

Comprehensive Annual Financial Report  
State Retirement and Pension System  
of Maryland



A Pension Trust Fund of the State of Maryland

For the Year Ended June 30, 2006

*Prepared by:*

State Retirement Agency of Maryland  
120 East Baltimore Street  
Baltimore, Maryland 21202

INTRODUCTORY SECTION:	
Letter of Transmittal .....	4
Message from the Board .....	7
Board of Trustees .....	8
Public Advisors to the Investment Committee .....	9
Organizational Chart .....	10
Professional Services .....	11
Certificate of Achievement .....	12
FINANCIAL SECTION:	
Independent Auditor's Report .....	14
Management's Discussion and Analysis .....	15
Financial Statements:	
Statements of Plan Net Assets .....	20
Statements of Changes in Plan Net Assets .....	21
Notes to the Financial Statements .....	22
Required Supplementary Information:	
Schedule of Funding Progress .....	35
Schedule of Contributions from Employers and Other Contributing Entity .....	35
Notes to the Required Supplementary Information .....	36
Other Supplementary Information:	
Schedule of Fund Balances .....	38
Schedule of Administrative Expenses .....	39
Schedule of Investment Expenses .....	39
Schedule of Plan Net Assets by System .....	40
Schedule of Changes in Plan Net Assets by System .....	42
INVESTMENT SECTION:	
Chief Investment Officer's Report .....	46
Investment Portfolios by Manager .....	52
Investment Portfolio Summary .....	53
Investment Portfolio Allocation .....	54
Fixed Income Distribution by Type .....	54
Equity Distribution by Type .....	55
Real Estate Distribution by Type .....	55
Comparative Investment Returns:	
Domestic Equity .....	56
Private Equity .....	56
International Equity .....	57
Real Estate .....	57
Fixed Income .....	58
Ten-Year History of Time-Weighted Annual Returns .....	59
Ten-Year Growth of Investment Portfolio .....	59
Largest 25 Holdings .....	60
Domestic and International Equity Commissions to Brokers .....	61

ACTUARIAL SECTION:

Independent Actuary's Certification Letter .....	64
Board Summary .....	65
Actuarial Methods and Assumptions .....	68
Accounting Statement Information .....	69
Summary of Unfunded Actuarial Liabilities/Solvency Test .....	70
Summary of Retirees and Beneficiaries Added to and Removed from Rolls .....	70
Statement of Changes in Total Actuarial Present Value of All Accrued Benefits .....	71
Summaries of Principal Results .....	72
Schedule of Active Membership Valuation Data by Plan .....	79

STATISTICAL SECTION:

Schedule of Retired Members by Type of Retirement and Option Selected .....	84
Schedule of Benefit Expense by Type .....	84
Summary of Membership Data by Plan .....	86
Ten-Year History of Membership by Plan .....	88
Total System Membership .....	88
Membership in Teachers' Plans .....	88
Membership in Employees' Plans .....	88
Ten-Year History of Retirees and Beneficiaries by Plan .....	89
Total System Retirees and Beneficiaries .....	89
Ten-Year History of Changes in Fund Balance .....	90
Ten-Year History of Employer Contribution Rates by Plan .....	90
Ten-Year History of Revenues by Source and Expenses by Type .....	91
Employer Contributions Received .....	92
Ten-Year History of Funding Progress .....	92
Ten-Year History of Revenues vs. Expenses .....	93
Summary of Principal Participating Employers .....	93
Governmental Units Participating in the Systems .....	94
Withdrawn Governmental Units .....	94

PLAN SUMMARY SECTION:

Teachers' Retirement System .....	96
Teachers' Pension System .....	98
Employees' Retirement System .....	100
Employees' Pension System .....	102
Judges' Retirement System .....	104
State Police Retirement System .....	106
Law Enforcement Officers' Pension System .....	108
Local Fire and Police System .....	110



STATE RETIREMENT  
and PENSION SYSTEM  
of MARYLAND

STATE RETIREMENT AGENCY  
120 East Baltimore Street  
Baltimore, MD 21202  
Tel: 410-625-5555  
1-800-492-5909  
TTD/TTY 410-625-5535  
www.sra.state.md.us

R. Dean Kenderdine  
*Interim Executive Director  
Secretary To The Board  
Board Of Trustees*

## LETTER OF TRANSMITTAL

December 15, 2006

Honorable Chairman & Members of the Board of Trustees:

We are pleased to submit the Comprehensive Annual Financial Report for the State Retirement and Pension System of Maryland (the "System") for the fiscal year ended June 30, 2006. We believe this report fairly reflects the results achieved during 2006.

