DEPARTMENT OF THE TREASURY
Bradley I. Abelow
State Treasurer

DIVISION OF PENSIONS AND BENEFITS
Frederick J. Beaver
Director

State of New Jersey
DIVISION OF PENSIONS AND BENEFITS
PO Box 295 • Trenton, NJ 08625-0295

TO THE HONORABLE
JON S. CORZINE
GOVERNOR of the STATE OF NEW JERSEY

Dear Governor Corzine:

The Board of Trustees of the

PUBLIC EMPLOYEES' RETIREMENT SYSTEM

is pleased to present the Fiscal Year 2005 Annual Report in accordance with the provisions of N.J.S.A. 43:15A-21.

Respectfully submitted,

George B. Babula

GEORGE B. BABULA
Chairperson

Public Employees' Retirement System

BOARD OF TRUSTEES

SIGNIFICANT LEGISLATION

CHAPTER 177, P.L. 2004

This law concerns the retirement allowance of Teachers' Pension and Annuity Fund (TPAF) and Public Employees' Retirement System (PERS) veteran members who retire after having attained age 55, and who have at least 35 years of service credit. It provides that the retirement allowance shall be based on the 12-month period of membership providing the largest possible benefit to the member or the member's beneficiary instead of the last year of employment upon which contributions to the annuity savings fund or contingent reserve fund are made.

This law was effective December 22, 2004.

CHAPTER 6, P.L. 2005

This law allows retired administrative law judges and workers' compensation judges to be recalled for service, with the judge's consent.

It amends N.J.S.A.52:14F-4 and N.J.S.A.34:15-49, which requires these judges to retire upon attaining age 70, to provide that upon such recall the retired administrative law judge or judge of compensation will have all the powers of such a judge and will be paid a per diem allowance to be fixed by the Director/ Chief Administrative Law Judge or the Director/Chief Judge of the Division of Workers' Compensation, as applicable. The recalled judge will be reimbursed for reasonable expenses actually incurred in connection with the assignment and will be provided with such facilities as may be required in the performance of the judge's duties. Those per diem compensation and expenses will be paid by the State. Payment for services and expenses will be made in the same manner as payment is made to the judges of the Office of Administrative Law or Division of Workers' Compensation, as applicable, from which the judge retired.

This law was effective January 19, 2005.

CHAPTER 64, P.L. 2005

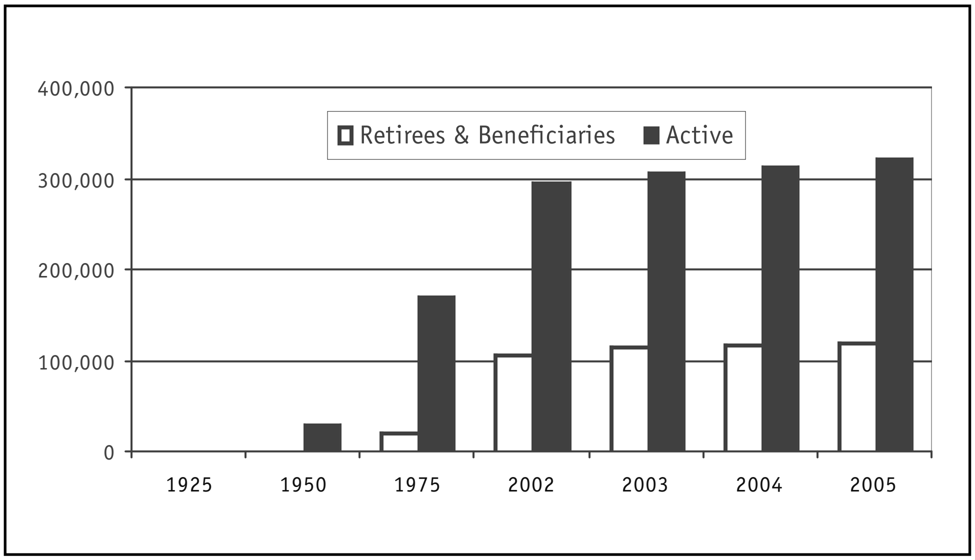
This law amends several statutes to define members of Operations Northern Watch and Southern Watch as veterans for the purposes of civil service hiring preferences, the purchase of service credit and the calculation of veterans benefits in the Public Employees' Retirement System (PERS) and Teachers' Pension and Annuity Fund (TPAF), the purchase of service credit in the Police and Firemen’s Retirement System (PFRS), and the receipt of a property tax deduction or exemption.

Operation Northern Watch and Operation Southern Watch are the names given to the missions that monitored and controlled airspace above and below the 33rd parallel in Iraq, otherwise known as "no-fly zones."

The pension-related sections of this law are effective immediately (April 7, 2005).

MEMBERSHIP

- As of June 30, 2005, the active membership of the System totaled 322,985. This includes 97,877 State employees and 225,108 employees from 1,682 participating local employers. Total inactive membership as of June 30, 2005 was 51,170.
- There were 121,177 retirees and beneficiaries receiving annual pensions totaling $1,605,184,591. *(This includes cost-of-living increases paid under the provisions of the Pension Adjustment Act)*.
- Beneficiaries of 730 active and 4,738 retired members received lump sum death benefits in the amount of $103,933,291.
- The System's assets totaled $28,028,338,402 at the close of the fiscal year 2005.



MEMBERSHIP ACTIVITY

During fiscal year 2005, the following transactions were processed by the Division of Pensions and Benefits on behalf of the membership of the Public Employees' Retirement System of New Jersey.

- **ENROLLMENTS** - 24,691 new members were enrolled in PERS during fiscal year 2005.
- **LOANS** - 75,087 loans were issued to members. The total loans receivable as of June 30, 2005 is $427,671,798.
- **WITHDRAWALS** - there were 7,272 withdrawals during fiscal year 2005.
- **RETIREMENT** - 7,481 members retired under the following retirement types:

TYPE OF RETIREMENT	
Service	4,371
Early	477
Ordinary Disability	1,054
Accidental Disability	55
Veteran	418
Deferred	346
Over 55 — Early	733
Other	27
TOTAL	7,481

OPTION SELECTION	
Maximum	3,811
Option 1	626
Option 2	171
Option 3	73
Option 4	14
Option A	1,151
Option B	376
Option C	755
Option D	502
Other	2
TOTAL	7,481

KPMG LLP
New Jersey Headquarters
150 John F. Kennedy Parkway
Short Hills, NJ 07078

Independent Auditors' Report

The Board of Trustees
State of New Jersey
Public Employees' Retirement System:

We have audited the accompanying statement of fiduciary net assets of the State of New Jersey Public Employees' Retirement System (the System) as of June 30, 2005, and the related statement of changes in fiduciary 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 auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 financial position of the State of New Jersey Public Employees' Retirement System as of June 30, 2005, and the changes in its financial position for the year then ended in conformity with U.S. generally accepted accounting principles.

