RSMo. It is a defined benefit plan providing service retirement, death and disability benefits to its members. Members are vested for service retirement benefits after accruing five years of creditable service. Individu-

als who (a) are at least age 60 and have a minimum of five years of service, (b) have 30 years of service, or (c) qualify for benefits under the "Rule of 80" (service credit and age total at least 80) are entitled to a monthly benefit for life, which is calculated using a 2.5% formula factor. Beginning July 1, 2001, and ending June 30, 2008, a 2.55% formula factor is used to calculate benefits for members who have 31 or more years of service. Actuarially age-reduced benefits are available for members with five to 24.9 years of service at age 55, or with 25 years of service (if not yet age 55). Members who are younger than age 55 and who do not qualify under the "Rule of 80" but have between 25 and 29.9 years of credit may retire with a lesser benefit formula factor during a window that will close July 1, 2008.

Beginning September 2003, members that are three years beyond normal retirement can elect to have their lifetime monthly benefits actuarially reduced in exchange for the right to also receive a one-time partial lump sum (PLSO) payment at retirement equal to 12, 24, or 36 times the Option 1, Single-Life benefit amount. Annual cost-of-living adjustments (COLAs) are provided for eligible service and disability retirees and for surviving beneficiaries receiving payments under optional retirement plans, up to a lifetime maximum of 80% of the original benefit amount.

**Contributions** – PSRS members were required to contribute 10.5% of their annual covered salary during both fiscal years. The employing districts were required to match the contributions made by employees. The contribution rate is set each year by the Board of Trustees upon the recommendation of the independent actuary within the contribution restrictions set in Section 169.030, RSMo. Administrative costs are financed through investment earnings. Contributions for employees of the state of Missouri were made by the state in accordance with the actuarially determined contribution rate needed to fund current costs and prior service costs of state employees as authorized in Section 104.342.8, RSMo.

## FINANCIAL SECTION

**Members** – The number of PSRS membership and benefit recipients served by the System at June 30 was:

	<u>2004</u>	<u>2003</u>
Retirees and beneficiaries receiving benefits	34,230	32,249
Inactive members entitled to but not yet receiving benefits	5,338	5,031
Active members:		
Vested	52,628	51,580
Non-vested	<u>21,169</u>	<u>22,767</u>
Total active members	73,797	74,347
Other inactive members	<u>6,336</u>	<u>5,300</u>
Total	<u>119,701</u>	<u>116,927</u>

**Employers** – PSRS had 545 contributing employers during 2003-2004, and 546 during 2002-2003.

### The Non-Teacher School Employee Retirement System

The Non-Teacher School Employee Retirement System of Missouri (NTRS) is a mandatory cost-sharing multiple employer retirement system for all public school district employees (except the school districts of St. Louis and Kansas City), employees of the Missouri Association of School Administrators, and community college employees (except the Community College of St. Louis). Employees of covered districts who work 20 or more hours per week on a regular basis and who are not contributing members of the Public School Retirement System of Missouri (PSRS) must contribute to NTRS. Employees of PSRS who do not hold Missouri teaching certificates also contribute to NTRS.

NTRS was established as a trust fund by an Act of the Missouri General Assembly effective October 13, 1965. Statutes governing the Retirement System are found in Sections 169.600-169.715 and Sections 169.560-169.595, RSMo. The statutes place responsibility for the operation of NTRS on the Trustees of the Public School Retirement System.

NTRS is a defined benefit plan providing service retirement and disability benefits to its members. Members are vested for service retirement benefits after accruing five years of creditable service. Individuals who (a) are at least age 60 and have a minimum of five years of service, (b) have 30 years of service, or (c) qualify for benefits under the “Rule of 80” (service credit and age total at least 80) are entitled to a monthly benefit for life, which

is calculated using a 1.61% formula factor. Members qualifying for “Rule of 80” or “30 and Out” are entitled to a temporary .8% benefit multiplier until reaching minimum Social Security age (currently age 62). Actuarially age-reduced retirement benefits are available with five years of service at age 55. Members who are younger than age 55 and who do not qualify under the “Rule of 80” but have between 25 and 29.9 years of credit may retire with a lesser benefit formula factor during a window that will close July 1, 2008. Beginning September 2003, members that are three years beyond normal retirement can elect to have their lifetime monthly benefits actuarially reduced in exchange for the right to also receive a one-time partial lump sum (PLSO) payment at retirement equal to 12, 24, or 36 times the Option 1, Single-Life benefit amount. Annual cost-of-living adjustments (COLAs) up to a lifetime maximum of 80% of the original benefit amount are provided for eligible service and disability retirees and for surviving beneficiaries receiving payments under optional retirement plans.