The system is responsible for properly administering all retirement allowances and other benefits. At the same time, it strives to keep employer contribution rates as reasonable as possible by maximizing investment returns while maintaining an acceptable level of risk. Members covered by the plans include State employees, teachers, law enforcement officers, legislators, judges, as well as local government employees and fire fighters whose employers have elected to participate in the System.

Seventy-nine years ago, the first statewide retirement plan in Maryland (the Teachers' Retirement System) was established. Fourteen years later, in 1941, the Employees' Retirement System was established. The System now consists of 10 plans, providing monthly allowances to more than 103,000 retirees and beneficiaries, and is an essential element of the future financial security for over 191,000 active participating members. Descriptions of the membership requirements and benefits provided by each plan administered by the System are included in the Plan Summary Section starting on page 96.

This Comprehensive Annual Financial Report contains six sections. The Introductory Section includes this letter of transmittal, along with information about the administrative structure of the System. The Financial, Actuarial and Investment Sections provide a comprehensive review of the System's financial position, the results of its operations and its funded status. Viewed separately, each of these three sections provides information about a different aspect of the System's long-standing record of stewardship and financial stability. In this regard, the Financial Section contains the report from the System's independent auditor, the combined financial statements and supplementary financial data. The Actuarial Section contains the independent actuary's certification, as well as the results of the System's annual actuarial valuation. The Investment Section includes a report highlighting the past year's performance in addition to various summary level portfolio composition and performance data. The Plan Summary and Statistical Sections provide detailed descriptions of the various plans' provisions and the demographic composition of the membership segments affected by each plan.

In addition to this Letter of Transmittal, additional narrative, overview, and analysis can be found in Management's Discussion and Analysis found on pages 15 through 19 of this annual report.

### **ECONOMIC ENVIRONMENT**

The System continued to experience strong investment gains during the fiscal year. Fund investments returned 10.4% in fiscal year 2006 which surpassed the return of 9.5% during fiscal 2005 and continued to remain above the System's actuarially determined target investment return of 7.75%. The actuarially determined target investment return of 7.75% is a long-term target and, as such, deviations from this target can be expected, both positive and negative, from year to year. Because returns are smoothed over a 5 year period for actuarial valuation purposes, coupled with benefit enhancements enacted in 2006, the System experienced a decrease in its funded ratio from 88.21% to 82.78%. The System remains financially strong and on schedule with regard to its long-term funding goals.

## MAJOR ISSUES AND INITIATIVES

The Board continues to be deeply concerned with the methodology used to calculate annual contributions to the trust fund and remains committed to its recommendation to change this funding method. During fiscal year 2005, the Board and staff spent a considerable amount of time thoroughly reviewing the current methodology, known as the Corridor Method, and the impact that this methodology is having on the System. Under the corridor method, contribution rates for the two largest systems, the employees' and teachers' systems, are fixed from year to year as long as the funded status for these systems remains in a "corridor" of 90% to 110%. The Board's review concluded that this methodology, at statute, should be replaced immediately with the actuarial contribution rate.

In the investments area, the System continued its focus on building a compliance framework to oversee external asset managers and implementing asset allocation changes. The enhancements that have been made in the areas of compliance and oversight are significant. With the help of the System's master custodian, State Street Bank and Trust Company, the Investment Division has developed a software tool that permits staff to independently assess equity and fixed income managers' compliance with their investment guidelines.

In the benefits administration area, the Agency continued working with the legislature to simplify existing pension law and document internal procedures and calculations. These initiatives facilitate implementation of information technology enhancements undertaken by the Agency. Accordingly, the Agency has begun development of the new Maryland Pension Administration System (MPAS) project. Project goals are to implement new agile technology architecture for the System.

## FINANCIAL INFORMATION

System management has committed the resources necessary to maintain an internal control structure which provides reasonable assurance that assets are adequately safeguarded and the financial records are consistently and accurately maintained. Accordingly, we are confident that the financial statements, supporting schedules and statistical tables included in this report fairly present the System's financial condition and the results of its operations in all material respects.