Management's Discussion and Analysis and the supplementary information included in the schedule of funding progress and schedule of employer contributions are not a required part of the basic financial statements but are supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming an opinion on the financial statements that collectively comprise the System's basic financial statements. The schedule of changes in fiduciary net assets by fund is presented for purposes of additional analysis and is not a required part of the basic financial statements of the System. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly presented in all material respects in relation to the financial statements taken as a whole.

KPMG LLP

December 14, 2005

STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

Management's Discussion and Analysis
June 30, 2005

Our discussion and analysis of the Public Employees' Retirement System (the System) financial performance provides an overview of the System's financial activities for the fiscal year ended June 30, 2005. Please read it in conjunction with the basic financial statements and financial statement footnotes which follow this discussion.

FINANCIAL HIGHLIGHTS

2005 - 2004

- Net assets held in trust for pension and post-retirement medical benefits increased by $882,461,208 as a result of fiscal year 2005's operations from $23,033,352,407 to $23,915,813,615.
- Additions for the year were $2,873,421,564, which are comprised of member and employer pension contributions of $944,599,323 and investment income of $1,928,822,241.
- Deductions for the year were $1,990,960,356, which are comprised of benefit and refund payments of $1,965,358,238 and administrative expenses of $25,602,118.

THE STATEMENT OF FIDUCIARY NET ASSETS AND THE STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS

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

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

FINANCIAL ANALYSIS

STATEMENT OF FIDUCIARY NET ASSETS

2005 - 2004

	2005	2004	Increase (Decrease)
Assets	$28,028,338,402	$27,087,808,205	$940,530,197
Liabilities	4,112,524,787	4,054,455,798	58,068,989
Net Assets	$23,915,813,615	$23,033,352,407	$882,461,208

The System's assets mainly consist of cash, securities lending collateral, investments and contributions due from members and participating employers. Between fiscal years 2004 and 2005, total assets increased by $940.5 million or 3.5%. The total assets increased due to increase in contributions receivable from members and employers. The increase in member contribution is based on increase in membership and elimination of a reduction in the employee contribution rate (returning to the normal rate of 5% from 3%), which was effective July 1, 2004 for State employees and January 1, 2005 for local employees.

Employer contributions receivables include contribution receivables from local employers for appropriations due April 1, 2006 based on Chapter 108, P.L. 2003, which provided that the State Treasurer will reduce local employer PERS normal and accrued liability contributions to be a percentage of the amount certified annually by the PERS to 40% for payments due in State fiscal year 2006. Employer contributions receivables are also including State appropriation based on Chapter 23, P.L. 2002 (early retirement incentive benefits to State employees) and appropriation due from local employers, based on Chapter 127, 128, and 129, P.L. 2003 (early retirement incentive benefits to local employees).

Liabilities consist of pension and death benefit payments owed to members and beneficiaries, noncontributory group insurance premiums owed to the System's insurance provider, securities lending collateral and rebates payable, and other payables. Total liabilities increased by $58.1 million or 1.4% over last year. This is mainly due to an increase in benefits payable to retirees and beneficiaries.

Net assets held in trust for pension and post-retirement medical benefits increased by $882.5 million or 3.8%.

STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS

ADDITIONS TO FIDUCIARY NET ASSETS
2005 - 2004

	2005	2004	Increase (Decrease)
Member Contributions	$533,862,353	$374,864,048	$158,998,305
Employer Contributions & Other	410,736,970	774,456,965	(363,719,995)
Investment	1,928,822,241	2,778,643,257	(849,821,016)
Totals	$2,873,421,564	$3,927,964,270	$(1,054,542,706)

Additions primarily consist of member and employer contributions and earnings from investment activities. Member contributions increased by $159.0 million or 42.4% due to increase in active member count and the contribution rate of 5% back from 3%, which was effective July 1, 2004 for State employees and January 1, 2005 for local employees.

Employer contributions dropped by $363.7 million or 47.0% over last year. The State made a contribution of $190.8 million for fiscal year 2005 post-retirement medical (PRM). Also, employer contributions include appropriation due April 1, 2006 from local employers, based on Chapter 108, P.L. 2003; State appropriation based on Chapter 23, P.L. 2002; and appropriation due from local employers, based on Chapter 127, 128, and 129, P.L. 2003.

For fiscal year 2005, the 50% of available excess valuation assets could be utilized to offset normal contributions. Thereafter, a certain percentage of available excess valuation assets may be used as specified in the legislation. The State and local employers were not required to make a normal contribution to the System between 1997 and 2004 based on Pension Security legislation passed in 1997.

Investment & other revenues decreased by $849.8 million or 30.6% due to decrease in net appreciation in fair value of investments.

The total investment gain for all pension funds was estimated to be 8.7% compared to 14.2% gain in the prior year.

DEDUCTIONS FROM FIDUCIARY NET ASSETS
2005 - 2004

	2005	2004	Increase (Decrease)
Benefits	$1,899,871,351	$1,771,806,236	$128,065,115
Refunds & Adjustments	65,486,887	65,677,159	(190,272)
Administrative Expenses	25,602,118	18,619,582	6,982,536
Totals	$1,990,960,356	$1,856,102,977	$134,857,379

Deductions are mainly comprised of pension benefit payments to retirees and beneficiaries, refunds of contributions to former members, and administrative costs incurred by the System. Benefit payments increased by $128.1 million or 7.2% partly due to an increase in number of retirees. The number of refunds processed has decreased compared to last year due to fewer terminations. Administrative expenses have increased by $7.0 million or 37.5% mainly due to the reimbursement to the State General Fund for the Special Project Fund Appropriation for the system reengineering project.

RETIREMENT SYSTEM AS A WHOLE

The overall funded ratios of 91.3% for fiscal year 2005 and 97.9% for fiscal year 2004 indicate that the System has sufficient assets to meet its benefit obligations.

CONTACTING SYSTEM FINANCIAL MANAGEMENT

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

STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

Statement of Fiduciary Net Assets

June 30, 2005

		PENSION FUND	POST-RETIREMENT MEDICAL FUND	TOTAL
Assets:				
Securities lending collateral	$	3,953,288,908	—	3,953,288,908
Investments, at fair value:				
Cash Management Fund		691,868,555	32,864	691,901,419
Bonds		118,360,381	6,828	118,367,209
Common Pension Fund A		11,409,902,828	658,209	11,410,561,037
Common Pension Fund B		5,873,527,783	338,829	5,873,866,612
Common Pension Fund D		4,404,736,054	254,098	4,404,990,152
Mortgage Backed Securities		105,990,035	6,114	105,996,149
Total investments		22,604,385,636	1,296,942	22,605,682,578
Receivables:				
Contributions:				
Members		68,518,669	—	68,518,669
Employers		845,969,563	—	845,969,563
Accrued interest and dividends		124,743,734	—	124,743,734
Members' loans		427,671,798	—	427,671,798
Other		2,463,152	—	2,463,152
Total receivables		1,469,366,916	—	1,469,366,916
Total assets		28,027,041,460	1,296,942	28,028,338,402
Liabilities:				
Accounts payable and accrued expenses		14,320,010	—	14,320,010
Retirement benefits payable		138,076,181	—	138,076,181
NCGI premiums payable		3,699,778	—	3,699,778
Cash overdraft		3,139,910	—	3,139,910
Securities lending collateral and rebates payable		3,953,288,908	—	3,953,288,908
Total liabilities		4,112,524,787	—	4,112,524,787
Net Assets:				
Held in trust for pension benefits	$	23,914,516,673	1,296,942	23,915,813,615

See schedule of funding progress on pages 27-28.
See accompanying notes to financial statements.

STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

Statement of Changes in Fiduciary Net Assets

Year ended June 30, 2005

	PENSION FUND	POST-RETIREMENT MEDICAL FUND	TOTAL
Additions:			
Contributions:			
Members	$ 533,862,353	—	533,862,353
Employers	219,912,516	190,824,454	410,736,970
Other	—	—	—
Total contributions	753,774,869	190,824,454	944,599,323
Investment income:			
Net appreciation in fair value of investments	1,189,990,877	97,706	1,190,088,583
Interest	511,024,216	—	511,024,216
Dividends	231,924,448	—	231,924,448
	1,932,939,541	97,706	1,933,037,247
Less: investment expense	4,215,006	—	4,215,006
Net investment income	1,928,724,535	97,706	1,928,822,241
Total additions	2,682,499,404	190,922,160	2,873,421,564
Deductions:			
Benefits	1,709,117,882	190,753,469	1,899,871,351
Withdrawals	65,486,887	—	65,486,887
Administrative expenses	25,602,118	—	25,602,118
Total deductions	1,800,206,887	190,753,469	1,990,960,356
Change in net assets	882,292,517	168,691	882,461,208
Net assets - Beginning of year	23,032,224,156	1,128,251	23,033,352,407
Net assets - End of year	$ 23,914,516,673	1,296,942	23,915,813,615

See accompanying notes to financial statements.

(1) DESCRIPTION OF THE SYSTEM

The State of New Jersey Public Employees' Retirement System (the System; PERS) is a cost-sharing multiple-employer contributory defined benefit plan which was established as of January 1, 1955, under the provisions of N.J.S.A. 43:15A. The System is included along with other state-administered pension trust and agency funds in the basic financial statements of the State of New Jersey.

At June 30, 2004, the date of the most recent actuarial valuation, participating employers consisted of the following:

	Participating employers
State of New Jersey	1
County agencies	66
Municipalities	584
School districts	564
Other public agencies	468
Total	1,683

The System's designated purpose is to provide retirement, death, disability and medical benefits to certain qualified members. Membership in the System is mandatory for substantially all full-time employees of the State of New Jersey or any county, municipality, school district or public agency, provided the employee is not required to be a member of another state-administered retirement system or other state pension fund or local jurisdiction's pension fund. The System's Board of Trustees is primarily responsible for the administration of the System.

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

Vesting and Benefit Provisions:

The vesting and benefit provisions are set by N.J.S.A. 43:15A and 43:3B. The System provides retirement, death and disability benefits, as well as medical benefits for certain qualified members. All benefits vest after eight to ten years of service, except for medical benefits, which vest after 25 years of service or under the disability provisions of the System. Retirement benefits for age and service are available at age 60 and are generally determined to be 1/55 of final average salary for each year of service credit (as defined). Final average salary equals the average salary for the final three years of service prior to retirement (or highest three years' compensation if other than the final three years). Members may seek early retirement after achieving 25 years service credit, as defined, or they may elect deferred retirement after achieving eight to ten years of service credit, in which case benefits would begin the first day of the month after the member attains normal retirement age.

Members are always fully vested for their own contributions and, after three years of service credit, become vested for earnings on their contributions at 2% per annum. In the case of death before retirement, members' beneficiaries are entitled to full interest credited to the members' accounts.

Eligible retirees receiving monthly benefits are entitled to cost-of-living increases equal to 60% of the change in the average consumer price index for the calendar year in which the pensioner retired as compared to the average consumer price index for a 12-month period ending with each August 31st immediately preceding the year in which the adjustment becomes payable. The regular retirement allowance is multiplied by the 60% factor as developed and results in a dollar amount of the adjustment payable. Retired members become eligible for pension adjustment benefits after 24 months of retirement.

Chapter 23, P.L. 2002 provided early retirement incentive benefits to State employees who meet specified age and service requirements and who retire within a specified time period that generally extends from February 1, 2002 to July 1, 2002. The incentive benefits include an additional three years of service credit to employees who are at least 50 years of age with at least 25 years of service credit; State paid health care benefits to employees who are at least 60 years of age with at least 20 but less than 25 years of service credit; and an additional monthly benefit of $500 per month for 24 months following the date of retirement to employees who are at least 60 years of age with at least 10 but not more than 20 years of service credit. For those eligible for veterans' retirement benefit, the incentive is an additional pension of 3/55 of the compensation upon which the retirement benefit is based to employees who are at least 55 years of age with 25 or more years of service credit. Similarly, Chapter 127, 128, and 129, P.L. 2003 provided early retirement incentive benefits to local employees.

Chapter 353, P.L. 2001 provided an increase in the special veterans' retirement allowance and the ordinary and accidental disability retirement allowances. The special veterans retirement allowance increased from 50% to 54.5% of the members' compensation during the highest-paid year of service. The minimum ordinary disability retirement allowance increased from 40% to 43.6% of final average compensation, and the accidental disability retirement allowance increased from 66.66% to 72.7% of the actual annual compensation at the time of the accident. Existing retirees and beneficiaries are eligible for the increases, which was effective October 2001.

Chapter 133, P.L. 2001 increased the retirement benefits under service, deferred, and early retirement by changing the formula from 1/60 to 1/55 of final compensation for each year of service. This legislation also increased the retirement benefit for veteran members with 35 or more years of service and reduced the age qualification from 60 to 55. Existing retirees and beneficiaries received a comparable percentage increase in their retirement allowances. This benefit enhancement was effective with the November 1, 2001 benefit payments.

Chapter 259, P.L. 2001 amended the PERS statutes and created special retirement benefits for members employed as workers' compensation judges. PERS members entitled to the new benefits are the Chief Judge, the administrative supervisory judges, the supervisory judges, and the judges of compensation of the Division of Workers' Compensation of the Department of Labor. Those in eligible titles would receive retirement benefits comparable to those provided to members of the Judicial Retirement System. The effective date of this legislation was December 6, 2001.

Chapter 366, P.L. 2001 provided enhanced pension benefits to selected individuals with County Prosecutor Offices and in the Division of Criminal Justice.

Significant Legislation:

P.L. 2003, effective July 14, 2003, provided employees of local employers with additional retirement benefits through early retirement incentive programs: Chapter 127 for a public agency other than State agencies under PERS; Chapter 128 for a county, a county college, or a municipality; and Chapter 129 for a local school board or educational services commission. They also permitted issuance of refunding bonds to fund benefits. Any employee who was eligible, or could have been if the employer elected, to participate in the State early retirement incentive program offered in 2002 pursuant to Chapter 23, P.L. 2002, is not eligible for the early retirement incentive benefits under this law.