**Contributions** – NTRS members were required to contribute 5.0% of their annual covered salary during both years. The employing districts were required to match the contributions made by their employees. The contribution rate is set each year by the Board of Trustees upon the recommendation of the independent actuary within the contribution restrictions in Section 169.620, RSMo. Administrative costs proportional to its membership size are reimbursed by NTRS to the Public School Retirement System and are financed through investment earnings.

## FINANCIAL SECTION

**Members** – The number of NTRS membership and benefit recipients served by the System at June 30 was:

	<u>2004</u>	<u>2003</u>
Retirees and beneficiaries receiving benefits	15,445	14,837
Inactive members entitled to but not yet receiving benefits	3,246	3,002
Active members:		
Vested	22,683	21,408
Non-Vested	<u>23,197</u>	<u>25,455</u>
Total active members	45,880	46,863
Other inactive members	<u>15,591</u>	<u>14,649</u>
Total	<u>80,162</u>	<u>79,351</u>

**Employers** – NTRS had 536 contributing employers during both years.

## Note 2 – Summary of Significant Accounting Policies

**Basis of Accounting** – The financial statements of both Systems were prepared using the accrual basis of accounting. For both Systems, member and employer contributions are recognized when due, pursuant to formal commitments and statutory requirements. Benefits and refunds are recognized when due and payable in accordance with the statutes governing the Systems. Expenses are recognized when the liability is incurred, regardless of when payment is made. Administrative expenses are funded through investment earnings.

**Cash** – Cash includes cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

**Receivables** – Receivables consist primarily of contributions owed and yet to be remitted by the employing districts, pending investment trades and interest and dividends payable to the Systems as of the end of each fiscal year.

**Method Used to Value Investments** – Investments are reported at fair value on a trade date basis. Securities traded on international exchanges are valued at the last reported sales price at current exchange rates. Mortgages are valued on the basis of future principal and interest payments and are discounted at prevailing interest rates for similar instruments. Investments that do not have an established market are reported at estimated fair value.

**Capital Assets** – The building and most other capital assets are owned by PSRS and are stated at cost less depreciation accumulated since acquisition. The stated value does not purport to represent replacement or realized value. Costs of major additions and improvements are capitalized. Expenditures for maintenance and repairs are charged to operations as incurred. Depreciation is calculated using the straight-line method, with estimated lives ranging from three to 40 years in the following major classes: computers and software, three years; vehicles, five years; equipment, five years; building and land improvements, 15 years; building, 40 years.

NTRS owns office equipment purchased before 1997 and follows the same guidelines for depreciation. NTRS reimburses PSRS for the use of capital assets used by the two Systems on a proportional basis. The amount of this reimbursement was \$309,557 in 2004 and \$240,353 in 2003.

**Estimates** – The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of net assets held in trust for pension benefits at June 30, 2004. Actual results could differ from those estimates.

**Note 3 – Designations of Net Assets Held in Trust for Pension Benefits**

The Systems designate the net assets held in trust for pension benefits for the following specific purposes:

**PSRS**

	<u>2004</u>	<u>2003</u>
<i>Designated for Members' Contributions (Member Reserves) –</i> Accumulation of active and terminated member contributions plus interest.	\$ 4,896,240,545	\$ 4,657,734,877
<i>Designated for the Payment of Benefits to Present Retirees –</i> Transfers from Member Reserves at retirement and an actuarially determined transfer from Operating Reserves to fund the System's obligation for benefit payments and cost-of-living adjustments to current retirees and beneficiary recipients.	12,624,731,188	11,386,250,807
<i>Designated for Additional Deposit Annuities –</i> Accumulation of the additional deposits over and above the contributions required by law. Defined contribution annuity payments are made to current retirees from this reserve.	1,193,950	1,292,088
<i>Designated for Operating Expenses/Benefits to Future Retirees (Operating Reserves) –</i> Accumulation of employer contributions and investment income used to fund future benefit payments, interest on member accounts and administration and maintenance expenses of the System.	4,628,214,222	4,002,703,765
<b>Net Assets Held In Trust For Pension Benefits</b>	<u>\$22,150,379,905</u>	<u>\$20,047,981,537</u>