## ACCOUNTING SYSTEM AND REPORTS

The System reports its transactions on the accrual basis of accounting. Under this method, revenues are reported in the accounting period they are earned and become meas-

urable, and expenses are reported when the related liability is incurred. Investments are reported at fair value at fiscal year end. Investment purchases and sales are reported in the accounting period in which the related trade dates occur.

## REVENUES

The reserves necessary to finance retirement allowances and other benefits are accumulated through investment earnings and the collection of employer and member contributions. During fiscal year 2006, investment earnings were \$3.2 billion, while revenues from employer and member contributions were \$717 million and \$215 million, respectively. For fiscal year 2006, member contribution rates remained unchanged, while employer rates varied depending on the System.

## EXPENSES

The System's expenses consist of monthly retirement allowances, refunds of contributions to terminated and transferring members and withdrawing employers, and the administrative cost of System operations. As expected, payments to retirees, beneficiaries and transferring or withdrawing members and employers continued to be the System's primary disbursements during 2006, totaling \$1,845.9 million. Of this amount, the System disbursed \$1,829.5 million as retirement allowances to members and beneficiaries. The remaining \$16.4 million was paid to members and withdrawing employers as a result of employment terminations and withdraws from the System. Administrative and investment expenses are entirely funded through investment income. Of the \$163.4 million disbursed during fiscal year 2006 to manage the investment portfolio and to administer the System, \$144.8 million was paid for investment management, portfolio custody, and securities lending services while \$18.6 million was used to fund the System's administrative operations.

## FUNDING AND RESERVES

Funds, derived from the excess of revenues over expenses, are accumulated by the System in order to meet benefit obligations to both current and future retirees and beneficiaries. The Annotated Code of Maryland requires participating employers to make periodic contributions which, as a level percentage of payroll, will fund the employers' "normal costs" over the members' average active service period, and the System's accrued unfunded liability in separate annual layers. Specifically, the unfunded actuarial liability that existed at June 30, 2000 will continue to be amortized over the remaining 14-year period to June 30, 2020, whereas each subsequent annual liability layer will be amortized

over a 25-year period. The required employer contribution rates of each year are based on the actuary's annual valuation and recommendations.

At June 30, 2006, the System's actuarial accrued liability was \$43.2 billion. With the actuarial value of assets accumulated to pay the liability at \$35.8 billion, the System now stands at 82.78 % funded.

#### **INVESTMENTS**

We are pleased the System delivered a third consecutive year of solid returns posting a 10.4% return during fiscal year 2006 for plan participants and beneficiaries. Looking forward to fiscal year 2007, the Agency will continue to search for the optimal investment tradeoffs that will provide an attractive return expectation while maintaining acceptable levels of investment risk.

#### **PROFESSIONAL SERVICES**

The System contracts for the services of various independent consulting, investment advisory and financial professionals to assist the Board of Trustees in carrying out its fiduciary responsibility to efficiently and effectively manage the System. For example, actuarial services were provided by The Segal Company and independent financial statement audit services were provided by Abrams, Foster, Nole & Williams, PA. The System's asset custody and portfolio accounting services are provided by the State Street Bank & Trust Company under a multi-year, master custody arrangement. A complete listing of the System's professional consultants and external investment advisors is presented on page 11.

#### **CERTIFICATE OF ACHIEVEMENT FOR EXCELLENCE IN FINANCIAL REPORTING**

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the State Retirement and Pension System of Maryland for its comprehensive annual financial report for the fiscal year ended June 30, 2005. This was the seventeenth consecutive year (1989 through 2005) the State Retirement and Pension System of Maryland has achieved this prestigious award. In order to be awarded a Certificate of Achievement, a governmental unit must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current comprehensive annual financial report continues to meet the Certificate of Achievement Program's requirements, and we are submitting it to the GFOA to determine its eligibility for another certificate.

#### **ACKNOWLEDGEMENTS**

This annual report reflects the dedicated efforts of the System's staff under the steady direction of the Board of Trustees. We extend our sincere gratitude to each member of the Board of Trustees, the System's staff, the Board's advisors and the many people who worked so hard to make fiscal year 2006 a success.