Chapter 108, P.L. 2003, effective July 1, 2003, provided that the State Treasurer will reduce local employer PERS normal and accrued liability contributions to be a percentage of the amount certified annually by the PERS as follows: 20% for payments due in State fiscal year 2005; not more than 40% in fiscal year 2006; not more than 60% in fiscal year 2007; and not more than 80% in fiscal year 2008. According to the Appropriation Act of 2003**,** the State as well is paying pension obligations through a five-year phase-in.

Membership:

Membership in the System consisted of the following at June 30, 2004, the date of the most recent actuarial valuation:

	PENSION BENEFITS	POST-RETIREMENT MEDICAL BENEFITS
Retirees and beneficiaries receiving benefits currently and terminated employees entitled to benefits but not yet receiving them	119,190	19,419
Active members:		
Vested	140,529	10,246
Non-vested	162,433	80,669
Total active members	302,962	90,915
Total	422,152	110,334

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Measurement Focus and Basis of Accounting:

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. The System is accounted for using an economic resources measurement focus. The System that focuses on total economic resources employs the accrual basis of accounting, which recognizes increases and decreases in economic resources as soon as the underlying event or transaction occurs.

The accrual basis of accounting is used for measuring financial position and changes in fiduciary net assets of the System. Under this method, revenues are recorded in the accounting period in which they are earned and deductions are recorded at the time the liabilities are incurred. The financial statements of the System conform to the provisions of Governmental Accounting Standards Board (GASB) Statement No. 25, "Financial Reporting for Defined Benefit Plans and Note Disclosures for Defined Contributions Plans" and No. 26, "Financial Reporting for Post-employment Healthcare Plans Administered by Defined Benefit Pension Plans." Employer contributions are recognized when payable to the System. Benefits and refunds are recognized when payable in accordance with the terms of the System.

Adoption of Accounting Standard:

Effective July 1, 2004, the Division adopted Statement No. 40 of the Governmental Accounting Standards Board (GASB), "Deposit and Investment Risk Disclosures", an amendment of GASB Statement No. 3.

Valuation of Investments:

Investments are reported at fair value as follows:

- U.S. Government and Agency, Foreign and Corporate obligations – prices quoted by a major dealer in such securities.
- Common Stock and Equity Funds, Foreign Equity Securities, Forward Foreign Exchange Contracts – closing prices as reported on the primary market or exchange on which they trade.
- Money Market Instruments – amortized cost which approximates fair value.

- Cash Management Fund – closing bid price on the last day of trading during the period as determined by the Transfer Agent.

Investment Transactions:

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

Unit Transactions:

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

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

Securities Lending:

Common Funds A, B and D and several of the direct pension plan portfolios participate in securities lending programs with their custodian banks, whereby securities are loaned to brokers and, in return, the pension funds have rights to the collateral received. All of the securities held in Common Funds A, B and D are eligible for the securities lending program. Collateral received may consist of cash, letters of credit, or government securities having a market value equal to or exceeding 102% (U.S. dollar denominated) or 105% (non-U.S. dollar denominated) of the value of the loaned securities at the time the loan is made. For Common Funds A and B, in the event that the market value of the collateral falls below 101% of the market value of all the outstanding loaned securities, additional collateral shall be transferred by the borrower to the respective funds no later than the close of the next business day so that the market value of such additional collateral, when added to the market value of the other collateral, shall equal 102% of the market value of the loaned securities. For Common Fund D, in the event that the market value of the collateral falls below the collateral requirement of either 102% or 105% of the market value of the outstanding loaned securities, additional collateral shall be transferred in an amount that will increase the aggregate of the borrower's collateral to meet the collateral requirements. As of June 30, 2005, the Common Funds have no aggregate credit risk exposure to brokers because the collateral amount held by the Common Funds exceeded the market value of the securities on loan.

The contracts with the Common Funds' custodian banks require them to indemnify the Common Funds if the brokers fail to return the securities or fail to pay the Common Funds for income distributions by the securities' issuers while the securities are on loan. The securities loans can be terminated by notification by either the broker or the Common Funds. The term to maturity of the securities loans is generally matched with the term to maturity of the investment of the cash collateral.

Derivatives:

The Common Funds' international managers utilize forward foreign currency contracts, a derivative security, as a means to hedge against the currency risk in the Common Funds' foreign stock and fixed income portfolios. A derivative security is an investment whose payoff depends upon the value of other assets such as bond and stock prices, a market index, or commodity prices. Derivative transactions involve, to varying degrees, credit risk and market risk. Credit risk is the possibility that a loss may occur because a party to a transaction fails to perform according to terms. Market risk is the possibility that a change in market prices or currency rates will cause the value of a financial instrument to decrease or become more costly to settle.

Forward foreign currency contracts are agreements to buy or sell a specific amount of a foreign currency at a specified delivery or maturity date for an agreed upon price. Forward foreign currency contracts are used to hedge against the currency risk in the Common Funds' foreign stock and fixed income portfolios.

The fair value of foreign forward currency contracts outstanding as of June 30, 2005 is as follows:

		Amount
Forward currency receivable	$	745,577,063
Forward currency payable		745,525,163
Net unrealized gain		(51,900)

The net unrealized gain is included in investments at June 30, 2005.

The Common Funds utilize covered call options in an effort to add value to the portfolio (collect premiums). Covered call options are agreements that give the owner of the option the right, but not obligation, to buy a specific amount of an asset from the Common Funds for a specific price (called the strike price) on or before a specified expiration date. As the writer of financial options, the Common Funds receive a premium at the outset of the agreement and bear the risk of an unfavorable change in the price of the instrument underlying the option. The Common Funds have written call options on 215,400 shares with a fair value of $548,100 at June 30, 2005 which are reflected as a contra-asset to the fair value of the portfolio.

Members' Loans:

Members who have at least three years of service in the System may borrow up to 50% of their accumulated member contributions. Repayment of loan balances is deducted from payroll checks and bears an interest rate of 4%. Members who retire with an outstanding loan have the option of paying the loan in full prior to receiving any benefits or continuing their monthly loan payment schedule into retirement.

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

Administrative Expenses:

The System is administered by the State of New Jersey Division of Pensions and Benefits. Administrative expenses are paid by the System to the State of New Jersey, Department of the Treasury, and are included in the accompanying statement of changes in fiduciary net assets.

(3) INVESTMENTS

The System is invested in Common Pension Fund A, Common Pension Fund B, Common Pension Fund D, and other investments, including bonds and mortgage backed securities, which represent 32.08%, 33.57%, 32.18%, and 9.23%, respectively, of each investment total of the pension funds.