**NTRS**

	<u>2004</u>	<u>2003</u>
<i>Designated for Members' Contributions (Member Reserves) –</i> Accumulation of active and terminated member contributions plus interest.	\$ 423,501,594	\$ 383,179,328
<i>Designated for the Payment of Benefits to Present Retirees –</i> Transfers from Member Reserves at retirement and an actuarially determined transfer from Operating Reserves to fund the System's obligation for benefit payments and cost-of-living adjustments to current retirees and beneficiary recipients.	804,863,982	731,059,146
<i>Designated for Operating Expenses/Benefits to Future Retirees (Operating Reserves) –</i> Accumulation of employer contributions and investment income used to fund future benefit payments, interest on member accounts and administration and maintenance expenses of the System.	659,904,338	563,531,171
<b>Net Assets Held In Trust For Pension Benefits</b>	<u>\$ 1,888,269,914</u>	<u>\$ 1,677,769,645</u>

## FINANCIAL SECTION

**Note 4 – Deposits and Investments**

**Deposits** – Cash balances include short-term securities held by the custodial bank to meet future System obligations and operating balances held by the depository banks.

At June 30, 2004, the PSRS carrying amount of deposits at the depository bank was \$11,923,921 and the bank balance was \$4,531,429. Of the bank balance, \$100,000 was covered by federal depository insurance. The remaining \$4,431,429 was collateralized with securities held by the pledging financial institution's trust department or agent in the System's name.

At June 30, 2004, the NTRS carrying amount of deposits at the depository bank was (\$671,176) and the bank balance was \$0. Since the bank balance was \$0, no amount was required to be collateralized. To maximize investment income, the float caused by outstanding checks was invested in overnight repurchase agreements, thus causing the negative book balance. These overnight repurchase agreements are reflected on the Schedule of Investments in Note 4.

The deposits held by the custodial bank are in a pooled short-term investment fund which are not required to be categorized.

The following are the balances of these accounts at June 30:

	<u>2004 Book</u>	<u>2004 Bank</u>	<u>2003 Book</u>	<u>2003 Bank</u>
<b>PSRS</b>				
Depository bank	\$ 11,923,921	\$ 4,531,429	\$ 16,884,157	\$ 14,588,084
Custodial bank	41,765,660	41,765,660	38,109,933	38,109,933
<b>NTRS</b>				
Depository bank	\$ (671,176)	\$ -	\$ (577,789)	\$ -
Custodial bank	10,302,490	10,302,490	23,412,206	23,412,206

**Authorization of Investments** – Funds for both Systems that are in excess of a safe operating balance are invested by the investment agents under policies and procedures established by the Board of Trustees. Chapter 160.040, RSMo as amended effective August 13, 1984, authorizes any investment which a prudent person acting in a like capacity and familiar with similar matters would use in the conduct of an enterprise of a like character and with like aims. Any person with fiduciary responsibility with respect to the Systems is covered by this “prudent person” rule.

**Categories of Custodial Credit Risk** – The Governmental Accounting Standards Board Statement No. 3 requires disclosure of custodial credit risk. Investments are categorized into three categories of credit risk. Category 1 includes investments

that are insured or registered or for which the securities are held by the Systems' custodial agent in the name of each System. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the name of each System. Category 3 includes uninsured and unregistered investments, which are held by the custodial agent, but not in the Systems' names.

A security for purposes of credit risk disclosure is a transferable financial instrument that evidences ownership or creditorship. “Securities” do not include investments made in open-end pooled funds or securities on loan to broker-dealers under the security lending program. Such investments are shown as “not categorized.”