R. Dean Kenderdine  
*Interim Executive Director &  
Secretary To The Board Of Trustees*



Vincent J. Marsiglia, CPA  
*Chief Financial Officer*



STATE RETIREMENT  
and PENSION SYSTEM  
of MARYLAND

STATE RETIREMENT AGENCY  
120 East Baltimore Street  
Baltimore, MD 21202  
Tel: 410-625-5555  
1-800-492-5909  
TTD/TTY 410-625-5535  
www.sra.state.md.us

R. Dean Kenderdine  
Interim Executive Director  
Secretary To The Board  
Board Of Trustees

December 15, 2006

Dear Members, Retirees and Beneficiaries:

For the third consecutive year the Maryland Retirement and Pension System posted strong investment returns. The total investment return for the System was 10.4% for the fiscal year ending June 30, 2006. Total fund assets increased from \$32.1 billion to \$34.4 billion, a \$2.3 billion increase. Over the last three fiscal years, assets under management have increased \$7.7 billion.

The fund saw continued growth in the equities and real estate asset classes over the year. Overall equity returns for the fund were 14.4%, with domestic equity returning 9.0% and international equity returning 28.2%. Returns for real estate were nearly 24%. The Board of Trustees continues to work diligently to ensure that the System's portfolio reflects market opportunities, while maintaining an appropriate level of risk.

We are also pleased to report that the System's long-term portfolio ranking among its peers is improving in the three, five and ten year categories, as determined by the Trust Universal Comparison Report (TUCS).

During the 2006 legislative session, the General Assembly approved benefit enhancement legislation that provided increased benefits to the members of the Teachers' and Employees' Pension Systems. The improvement coupled an increase in the annual benefit multiplier to 1.8% per year of service retroactive to July 1, 1998 with a phased-in increase in employee contribution rates to 5% over the next three years.

In June, the Board awarded the Maryland Pension Administration System Step One – Modernizing Legacy Technology (MPAS-1) contract to replace the Legacy Pension System (LPS). The new custom developed system will perform the same functions as the LPS, but with a modern technology architecture that can be more easily maintained and enhanced. This updated information technology will ensure that the Retirement Agency's business operations will be more efficient.

The Board announced that Major Morris Krome won reelection as the State Police Board of Trustees representative with 55.6% of the vote.

Lastly, our Executive Director, Thomas K. Lee, accepted a position with the New York State Teachers' Retirement System starting in September. On behalf of the entire Board and membership, we thank Tom for his leadership and vision and wish him much success in his new endeavor. The Board named R. Dean Kenderdine as Interim Executive Director while it conducts a search for a new executive director. Mr. Kenderdine is intimately familiar with the System and the Board has the utmost confidence in his abilities to run the operations of the Agency.

Your benefits continue to be safe and secure. As always, your support and participation are greatly appreciated.

Sincerely,

WILLIAM DONALD SCHAEFER  
Chairman

NANCY K. KOPP  
Vice Chairman

BOARD OF TRUSTEES



**WILLIAM DONALD SCHAEFER, *Chairman***  
**State Comptroller**

Ex Officio since January 25, 1999  
Member, Investment Committee



**NANCY K. KOPP, *Vice Chairman***  
**State Treasurer**

Ex Officio since February 14, 2002  
Vice Chairman, Investment Committee  
Member, Administrative Committee  
Member, Audit Committee  
Member, Corporate Governance Subcommittee  
Member, Real Estate Subcommittee



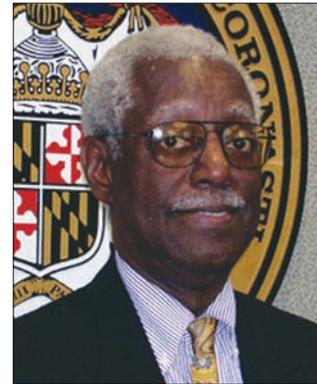
**WILLIAM D. BROWN**

August 1, 1997 – July 31, 2009  
Member, Administrative Committee  
Member, Investment Committee



**CECILIA JANUSZKIEWICZ**

Ex Officio since June 17, 2005  
Member, Investment Committee



**JOHN W. DOUGLASS**

May 18, 2004 – July 31, 2007  
Member, Administrative Committee  
Member, Audit Committee  
Member, Corporate Governance Subcommittee



**DAVID B. HAMILTON**

July 1, 2003 - June 30, 2007  
Member, Audit Committee  
Member, Administrative Committee