The pension funds investments as of June 30, 2005 are as follows:

	Amount
Domestic equities	$ 34,782,276,119
International equities	11,232,483,997
Domestic fixed income	16,521,446,786
International fixed income	2,201,826,936
Domestic floating rate securities	77,922,181
Police and Firemen's mortgages	896,706,544
Net forward foreign exchange contracts	51,900
	$ 65,712,714,463

New Jersey state statute provides for a State Investment Council (Council) and a Director. Investment authority is vested in the Director of the Division and the role of the Council is to formulate investment policies. The Council issues regulations which establish guidelines for permissible investments which include domestic and international equities, obligations of the U.S. Treasury, government agencies, corporations, finance companies and banks, international government and agency obligations, Canadian obligations, New Jersey State and Municipal general obligations, public authority revenue obligations, collateralized notes and mortgages, commercial paper, certificates of deposit, repurchase agreements, bankers acceptances, guaranteed income contracts and money market funds.

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

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 agencies such as Moody's Investors Service, Inc. (Moody's) or Standard & Poor's Corporation (S&P). Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. There are no restrictions in the amount that can be invested in United States treasury and government agency obligations. Council regulations require minimum credit ratings for certain categories of fixed income obligations and limit the amount that can be invested in any one issuer or issue as follows:

Category	Minimum Rating Moody's	Minimum Rating S&P	Limitation of Issuer's Outstanding Debt	Limitation of Issue	Other Limitations
Corporate obligations	Baa	BBB	25%	25%	—
U.S. finance company debt, bank debentures and NJ state & municipal obligations	A	A	10%	10%	—
Canadian obligations	A	A	10%	10%	Purchase cannot exceed $10 million
International government and agency obligations	Aa	AA	2%	10%	Not more than 1% of fund assets can be invested in any one issuer
Public Authority revenue obligations	A	A	—	10%	Not more than 2% of fund assets can be invested in any one public authority
Collateralized notes and mortgages	Baa	BBB	—	33.3%	Not more than 2% of fund assets can be invested in any one issuer
Commercial paper	P-1	A-1	—	—	—
Certificates of deposit and Banker's acceptances (rating applies to international)	Aa/P-1	—	—	—	Uncollateralized certificates of deposit and banker's acceptances cannot exceed 10% of issuer's primary capital
Guaranteed income contracts	P-1	—	—	—	A+ rating from A.M. Best for insurance companies
Money market funds	—	—	—	—	Not more than 10% of fund assets can be invested in money market funds; limited to 5% of shares or units outstanding

STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

Notes to Financial Statements, Continued

For securities exposed to credit risk in the fixed income portfolio, the following table discloses aggregate market value, by major credit quality rating category at June 30, 2005:

(000's)	Moody's Rating			
	Aaa	Aa	A	Baa
United States Treasury Notes	$ 1,813,358	—	—	—
United States Treasury TIPS	598,125	—	—	—
United States Treasury Bonds	2,193,224	—	—	—
United States Treasury Strips	42,326	—	—	—
Title XI Merchant Marine Notes	3,956	—	—	—
Federal Agricultural Mortgage Corp. Notes	—	101,698	—	—
Federal Farm Credit Bank Bonds	102,225	—	—	—
Federal Home Loan Bank Bonds	521,527	—	—	—
Federal Home Loan Bank Discounted Notes	4,244	—	—	—
Federal Home Loan Mortgage Corp. Notes	265,077	26,953	—	—
Federal National Mortgage Association Notes	698,324	26,078	—	—
Resolution Funding Corp. Obligations	7,337	—	—	—
Floating Rate Notes	25,026	19,983	9,999	22,914
Corporate Obligations	645,239	594,643	2,722,186	1,310,398
Real Estate Investment Trust Obligations	—	—	—	99,301
Finance Company Debt	285,528	963,800	757,113	132,094
Supranational Obligations	122,496	—	—	—
International Bonds and Notes	420,419	—	—	—
Foreign Government Obligations	1,293,765	283,284	58,319	—
Remic/FHLMC	638,865	—	—	—
Remic/ FNMA	73,982	—	—	—
Remic/ GNMA	17,993	—	—	—
GNMA Mortgage Backed Certificates	112,091	—	—	—
FHLM Mortgage Backed Certificates	774,802	—	—	—
FNMA Mortgage Backed Certificates	645,810	—	—	—
Asset Backed Obligations	252,973	—	—	—
Private Export Obligations	34,127	—	—	—
Exchange Traded Securities	—	—	56,050	—
	$ 11,592,839	2,016,439	3,603,667	1,564,707

The table does not include certain investments which do not have a Moody's rating which include foreign government obligations totaling $18,842,884 with an S&P rating of AAA and convertible zero coupon bonds totaling $4,701,462 with an S&P rating of BBB. The Police and Firemen's Mortgages and the Cash Management Fund are unrated.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Commercial paper must mature within 270 days. Certificates of deposits and bankers acceptances are limited to a term of one year or less. The maturity of repurchase agreements shall not exceed 15 days. The investment in a guaranteed income contract is limited to a term of 10 years or less.

The following table summarizes the maturities of the fixed income portfolio at June 30, 2005:

(000's)			Maturities in Years			
Fixed Income Investment Type		Total Market Value	Less than 1	1-5	6-10	More than 10
United States Treasury Notes	$	1,813,358	111,930	795,152	906,276	—
United States Treasury Tips		598,125	—	—	517,312	80,813
United States Treasury Bonds		2,193,224	—	—	—	2,193,224
United States Treasury Strips		42,326	—	—	—	42,326
Title XI Merchant Marine Notes		3,956	—	—	—	3,956
Federal Agricultural Mortgage Corp. Notes		101,698	—	101,698	—	—
Federal Farm Credit Bank Bonds		102,225	49,578	52,647	—	—
Federal Home Loan Bank Bonds		521,527	49,610	471,917	—	—
Federal Home Loan Bank Discounted Notes		4,244	—	—	—	4,244
Federal Home Loan Mortgage Corp. Notes		292,030	—	174,938	117,092	—
Federal National Mortgage Association Notes		724,402	226,752	315,835	26,078	155,737
Resolution Funding Corp. Obligations		7,337	—	—	—	7,337
Floating Rate Notes		77,922	—	67,923	9,999	—
Corporate Obligations		5,272,466	492,077	1,632,208	1,509,472	1,638,709
Real Estate Investment Trust Obligations		99,301	—	19,836	79,465	—
Finance Company Debt		2,138,535	405,222	1,021,737	576,593	134,983
Supranational Obligations		122,496	25,227	—	—	97,269
International Bonds and Notes		420,419	54,846	300,229	19,865	45,479
Foreign Government Obligations		1,654,211	45,065	632,606	567,437	409,103
Remic/FHLMC		638,865	—	9,872	20,959	608,034
Remic/ FNMA		73,982	196	4,734	18,358	50,694
Remic/ GNMA		17,993	—	—	—	17,993
Police and Firemen's Mortgages		896,707	—	—	—	896,707
GNMA Mortgage Backed Certificates		112,091	41	1,479	—	110,571
FHLM Mortgage Backed Certificates		774,802	—	265	4,999	769,538
FNMA Mortgage Backed Certificates		645,810	—	7,343	29,116	609,351
Asset Backed Obligations		252,973	—	153,828	34,509	64,636
Private Export Obligations		34,127	—	12,289	21,838	—
Convertible Zero Coupon Bonds		4,701	—	—	4,701	—
	$	19,641,853	1,460,544	5,776,536	4,464,069	7,940,704