## FINANCIAL SECTION

**PSRS**

	<u>June 30, 2004</u>	<u>June 30, 2003</u>
<b>Category 1 Investments</b>		
Municipals	\$ 5,918,455	\$ 18,995,888
U.S. Government & agencies securities	2,262,209,909	3,469,437,328
Domestic fixed income	1,703,635,959	1,601,906,662
Domestic equities	5,732,753,650	5,120,315,836
International equities	3,303,545,619	2,283,849,138
REITS	-	8,731,610
<b>Category 2 Investments</b>		
Repurchase agreements	2,549,677	526,665
<b>Investments Not Categorized</b>		
Loaned under the securities lending program		
U.S. Government & agencies securities	1,968,468,370	1,175,432,075
Domestic corporate fixed income securities	127,339,698	64,444,910
Domestic equities	446,300,952	396,286,661
International equities	538,624,836	459,031,133
Pooled funds		
Domestic corporate fixed income securities	2,646,903,719	3,299,006,678
Domestic equities	3,097,174,959	1,964,540,138
Money market fund	451,558,155	1,026,676,673
<b>Total Investments</b>	<u>22,286,983,958</u>	<u>20,889,181,395</u>
Security lending collateral (not categorized)	3,080,733,856	2,095,194,779
<b>Total</b>	<u>\$ 25,367,717,814</u>	<u>\$ 22,984,376,174</u>
<b>Reconciliation to Statements of Plan Net Assets</b>		
Number from above	\$ 25,367,717,814	\$ 22,984,376,174
Less:		
Security lending collateral	(3,080,733,856)	(2,095,194,779)
Repurchase agreements reported as cash	(2,549,677)	(526,665)
Investments per Statements of Plan Net Assets	<u>\$ 22,284,434,281</u>	<u>\$ 20,888,654,730</u>

## FINANCIAL SECTION

**NTRS**

	<u>June 30, 2004</u>	<u>June 30, 2003</u>
<b>Category 1 Investments</b>		
Municipals	\$ 11,020,815	\$ 1,538,048
U.S. Government & agencies securities	232,149,591	283,769,008
Domestic fixed income	135,293,744	132,363,051
Domestic equities	494,557,039	426,293,352
International equities	288,673,678	195,728,912
REITS	1,301,633	703,864
<b>Category 2 Investments</b>		
Repurchase agreements	1,334,826	1,736,565
<b>Investments Not Categorized</b>		
Loaned under the securities lending program		
U.S. Government & agencies securities	129,254,569	95,389,446
Domestic fixed income	9,646,743	4,530,475
Domestic equities	28,511,660	26,535,870
International equities	37,388,029	29,728,868
Pooled funds		
Domestic corporate fixed income securities	223,076,872	279,395,050
Domestic equities	263,077,282	260,248,053
Money market fund	48,688,253	75,096,973
<b>Total Investments</b>	<u>1,903,974,734</u>	<u>1,713,057,535</u>
Security lending collateral (not categorized)	204,801,001	156,184,659
<b>Total</b>	<u><u>\$ 2,108,775,735</u></u>	<u><u>\$ 1,869,242,194</u></u>
<b>Reconciliation to Statements of Plan Net Assets</b>		
Number from above	\$ 2,108,775,735	\$ 1,869,242,194
Less:		
Security lending collateral	(204,801,001)	(156,184,659)
Repurchase agreements reported as cash	(1,334,826)	(1,736,565)
Investments per Statements of Plan Net Assets	<u><u>\$ 1,902,639,908</u></u>	<u><u>\$ 1,711,320,970</u></u>

## FINANCIAL SECTION

**Derivatives** – The Systems are parties to certain financial investments with off-balance sheet risk used in the normal course of business to generate earnings and reduce exposure to fluctuations in market conditions. Derivatives are reported at fair value on the Statement of Plan Net Assets.

International security managers are authorized to engage in forward contracts to exchange different currencies at a specified date and rate. These forward contracts involve elements of custodial and market risk in excess of the amount recognized in the Statements of Plan Net Assets. The forward exchange contracts purchased/sold in effect at June 30 are shown below.

<u>2004</u>	<u>Purchase Value</u>	<u>Fair Value</u>
PSRS	\$ 415,301,646	\$ 414,301,788
NTRS	37,987,519	37,896,109
<u>2003</u>	<u>Purchase Value</u>	<u>Fair Value</u>
PSRS	\$ 61,969,938	\$ 62,812,527
NTRS	4,982,163	4,972,295

The Net Appreciation in Fair Value of Investments found on the Statements of Changes in Plan Net Assets includes for PSRS a net gain on forward contracts and currency disposal of \$11,931,529 during 2003-2004 and a net loss of \$1,722,322 during 2002-2003. NTRS had a similar net gain of \$978,997 during 2003-2004 and a net loss of \$149,542 in 2002-2003.