**JAMES M. HARKINS**

October 1, 2004 - June 30, 2010  
Chairman, Administrative Committee



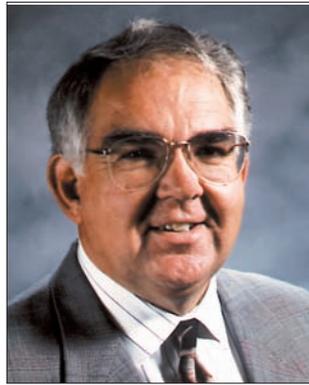
**F. PATRICK HUGHES**

July 1, 2003 - June 30, 2009  
Chairman, Audit Committee  
Member, Investment Committee  
Member, Real Estate Subcommittee

BOARD OF TRUSTEES



**MAJOR MORRIS L. KROME**  
August 1, 1998 – July 31, 2010  
Vice Chairman, Administrative Committee  
Member, Audit Committee  
Member, Investment Committee



**CARL D. LANCASTER**  
August 1, 1987 – July 31, 2007  
Chairman, Investment Committee  
Member, Corporate Governance Subcommittee  
Member, Real Estate Subcommittee



**A. MELISSA MOYE, PH.D.**  
July 1, 2003 - June 30, 2007  
Chairman, Corporate Governance  
Subcommittee  
Member, Investment Committee