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The Common Funds invest in global markets. The Common Funds can invest in securities of companies incorporated in one of thirty countries approved by the Council. The market value of international preferred and common stocks and issues convertible into common stocks, when combined with the market value of international government and agency obligations, cannot exceed 22 percent of the market value of forward contracts totaling approximately $650 million at June 30, 2005. At June 30, 2005, the Common Funds had the following foreign currency exposure (expressed in U.S. dollars):

Currency		Total Market Value	Equities	Foreign Government Obligations
Australian dollar	$	401,418,580	272,431,668	128,986,912
Canadian dollar		587,693,580	502,887,128	84,806,452
Danish krone		148,396,127	148,396,127	—
Euro		4,447,969,733	3,646,096,193	801,873,540
Hong Kong dollar		167,808,826	167,808,826	—
Japanese yen		2,218,395,101	2,213,693,639	4,701,462
Mexican peso		40,732,398	40,732,398	—
New Zealand dollar		72,765,425	32,928,859	39,836,566
Norwegian krone		198,279,321	91,284,080	106,995,241
Pound sterling		2,181,964,380	1,957,488,690	224,475,690
Singapore dollar		75,677,979	75,677,979	—
South Korean won		141,633,342	141,633,342	—
Swedish krona		735,391,335	628,135,901	107,255,434
Swiss franc		1,017,523,657	1,017,523,657	—
	$	12,435,649,784	10,936,718,487	1,498,931,297

The Cash Management Fund is unrated. The Cash Management Fund is not evidenced by securities that exist in physical or book entry form held by the pension funds.

Net appreciation or depreciation in fair value of investments includes net realized gains and the change in net unrealized gains and losses on investments for the fiscal year ended June 30, 2005. The net realized gain from investment transactions amounted to $2,729,925,208 and the net increase in unrealized gains on investments amounted to $935,762,205 for the year ended June 30, 2005.

(4) SECURITIES LENDING COLLATERAL

The System's share in the securities lending program is 32.6% of the total market value of the collateral at June 30, 2005.

The securities lending collateral is subject to various risks. Among these risks are credit risk, concentration of credit risk and interest rate risk. Agreements with the lending agents require minimum credit ratings for certain categories of fixed income obligations and limit the amount that can be invested in any one issuer or issue as follows:

Category	Minimum Rating Moody's	Minimum Rating S&P	Limitation of Issuer's Outstanding Debt	Limitation of Issue	Other Limitations
Corporate obligations	A3	A-	25%	25%	—
U.S. finance company debt and bank debentures	A2	A	10%	10%	—
Collateralized notes and mortgages	Aaa	AAA	—	33.3%	Limited to not more than 10% of the assets of the collateral portfolio
Commercial paper	P-1	A-1	—	—	—
Certificates of deposit/ Banker's acceptances	Aa3/P-1	—	—	—	Uncollateralized certificates of deposit and banker's acceptances' cannot exceed 10% of issuer's primary capital
Guaranteed income contracts	P-1	—	—	—	Limited to 5% of the assets of the collateral portfolio; A+ rating from A.M. Best for insurance companies
Money market funds	—	—	—	—	Limited to 10% of the assets of the collateral portfolio; limited to approved money market funds

Maturities of corporate obligations, U.S. finance company debt, bank debentures, collateralized notes and mortgages and guaranteed income contracts must be less than 25 months. Commercial paper maturities cannot exceed 270 days. Repurchase agreement maturities cannot exceed 15 days. Certificates of deposit and banker's acceptances must mature in one year or less.

The collateral for repurchase agreements is limited to obligations of the U.S. Government or certain U.S. Government agencies.

Total exposure to any individual issuer is limited, except for U.S. Treasury and Government Agency Obligations. For money market funds, the total amount of shares or units purchased or acquired of any money market fund shall not exceed five percent of the shares or units outstanding of said money market fund. For Collateralized Notes and Mortgages, not more than two percent of the assets of the collateral portfolio shall be invested in the obligations of any one issuer. For Guaranteed Income Contracts, the total investment in any one issuer shall be limited to 2.5% of the collateral portfolio. The Division sets individual issuer limits for Commercial Paper and Certificate of Deposits. For Corporate Obligations, U.S. Finance Company Debt, Bank Debentures and Bankers Acceptances, exposure to any one issuer shall be limited to the following percentages of the collateral portfolio in accordance with the issuer's rating from Moody's: Aaa (4%), Aa (3%) and A (2%).

For securities exposed to credit risk in the collateral portfolio, the following table discloses aggregate market value, by major credit quality rating category at June 30, 2005:

(000's)		**Moody's Rating**				**S&P Rating (1)**
		Aaa	**Aa**	**A**	**P-1**	**A**
Corporate Obligations	$	440,053	3,748,203	2,052,074	—	—
Commercial Paper		—	—	—	2,373,183	—
Certificates of Deposit		—	1,357,406	—	—	97,900
Repurchase Agreements		—	—	—	—	—
Guaranteed Investment Contracts		—	150,000	200,000	—	—
Money Market Funds		103,815	—	—	—	—
Collateralized Notes		10,000	—	—	—	—
	$	553,868	5,255,609	2,252,074	2,373,183	97,900

(1) Moody's rating not available

In addition, the collateral portfolio includes money market funds with a current market value of $1,074,355 and repurchase agreements with a current market value of $1,588,984,270 at June 30, 2005 which are not rated.

The following table summarizes the maturities of the collateral portfolio at June 30, 2005:

(000's)		**Total Market Value**	**Maturities: Less than one year**	**Maturities: One year to 25 months**
Corporate Obligations	$	6,240,331	4,753,161	1,487,170
Commercial Paper		2,373,183	2,373,183	—
Certificates of Deposit		1,455,306	1,455,306	—
Repurchase Agreements		1,588,984	1,588,984	—
Guaranteed Investment Contracts		350,000	250,000	100,000
Money Market Funds		104,889	104,889	—
Collateralized Notes		10,000	10,000	—
	$	12,122,693	10,535,523	1,587,170

As of June 30, 2005, the Common Funds had received cash collateral of $12,166,888,240 for outstanding loaned investment securities having market values of $11,780,098,612. In addition, as of June 30, 2005, the Common Funds loaned investment securities having market values of $38,245,996, against which it had received non-cash collateral with a current value of $39,118,460, which is not reflected in the accompanying financial statements.