Certain managers are authorized to enter into contractual commitments involving other financial instruments with off-balance-sheet risk. During the year, the Systems held Russell 2000 futures, S&P 500 futures, equity linked notes, and Treasury futures. These are used to minimize the expenses and volatility of the portfolio.

In addition to the currency forwards listed above, the following derivatives were held by the Systems at June 30, 2004:

<u>Type</u>	<u>PSRS Notional Value</u>	<u>NTRS Notional Value</u>
S&P 500 futures	\$ 33,003,471	\$ 2,750,458
Russell 2000 futures	6,528,744	550,907
Equity linked notes	4,678,721	432,740
Treasury futures	67,202,827	5,365,663
Total	<u>\$ 111,413,763</u>	<u>\$ 9,099,768</u>

The Systems' exposure to derivatives as a percent of total investments does not differ substantially from June 30, 2003.

**Security Lending Activity** – Under the “prudent person” authority of the governing statutes and in accordance with the policies set by the Board of Trustees, the Systems lend securities to broker-dealers and banks pursuant to a form of loan agreement. The Systems' custodial bank is authorized to lend available securities to approved broker-dealers and banks subject to the receipt of acceptable collateral.

During the fiscal year, the Systems lent securities and received cash (both U.S. and foreign currency), securities issued or guaranteed by the U.S. government or its agencies, sovereign debt of foreign countries, and irrevocable bank letters of credit as collateral. The Systems did not have the ability to pledge or sell noncash collateral absent borrower default. Borrowers were required to deliver collateral for each loan equal to: (1) in the case of loaned securities denominated in U.S. dollars or whose primary trading market was located in the United States, or sovereign debt issued by foreign governments, 102% of the fair value of the loaned securities; and (2) in the case of loaned securities not denominated in U.S. dollars or whose primary trading market was not located in the United States, 105% of the fair value of the loaned securities.

The Systems did not impose any restrictions during the fiscal year on the amount of the loans that the custodial bank made on their behalf. There were no failures by any borrowers to return loaned securities or pay distributions thereon during the year. There were no losses during the year resulting from a default of the borrowers or the custodial bank.

The Systems and borrowers each maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested; together with the cash collateral of other qualified tax-exempt plan lenders in a collective investment pool. The average duration of such investment pool as of June 30, 2004 was 55 days and an average weighted maturity of 483 days. Because the loans were terminable at will, their duration did not match the duration of the investments made with cash collateral. On June 30, 2004 the Systems had no credit risk exposure to borrowers because the amounts the Systems owed the borrowers exceeded the amounts the borrowers owed the Systems.

The collateral held (including both cash collateral recognized in the Statements of Plan Net Assets and non-cash collateral) and the fair values of securities on loan for PSRS were \$3,213,285,256 and \$3,143,015,722 for June 30, 2004 and \$2,363,532,666 and \$2,270,277,863 for June 30, 2003. Net security lending income was \$10,581,715 for the 2003-2004 fiscal year and \$12,129,376 for the 2002-2003 fiscal year.

The collateral held (including both cash collateral recognized in the Statements of Plan Net Assets and non-cash collateral) and the fair values of securities on loan for NTRS were \$220,773,492 and \$215,953,336 for June 30, 2004 and \$183,147,489 and \$174,836,594 for June 30, 2003. Net security lending income was \$836,023 for the 2003-2004 fiscal year and \$988,933 for the 2002-2003 fiscal year.

The collective investment pool in which the collateral received from security lending loans is invested has the following characteristics. The fair value of the investments held by the pooled fund is based upon valuations provided by a recognized pricing service. Because the pooled fund does not meet the requirements of Rule 2a-7 of the Investment Company Act of 1940, the fund's investments are val-

ued at fair market value for reporting purposes. The pooled fund is not registered with the Securities and Exchange Commission.

The custodial bank and, consequently, the investment vehicles it sponsors (including the pooled fund), are subject to the oversight of the Federal Reserve Board and the Massachusetts Commissioner of Banks. The fair value of the Systems' position in the pooled fund is not the same as the value of the fund shares. The Systems had no involuntary participation in an external investment pool through this fund and no income from one fund was assigned to another fund by the custodial bank during either fiscal year.