**SHEILA HILL**  
October 19, 2004 – July 31, 2009  
Member, Administrative Committee  
Member, Investment Committee



**PATRICK A. O'SHEA**  
July 1, 2003 - June 30, 2007  
Member, Investment Committee  
Chairman, Real Estate Subcommittee

---

ADVISORS TO THE INVESTMENT COMMITTEE



**ROBERT W. SCHAEFER**



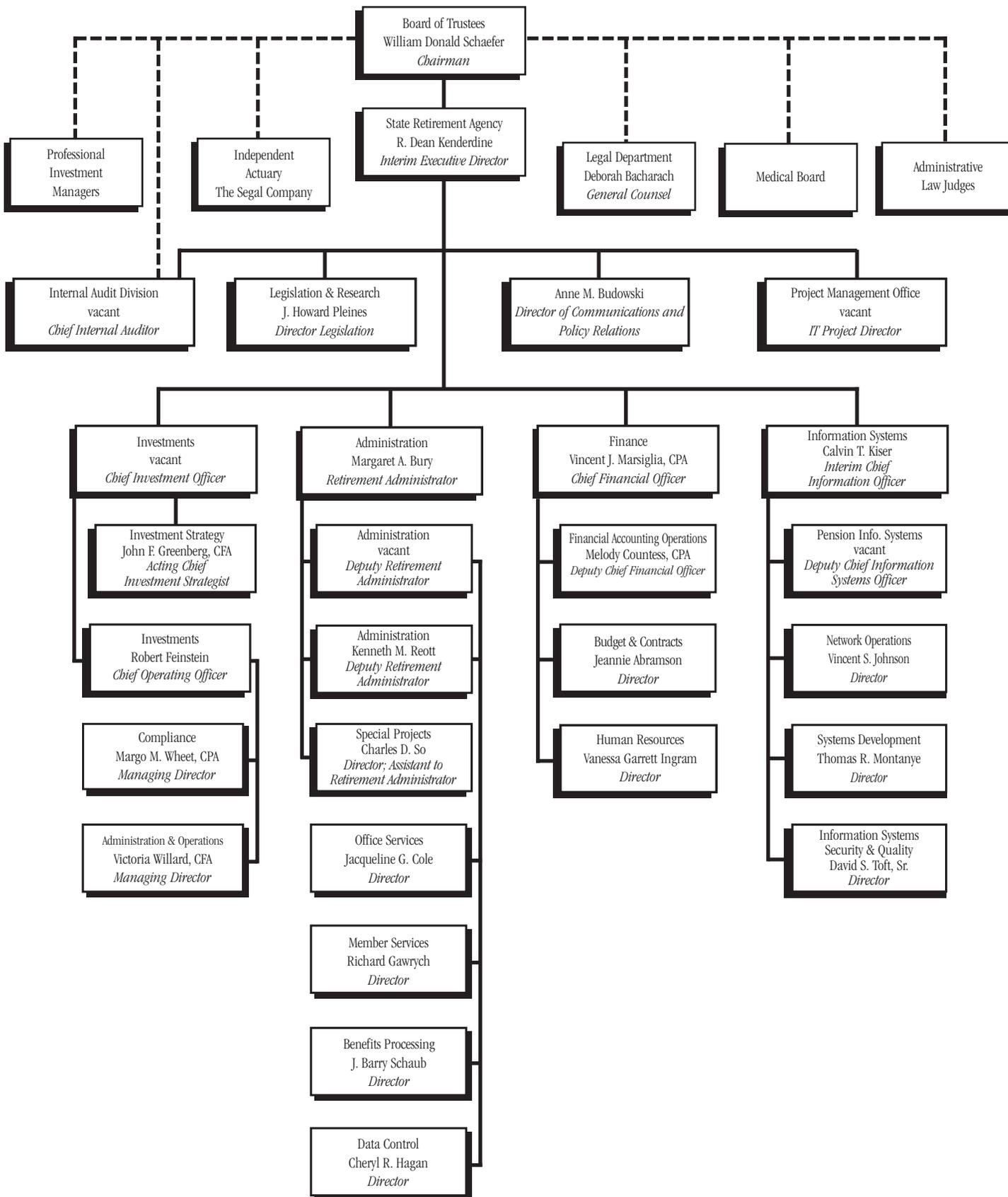
**WAYNE H. SHANER**



**BRIAN B. TOPPING**

ORGANIZATIONAL CHART

(November, 2006)



\*Additional information regarding investment professionals who provide services to the System can be found on pages 11, 52, and 61.

PROFESSIONAL SERVICES

**Asset & Income Verification Services**

Financial Control Systems, Inc.  
*Chadds Ford, Pennsylvania*

**Equity Investment Managers**

Acadian Asset Management  
*Boston, Massachusetts*

Artisan Partners Limited Partnership  
*San Francisco, California*

Brown Investment Advisory &  
Trust Company  
*Baltimore, Maryland*

Capital Guardian Trust Company  
*Washington, D.C.*

Dimensional Fund Advisors, Inc.  
*Santa Monica, California*

GlobeFlex Capital, LP  
*San Diego, California*

Legg Mason Capital Management, Inc.  
*Baltimore, Maryland*

Maryland Venture Capital Trust  
*Baltimore, Maryland*

Payden & Rygel  
*Los Angeles, California*

Relational Investors, LLC  
*San Diego, California*

Smith Breeden Associates, Inc.  
*Chapel Hill, North Carolina*

State Street Global Advisors  
*Boston, Massachusetts*

T. Rowe Price Associates, Inc.  
*Baltimore, Maryland*

Templeton Investment Counsel, Inc.  
*Fort Lauderdale, Florida*

Wellington Management Co., LLP  
*Boston, Massachusetts*

**Fixed Income Investment Managers**

Bridgewater Associates, Inc.  
*Westport, Connecticut*

Pacific Investment Management Company  
*Newport Beach, California*

Payden & Rygel  
*Los Angeles, California*

State Street Global Advisors  
*Boston, Massachusetts*

Western Asset Management  
*Pasadena, California*

**Global Custodial Bank &  
Security Lending**

State Street Bank and Trust Company  
*Boston, Massachusetts*

**Hearing Officers**

Office of Administrative Hearings  
*Baltimore, Maryland*

**Independent Actuary**

The Segal Company  
*Atlanta, Georgia*

**Independent Auditor**

Abrams, Foster, Nole & Williams, P.A.  
*Baltimore, Maryland*

**Independent Investment Consultants**

Altius Associates Limited  
*Richmond, Virginia*

Ennis Knupp & Associates  
*Chicago, Illinois*

Pension Consulting Alliance  
*Encino, California*

**Medical Board**

John J. Fahey, M.D.  
Norman Freeman, Jr. M.D.  
Arthur Hildreth, M.D.  
Bruce Z. Kohn, M.D.  
William B. Russell, M.D.  
Alfred Wiedmann, M.D.