(5) CONTRIBUTIONS

The contribution policy is set by N.J.S.A. 43:15A and requires contributions by active members and contributing employers. Plan member and employer contributions may be amended by State of New Jersey legislation. Members contribute at a uniform rate. The full normal employee contribution rate is 5% of base salary. However, as a result of special legislation (Chapter 415, P.L. 1999), the employee rate was reduced to 3% of base salary effective January 1, 2000. The rate for State and local employees returned to the normal rate of 5% effective July 1, 2004 and January 1, 2005, respectively per statute since there are no longer surplus assets available in the System. On the other hand, the rate for members who are eligible for the Prosecutors Part of the PERS (Chapter 366, P.L. 2001) remains unchanged at 7.5% of base salary. Employers are required to contribute at an actuarially determined rate. The annual employer contributions include funding for basic retirement allowances, cost-of-living adjustments, and noncontributory death benefits. The State of New Jersey's contribution also includes funding for the cost of medical premiums after retirement for qualified retirees. In accordance with Chapter 62, P.L. 1994, post-retirement medical benefits have been funded on a pay-as-you-go basis since 1994. Prior to 1994, medical benefits were funded on an actuarial basis. Beginning in 1996, the State has made an additional contribution to the Post-Retirement Medical Reserve Fund to ensure an increase in the fund balance of 1/2 of 1% of the salary of active state employees.

For fiscal year 2005, the 50% of available excess valuation assets could be utilized to offset normal contributions. Thereafter, a certain percentage of available excess valuation assets may be used as specified in the legislation. The State and local employers were not required to make a normal contribution to the System between the years 1997 and 2004. The normal contribution for basic pension benefits, noncontributory death benefits, and cost-of-living adjustments was funded by excess valuation assets in accordance with Chapter 115, P.L. 1997. This legislation provides for actuarially determined excess valuation assets to offset the required normal contributions of the State of New Jersey and the local participating employers.

The State made a contribution of $190.8 million for fiscal year 2005 post-retirement medical (PRM). Legislation passed in 2002 (Chapter 11, P.L. 2002) allowed the State to use net assets in PRM Fund to cover the required pay-as-you-go medical premiums.

To fund the benefit increases provided by Chapter 133, the legislation provided for the use of excess assets. A special benefit enhancement fund (BEF) was established from which the required normal contributions for the increased benefits will be charged. To fund the accrued liabilities incurred by the System, the actuarial value of assets for the valuation period ending June 30, 1999 was adjusted to reflect the full market value of assets.

The BEF will also provide funding for the benefit increases under Chapter 353, P.L. 2001. Actuarially determined excess valuation assets will cover the additional accrued liability incurred by the retirement system. No additional formula State contribution is required in fiscal year 2005; instead, that contribution will be covered by the BEF.

Chapter 108, P.L. 2003 provided that the State Treasurer will reduce local employer PERS normal and accrued liability contributions to be a percentage of the amount certified annually by the PERS as follows: 20% for payments due in State fiscal year 2005; not more than 40% in fiscal year 2006; not more than 60% in fiscal year 2007; and not more than 80% in fiscal year 2008. According to the Appropriation Act of 2003, the State as well is paying pension obligations through a five-year phase-in. In fiscal year 2005, the State paid 30% of the normal and accrued liability pension cost by using the BEF.

(6) FUNDS

This System maintains the following legally required funds:

Members' Annuity Savings and Accumulative Interest Fund ($7,273,813,479)

The Members' Annuity Savings Fund is credited with all contributions made by active members of the System. Interest earned on member contributions is credited to the Accumulated Interest Fund. The annual rate of interest on member contributions, as required by Chapter 62, P.L. 1994, is 8.75%.

Contingent Reserve Fund ($830,151,874)

The Contingent Reserve Fund is credited with the contributions of contributing employers other than post-retirement medical contributions. Interest earnings, after crediting the Accumulative Interest Fund, Retirement Reserve Fund and Special Reserve Fund, as required, are credited to this account. Additionally, payments for life insurance premiums are made from this Fund.

Retirement Reserve Fund ($14,764,795,737)

The Retirement Reserve Fund is the account from which retirement benefits other than life insurance premiums, contributory group insurance premiums, and post-retirement medical premiums, including cost-of-living benefits and medical benefits for certain retirees, are paid. Upon retirement of a member, accumulated contributions, together with accumulated interest, are transferred to the Retirement Reserve Fund from the Members' Annuity Savings and Accumulative Interest Fund. Any additional reserves needed for the retirement and cost-of-living benefits are transferred from the Contingent Reserve Fund. Annually, interest as determined by the State Treasurer (8.75% for fiscal years 2005) is credited to the Retirement Reserve Fund.

Special Reserve Fund ($197,407,522)

The Special Reserve Fund is the fund to which excess interest earnings and gains from sales and maturities of investments are transferred and against which any losses from the sales of securities are charged. The maximum limit on the accumulation of this account is 1% of the market value of the investments allocated to the System, excluding Cash Management Fund investments and bonds allocated to the Contributory Group Insurance Premium Fund which amounted to $209.96 million as of June 30, 2005. Amounts in excess of 1% are credited to the Contingent Reserve Fund.

Contributory Group Insurance Premium Fund ($211,220,174)

The Contributory Group Insurance Premium Fund represents the accumulation of member group insurance contributions in excess of premiums disbursed to the insurance carrier since the inception of the contributory death benefit program plus reserves held by the insurance carrier. Members are required by statute to participate in the contributory group insurance plan in the first year of membership and may cancel the contributory coverage thereafter. The current contribution rate for active members is 0.5 of 1% of salary, as defined.

Post-Retirement Medical Fund ($1,296,942)

The Post-Retirement Medical Fund is credited with employer contributions for post-retirement medical benefits, interest earnings on post-retirement medical reserves, and from which post-retirement medical premiums are paid.

Benefit Enhancement Reserve Fund ($637,127,887)

The Benefit Enhancement Reserve Fund is a special reserve fund from which the required normal contributions to provide benefit increases under Chapter 353, P.L. 2001 and Chapter 133, P.L. 2001 will be charged. The fund was established in 2002 and credited with excess assets equivalent to member contributions for fiscal years 2000 and 2001 by transferring reserves in the Contingent Reserve Fund to the Benefit Enhancement Fund. Additional transfers will be made, as required, to maintain a fund balance equal to the present value of expected additional normal contributions due to the increased benefits. The State will be required to make contributions to the Benefit Enhancement Fund on behalf of State and local employers if excess valuation assets are not available.

(7) INCOME TAX STATUS

Based on a 1986 declaration of the Attorney General of the State of New Jersey, the System is a qualified plan as described in Section 401(a) of the Internal Revenue Code.