### Note 5 – Additional Deposits Program

Section 169.035, RSMo provides for an additional deposits program for PSRS members. Members may make payments above the required defined benefit contribution amount to the retirement system in order to provide a monthly annuity at retirement based on the total of the deposits and interest.

This annuity is in addition to the defined benefit allowance provided by the System. Contributions to the program are tax-sheltered. As of September 1, 1996 new deposits to the program were limited to members currently with deposits in the program. No additional deposits were made during 2003-2004. The deposits and interest of the one member who has not yet retired totaled \$1,465 as of June 30, 2004.

The deposits to the program are included in the investment program of the PSRS defined benefit plan. The additional deposits program's basis of accounting and the asset valuation are identical to the defined benefit plan.

### Note 6 – Retirement Plans

#### Section 401 (a) Defined Benefit Plan

All full-time System employees holding a valid Missouri teaching certificate are covered by PSRS. All other eligible employees are members of NTRS. Both Systems provide retirement and disability benefits, annual cost-of-living adjustments and death benefits to plan members and beneficiaries. Chapter 169 RSMo contains the statutory provisions of both Systems.

PSRS members were required to contribute 10.5% of their annual covered salary during both years. PSRS, as the employer, was required to match that amount. The contribution rate is established and may be amended by the Board of Trustees. Employer contributions to PSRS totaled \$24,164 for the 2003-2004 fiscal year and \$28,618 for 2002-2003. The amounts for these years are equal to the required contributions.

NTRS members were required to contribute 5% of their annual covered salary during both years. PSRS, as the employer, was required to match that amount. The contribution rate is established and may be amended by the Board of Trustees. Employer contributions to NTRS totaled \$216,429 for the 2003-2004 fiscal year and \$195,887 for 2002-2003. The amounts for these years are equal to the required contributions.

#### ***Section 457 Deferred Compensation Plan***

A voluntary Section 457 deferred compensation plan is administered to provide additional retirement benefits for employees. The plan provides for employer-matching contributions up to a set maximum. The total contributions are subject to the limitations established in IRC Section 457. The Board of Trustees has authority to establish the employer contribution levels. For employees that are members of PSRS, the System will match up to \$50 per month. For employees that are members of NTRS, the System will match \$50 plus 0.52% of salary per month. For certain employees, the System will make employer-paid contributions of \$1,000 per month. This is governed by individual employment contracts as approved by the Board of Trustees.

All employees immediately vest in the employer-matching and employer-paid contributions. Employer-matching contributions totaled \$60,804 for the 2003-2004 fiscal year and \$57,722 for the 2002-2003 fiscal year. Employer-paid contributions totaled \$24,000 for the 2003-2004 fiscal year and \$17,250 for the 2002-2003 fiscal year. Employee contributions totaled \$126,939 for the 2003-2004 fiscal year and \$131,077 for the 2002-2003 fiscal year.

Maintenance of individual member accounts and custody of assets have been contracted to a third party administrator and investment custodian. Total contributions are sent directly to the third party administrator by the employer. Employees can self-direct investments of their contributions and their respective share of matching contributions in a number of investment options. Because the System does not hold the plan's assets and does not have significant administrative responsibilities, the plan's assets and changes in net assets are not reported in the Systems' financial statements.

#### ***Note 7 – Risk Management***

The Systems are exposed to various risks of loss related to natural disasters, errors and omissions, loss of assets, torts, etc. The Systems have chosen to cover such losses through the purchase of commercial insurance. There have been no material insurance claims filed or paid during the past three years.

The Systems have a disaster recovery plan that provides for continued computer operations at a remote location should the retirement office be unavailable for normal operations.

#### ***Note 8 – Commitments and Contingencies***

PSRS was committed to the future purchase of investments at a cost of \$1,630,853,923 on June 30, 2004 and to the future purchase of \$2,145,805,458 in investments on June 30, 2003. NTRS had investment commitments of \$163,506,329 on June 30, 2004 and \$163,224,108 on June 30, 2003.

Certain legal proceedings are pending against PSRS and NTRS arising from normal activities. Although unable to predict the outcome of these matters, the Systems believe the final outcome of these actions will not have a material adverse effect on the Systems' financial statements.