**Operational Banking Services**

M & T Bank  
*Baltimore, Maryland*

The Harbor Bank of Maryland  
*Baltimore, Maryland*

**Private Equity**

Abbott Capital Management, LLC  
*New York, New York*

Adams Street Partners, LLC  
*Chicago, Illinois*

Advent International GPE V-D, LP  
*Boston, Massachusetts*

Alchemy Partners, LP  
*London, England*

Apax Europe VI-A, LP  
*London, England*

Audax Private Equity Fund II, LP  
*Boston, Massachusetts*

Bain Capital IX Fund, LP  
*Boston, Massachusetts*

BC European Capital VIII  
*Guernsey, Channel Islands*

Calvert Street Capital Partners III, LP  
*Baltimore, Maryland*

ECI 8, LP  
*London, England*

Frazier Healthcare V, LP  
*Seattle, Washington*

Great Hill Equity Partners III, LP  
*Boston, Massachusetts*

Hancock Park Capital III, LP  
*Los Angeles, California*

HarbourVest Partners, LLC  
*Boston, Massachusetts*

Hg Capital 5, LP  
*London, England*

Lion Capital Fund I, LP  
*London, England*

Natural Gas Partners VIII, LP  
*Greenwich, Connecticut*

RLH Investors II, LP  
*Los Angeles, California*

TA Associates Inc., LP  
*Boston, Massachusetts*

Vestar Capital Partners V, LP  
*New York, New York*

**Real Estate Investment Managers**

Chesapeake Maryland Limited Partnership  
*Baltimore, Maryland*

J.P. Morgan Investment Management, Inc.  
*New York, New York*

LaSalle Investment Management, Inc.  
*Baltimore, Maryland*

LaSalle Investment Management  
Securities, LP  
*Baltimore, Maryland*

Lubert-Adler Management, Inc.  
*Philadelphia, Pennsylvania*

Prudential Investment/CIGNA  
*Parsippany, New Jersey*

# Certificate of Achievement for Excellence in Financial Reporting

Presented to

## State Retirement and Pension System of Maryland

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

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



*Carla E. Perry*

President

*Jeffrey R. Emer*

Executive Director

## **TEACHERS' RETIREMENT & PENSION SYSTEMS**

The Teachers' Retirement System was established by the General Assembly in 1927 and is the oldest plan administered by the State Retirement and Pension System of Maryland. Equally important to the retirement security of state and local teachers is the Teachers' Pension System which was established in 1980. Today, the Teachers' Retirement and Pension Systems comprise state and local teachers of the public school systems, as well as certain employees of boards of education, public libraries and community colleges. Active membership involves over 100,000 participants. The combined systems provide survivor, disability and retirement benefits to plan members.

Abrams, Foster, Nole & Williams, P.A.

Certified Public Accountants

2 Hamill Road, Suite 272 N. Quadrangle  
Baltimore, MD 21210-1815  
(410) 433-6830 / Fax (410) 433-6871

Member: American Institute of Certified Public Accountants  
and Maryland Association of Certified Public Accountants

## INDEPENDENT PUBLIC ACCOUNTANTS' REPORT

Board of Trustees  
State Retirement and  
Pension System of Maryland

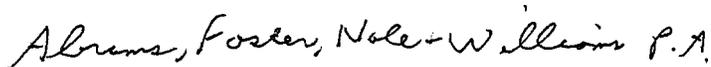
We have audited the accompanying basic financial statements of the State Retirement and Pension System of Maryland, which is a pension trust fund of the State of Maryland, as of and for the years ended June 30, 2006 and 2005, as listed in the table of contents. These financial statements are the responsibility of the 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

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

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

Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying required supplementary information and other supplementary information, as listed in the table of contents, are presented to provide supplementary information required by accounting standards generally accepted in the United States of America or for purposes of additional analysis and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.



Abrams, Foster, Nole & Williams, P.A.  
Certified Public Accountants

October 18, 2006  
Baltimore, Maryland

## MANAGEMENT'S DISCUSSION AND ANALYSIS

To help facilitate a better understanding of the State Retirement and Pension System of Maryland's (the "System") financial condition as of June 30, 2006, the results of its operations for the fiscal year then ended and the fiscal policies that govern its significant business operations, management has prepared this narrative analysis. This narrative is intended to supplement the System's audited financial statements and, as such should be read in conjunction with these statements, which are presented beginning on page 20.

### OVERVIEW OF THE FINANCIAL STATEMENTS

As required by generally accepted accounting principles, the System's basic financial statements comprise the comparative Statements of Plan Net Assets and Statements of Changes in Plan Net Assets, along with the related note disclosures. In addition, the System's financial statements include certain required supplementary information (e.g., schedules of funding progress, and employer contributions) as well as other supplementary schedules considered relevant to the financial statement user (e.g., schedules of fund balances, administrative and investment expenses, plan net assets and related changes by system). To better understand the relevance of the information presented in the System's financial statements and related notes and supplementary information, it is helpful to first consider what purpose each component is intended to serve.