Schedule 1

STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

Required Supplementary Information

Schedule of Funding Progress

ACTUARIAL VALUATION DATE	ACTUARIAL VALUE OF ASSETS (a)	ACTUARIAL ACCRUED LIABILITY (b)	UNFUNDED (OVERFUNDED) ACTUARIAL ACCRUED LIABILITY (b - a)	FUNDED RATIO (a / b)	COVERED PAYROLL (c)	UNFUNDED (OVERFUNDED) ACTUARIAL ACCRUED LIABILITY AS A PERCENTAGE OF COVERED PAYROLL ((b - a) / c)
State						
March 31, 1997	$6,987,217,172	$6,606,707,924	$(380,509,248)	105.8%	$2,714,991,457	(14.0%)
March 31, 1998	7,600,621,930	7,155,035,122	(445,586,808)	106.2%	2,805,791,909	(15.9%)
June 30, 1999	8,879,920,323	7,823,576,056	(1,056,344,267)	113.5%	2,928,470,790	(36.1%)
June 30, 2000	9,743,727,383	8,538,685,222	(1,205,042,161)	114.1%	3,094,280,664	(38.9%)
June 30, 2001	11,123,818,861	9,886,463,368	(1,237,355,493)	112.5%	3,288,383,788	(37.6%)
June 30, 2002	11,073,156,965	10,760,557,483	(312,599,482)	102.9%	3,511,151,199	(8.9%)
June 30, 2003	10,829,953,189	11,942,299,170	1,112,345,981	90.7%	3,576,118,300	31.1%
June 30, 2004	10,693,508,592	12,620,379,435	1,926,870,843	84.7%	3,751,765,096	51.4%
Local						
March 31, 1997	10,523,061,499	9,599,816,842	(923,244,657)	109.6%	4,407,751,955	(20.9%)
March 31, 1998	11,486,495,310	10,286,532,879	(1,199,962,431)	111.7%	4,513,357,772	(26.6%)
June 30, 1999	13,171,311,650	11,163,283,877	(2,008,027,773)	118.0%	4,655,241,261	(43.1%)
June 30, 2000	14,380,511,913	12,007,160,806	(2,373,351,107)	119.8%	4,910,962,708	(48.3%)
June 30, 2001	16,625,288,260	13,819,038,491	(2,806,249,769)	120.3%	5,240,338,738	(53.6%)
June 30, 2002	16,503,081,054	14,929,334,103	(1,573,746,951)	110.5%	5,534,322,805	(28.4%)
June 30, 2003	16,406,284,200	15,887,012,746	(519,271,454)	103.3%	5,811,726,702	(8.9%)
June 30, 2004	16,414,022,003	17,077,938,057	663,916,054	96.1%	6,140,413,756	10.8%

Schedule 1, Continued

STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

Required Supplementary Information, Continued

Schedule of Funding Progress - Additional Actuarial Information

Significant actuarial methods and assumptions used in the most recent June 30, 2004 actuarial valuation included the following:

Actuarial cost method	Projected unit credit
Asset valuation method	5 year average of market value
Amortization method	Level percent, closed
Remaining amortization period	37 years for UAAL balance
	7 years for asset method change

Actuarial assumptions:	
Interest rate	8.25%
Salary range	5.45%
Cost-of-living adjustments	1.80%

Annual covered payroll is an estimate based upon annualizing one quarter's actual payroll.

STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

Required Supplementary Information, Continued

Schedule of Employer Contributions

YEAR ENDED JUNE 30,	ANNUAL REQUIRED CONTRIBUTION	EMPLOYER CONTRIBUTIONS[1]	PERCENTAGE CONTRIBUTED
State			
1997	$134,878,582	$241,106,642[2]	178.8%
1998	78,833,287	—	0.0%
1999	86,945,810	—	0.0%
2000	103,033,425	—	0.0%
2001	85,078,620	—	0.0%
2002	88,911,187	—	0.0%
2003	44,636,619	—	0.0%
2004	50,365,892	526,505[3]	1.0%
2005	115,017,395	463,342[3]	0.4%
Local			
1997	142,672,255	67,476,771	47.3%
1998	84,639,988	19,034,673	22.5%
1999	111,886,040	19,599,153	17.5%
2000	112,800,127	20,541,177	18.2%
2001	88,717,727	21,670,774	24.4%
2002	77,254,063	16,174,534	20.9%
2003	—	16,987,033	N/A
2004	—	20,882,718	N/A
2005	29,425,853	56,916,883	193.4%

Notes to Schedule

(1) Excludes post-retirement medical contributions (State only) and contributions received from other State of New Jersey retirement systems for certain members who transferred their eligible prior service credit to the Public Employees' Retirement System. The local employer contributions from 1998 to 2004 consist of the required contributions under the early retirement incentive programs.

In accordance with Chapter 115, P.L. 1997, available excess valuation assets were used to fund, in full or in part, the required contributions of the State and local employers.

(2) For the year ended June 30, 1997, the state portion of employer contributions exceeded the annual required contributions as a result of legislation that was enacted (Chapter 114, P.L. 1997), authorizing the New Jersey Economic Development Authority to issue bonds, notes or other obligations for the purpose of financing, in full or in part, the State of New Jersey's portion of the unfunded accrued liability under the State of New Jersey retirement systems.

(3) The statutory required contributions which were reduced in anticipation of the provisions of the Appropriation Act of 2003 will be covered by available excess assets in the Benefit Enhancement Fund. The $526,505 and $463,342 contribution shown represent the fund transfer from the Second Injury Fund in accordance with Chapter 259, P.L. 2001.

Schedule 3

STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

Schedule of Changes in Fiduciary Net Assets by Fund

Year ended June 30, 2005

	MEMBERS' ANNUITY SAVINGS AND ACCUMULATIVE INTEREST FUND	CONTINGENT RESERVE FUND	RETIREMENT RESERVE FUND	SPECIAL RESERVE FUND	CONTRIBUTORY GROUP INSURANCE PREMIUM FUND	POST-RETIREMENT MEDICAL FUND	BENEFIT ENHANCEMENT FUND	TOTAL
Additions:								
Contributions:								
Members	$ 484,808,707	—	—	—	49,053,646	—	—	533,862,353
Employers	—	219,912,516	—	—	—	190,824,454	—	410,736,970
Total contributions	484,808,707	219,912,516	—	—	49,053,646	190,824,454	—	944,599,323
Distribution of net investment income	549,241,803	104,978,747	1,218,055,423	—	5,185,398	97,706	51,263,164	1,928,822,241
Total additions	1,034,050,510	324,891,263	1,218,055,423	—	54,239,044	190,922,160	51,263,164	2,873,421,564
Deductions:								
Benefit payments	—	66,044,616	1,605,184,590	—	37,888,676	190,753,469	—	1,899,871,351
Refunds of contributions	59,973,889	5,512,998	—	—	—	—	—	65,486,887
Administrative expenses	—	25,602,118	—	—	—	—	—	25,602,118
Total deductions	59,973,889	97,159,732	1,605,184,590	—	37,888,676	190,753,469	—	1,990,960,356
Net increase (decrease) before transfers among reserves	974,076,621	227,731,531	(387,129,167)	—	16,350,368	168,691	51,263,164	882,461,208
Transfers among reserves:								
Retirements	(395,216,783)	(855,914,917)	1,251,131,700	—	—	—	—	—
Other	5,035,907	63,721,713	13,466,356	(19,613,988)	—	—	(62,609,988)	—
Net increase (decrease)	583,895,745	(564,461,673)	877,468,889	(19,613,988)	16,350,368	168,691	(11,346,824)	882,461,208
Net assets held in trust for pension and post-retirement medical benefits:								
Beginning of year	6,689,917,734	1,394,613,547	13,887,326,848	217,021,510	194,869,806	1,128,251	648,474,711	23,033,352,407
End of year	$ 7,273,813,479	830,151,874	14,764,795,737	197,407,522	211,220,174	1,296,942	637,127,887	23,915,813,615

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