## Schedules of Funding Progress

### Required Supplementary Information

#### Public School Retirement System

(Dollar amount in thousands)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL)– Entry Age (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a % of Covered Payroll ((b-a)/c)
6/30/1999	\$ 17,209,870	\$ 16,373,144 <sup>1</sup>	\$ (836,726)	105.1%	\$ 2,690,007	(31.1)%
6/30/2000	19,437,223	18,279,113 <sup>2</sup>	(1,158,110)	106.3	2,836,062	(40.8)
6/30/2001	21,146,294	21,282,203 <sup>3</sup>	135,909	99.4	2,982,051	4.6
6/30/2002	22,236,105	23,333,937 <sup>4</sup>	1,097,832	95.3	3,213,461	34.2
6/30/2003	20,047,982	24,719,450 <sup>5</sup>	4,671,468	81.1	3,373,058	138.5
6/30/2004	21,501,572	26,225,259 <sup>6</sup>	4,723,687	82.0	3,408,230	138.6

<sup>1</sup>Legislative improvement to age of eligibility (“Rule of 80”) and ad hoc benefit increases for retirees added \$982.5 million to the AAL.

<sup>2</sup>Legislative improvements to the benefit formula and ad hoc benefit increases for retirees added \$643 million to the AAL.

<sup>3</sup>Legislative improvements to the benefit formula and ad hoc benefit increases for retirees added \$630.3 million to the AAL.

Actuarial assumptions were also revised.

<sup>4</sup>There were no legislative changes in fiscal year 2002.

<sup>5</sup>The extension of the 25-and-Out provision to 2008 is included in the AAL for 2003.

<sup>6</sup>There were no legislative changes in fiscal year 2004.

#### Non-Teacher School Employee Retirement System

(Dollar amounts in thousands)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL)– Entry Age (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a % of Covered Payroll ((b-a)/c)
6/30/1999	\$ 1,335,308	\$ 1,168,511 <sup>1</sup>	\$ (166,797)	114.3%	\$ 685,272	(24.3)%
6/30/2000	1,522,660	1,395,300 <sup>2</sup>	(127,360)	109.1	735,400	(17.3)
6/30/2001	1,686,242	1,636,076 <sup>3</sup>	(50,166)	103.1	814,158	(6.2)
6/30/2002	1,810,619	1,855,982 <sup>4</sup>	45,363	97.6	895,420	5.1
6/30/2003	1,677,770	2,049,716 <sup>5</sup>	371,946	81.9	971,177	38.3
6/30/2004	1,837,308	2,221,210 <sup>6</sup>	383,902	82.7	984,866	39.0

<sup>1</sup>Legislative improvements to age of eligibility and benefit formula plus ad hoc benefit increases for retirees added \$80.3 million to the AAL.

<sup>2</sup>Legislative improvements to the benefit formula and ad hoc benefit increases for retirees added \$121.7 million to the AAL.

<sup>3</sup>Legislative improvements to the benefit formula and ad hoc benefit increases for retirees added \$126.4 million to the AAL.

Actuarial assumptions were also revised.

<sup>4</sup>There were no legislative changes in fiscal year 2002.

<sup>5</sup>The extension of the 25-and-Out provision to 2008 is included in the AAL for 2003.

<sup>6</sup>There were no legislative changes in fiscal year 2004.

## Schedules of Employer Contributions

### Required Supplementary Information

#### Public School Retirement System

Year Ended June 30	Annual Required Contribution (ARC)	Percentage Contributed
1999	\$ 287,698,736	100.0%
2000	304,944,352	100.0
2001	324,525,673	100.0
2002	340,000,556	100.0
2003	355,979,027	94.5
2004	359,762,556	75.7

#### Non-Teacher School Employee Retirement System

Year Ended June 30	Annual Required Contribution (ARC)	Percentage Contributed
1999	\$ 30,012,859	100.0%
2000	34,185,605	100.0
2001	37,500,243	100.0
2002	45,773,119	100.0
2003	48,933,326	92.6
2004	49,976,808	80.2

#### Notes to the Schedules of Trend Information

The information presented in the required supplementary schedules was determined as part of the actuarial valuation at the dates indicated. Additional information as of the latest actuarial valuation follows:

Valuation date	June 30, 2004
Actuarial cost method	Entry Age Normal
Amortization method	Level Percent, Open
Remaining amortization period	
PSRS	30 years (1)
NTRS	30 years (2)
Asset valuation method	5-year smoothed market Marked to Market as of June 30, 2003
Actuarial assumptions:	
Investment rate of return	8.0%
Projected salary increases*	
PSRS	5.0 - 10.0%
NTRS	5.0 - 10.0%
*Includes inflation at	3.5%
Cost-of-living adjustments	3.5%

- 1) 30 year amortization assumes an ARC rate of 27.76% for fiscal year 2005. The annual statutory increase in the total contribution rate may not exceed 1% of pay. Contribution rates will be established by actuarial valuation.
- 2) 30 year amortization assumes an ARC rate of 12.56% for fiscal year 2005. The annual statutory increase in the total contribution rate may not exceed .5% of pay. Contribution rates will be established by actuarial valuation.

See accompanying Independent Auditors' Report.

## Schedule of Administrative Expenses

For the year ended June 30, 2004

	PSRS	NTRS	TOTAL
<b>Personal services</b>	\$ 2,900,969	\$ 1,932,723	\$ 4,833,692
<b>Professional services</b>			
Actuarial	67,911	42,790	110,701
Audit	20,100	13,400	33,500
Computer consultants	95,152	63,435	158,587
Insurance consultant	3,600	2,400	6,000
Legislative consultant	19,200	12,800	32,000
Other consultants	12,583	8,389	20,972
Legal expenses	132,532	18,989	151,521
Total professional services	351,078	162,203	513,281
<b>Communications</b>			
Information and publicity	366,311	246,021	612,332
Postage	69,143	55,778	124,921
Printing	73,492	62,302	135,794
Staff field	23,517	8,061	31,578
Telephone	65,952	43,967	109,919
Total communications	598,415	416,129	1,014,544
<b>Miscellaneous</b>			
Building and utilities	72,762	48,505	121,267
Board of Trustees	90,640	60,426	151,066
Insurance	73,214	48,809	122,023
Office	205,475	136,983	342,458
Staff development	105,705	70,568	176,273
Miscellaneous	89,305	24,258	113,563
Total miscellaneous	637,101	389,549	1,026,650
<b>Charge for use of capital assets</b>	-	309,557	309,557
<b>Depreciation expense</b>	777,696	-	777,696
<b>Total administrative expenses</b>	\$ 5,265,259	\$ 3,210,161	\$ 8,475,420

See accompanying Independent Auditors' Report.

## Schedule of Investment Expenses

For the year ended June 30, 2004

	<u>PSRS</u>	<u>NTRS</u>	<u>TOTAL</u>
Investment management expenses			
U.S. equity	\$ 14,250,508	\$ 1,195,701	\$ 15,446,209
International equity	8,549,128	717,222	9,266,350
Fixed income	5,380,705	456,786	5,837,491
Private equity	792,958	61,948	854,906
Total investment management expenses	<u>28,973,299</u>	<u>2,431,657</u>	<u>31,404,956</u>
Investment consultant fees	378,246	36,768	415,014
Custodial bank fees	2,089,436	177,312	2,266,748
Investment staff expenses	391,948	261,301	653,249
Total investment income expenses	<u>\$ 31,832,929</u>	<u>\$ 2,907,038</u>	<u>\$ 34,739,967</u>
Security lending expenses			
Agent fees	\$ 2,140,864	\$ 166,117	\$ 2,306,981
Broker rebates	23,148,361	1,743,953	24,892,314
Total security lending expenses	<u>\$ 25,289,225</u>	<u>\$ 1,910,070</u>	<u>\$ 27,199,295</u>

See accompanying Independent Auditors' Report.

## Schedule of Professional/Consultant Fees

For the year ended June 30, 2004

	<u>PSRS</u>	<u>NTRS</u>	<u>TOTAL</u>
Actuarial services	\$ 67,911	\$ 42,790	\$ 110,701
Legal counsel	132,532	18,989	151,521
Financial audit	20,100	13,400	33,500
Legislative consulting	19,200	12,800	32,000
Technology consulting	95,152	63,435	158,587
Insurance consulting	3,600	2,400	6,000
Other consulting	12,583	8,389	20,972
Total fees	<u>\$ 351,078</u>	<u>\$ 162,203</u>	<u>\$ 513,281</u>

*See accompanying Independent Auditors' Report.*