The Statements of Plan Net Assets present a comparative, summary-level snapshot, as of a specific point in time (i.e., June 30th – the last day of the System's fiscal year), of the market value of the net assets available to pay future pension benefits to retirees and beneficiaries. To assist the reader in understanding the composition of the System's accumulated net assets the most significant components (e.g., cash and cash-equivalent securities, investments) are separately disclosed. In this regard, cash and cash equivalents represent that portion of the System's assets that, as of the end of the fiscal year, reside in the form of actual cash or short-term, highly liquid, investment securities. This amount gives an indication of the System's liquidity at fiscal year end. Conversely, the amounts shown as investments represent those funds invested in longer-term securities (e.g., stocks, bonds, real estate) held for the purpose of generating investment income. The sum of these assets, reduced by any liabilities owed by the System at fiscal year-end, represents the net assets held in trust to pay pension benefits.

By contrast, the Statements of Changes in Plan Net Assets are intended to show, on a comparative basis, the major categories of income earned (additions to plan net assets) and expenses incurred (deductions from plan net assets) by the System during the previous fiscal year. As such, the System's net income or loss accounts for the entire change in the net assets held in trust to pay pension benefits during the fiscal year as a result of System operations. As with the System's assets and liabilities, significant categories of income and expense, as reported on the Statements of Changes in Plan Net Assets, are separately disclosed to help clarify the major sources and uses of System resources.

Finally, the note disclosures are provided as an integral component of the financial statements to help explain in narrative form some of the more complex or less obvious elements of the statements. Further, the notes to the financial statements provide additional information (e.g., significant accounting policies, varying types of investment risk) that is essential for a comprehensive understanding of the System's financial condition and the results of its operations.

Beyond the basic financial statements, the System provides certain required schedules and related note disclosures that collectively demonstrate the System's annual progress toward funding its actuarial accrued liability (i.e., Schedule of Funding Progress) and discloses a ten-year history of required employer contributions (i.e., Schedule of Contributions from Employers and Other Contributing Entity). The importance of these schedules is best explained by reference to the previously discussed basic financial statements.

The Schedule of Funding Progress, while similar in scope to the Statements of Plan Net Assets in that it is primarily focused on reporting on the accumulation of assets, differs from such statements both in its method for valuing such assets and in its approach to explaining their relevance to the liability they are being accumulated to satisfy. In this regard, the Schedule of Funding Progress first takes a long-term, actuarial view toward valuing the System's investment portfolio, as opposed to the market value approach reflected on the Statements of Plan Net Assets. Specifically, the System's assets are valued (for funding purposes)

using a methodology that distributes investment gains and losses over a five-year period in order to minimize the effects of annual market volatility on employer contribution rates. The schedule then discloses the total actuarial accrued liability as projected to reflect the estimated effects of actuarial assumptions about future membership, service credit and covered payroll. Thus computed, the actuarial value of assets and the actuarial accrued liability are compared to disclose both the changes in the amount of unfunded actuarial liability, over a ten-year period, and the System's progress toward accumulating the necessary assets. This final piece, progress toward funding the actuarial accrued liability, is measured on the schedule in two significant ways. First is the funded ratio, which measures the System's ability to pay all projected benefits as they become due. Second is the unfunded liability, as a percentage of covered payroll, which measures the participating employers' capacity to pay all contributions required to fund the actuarial liability.

The Schedule of Contributions from Employers and Other Contributing Entity, much like the Schedule of Funding Progress, shares common characteristics with data disclosed in the basic financial statements. In this regard, both the Statements of Changes in Plan Net Assets and the Schedule of Contributions from Employers and Other Contributing Entity disclose the amount of contributions received from participating employers. However, the Schedule of Contributions from Employers and Other Contributing Entity differs from the Statements of Changes in Plan Net Assets in that the schedule's only focus is to disclose the contributions required to be made in accordance with the System's funding policy and the percentage of the required contributions actually made during the fiscal years presented.

The notes to the required supplementary information provide background information and explanatory detail to aid in understanding the required supplementary schedules. Finally, the other supplementary schedules, presented immediately after the required supplementary information, summarize the changes in fund balances, disclose major categories of operating and investment expenses and provide combining, plan-level detail related to asset, liability, income and expense amounts summarized in the basic financial statements.

#### ANALYSIS OF FINANCIAL POSITION AND RESULTS OF OPERATIONS

The System's overall funding objective is to accumulate sufficient assets over time to meet its long-term benefit obligations as they become due. Accordingly, collecting employer and member contributions as well as earning an adequate long-term rate of return on its investments are essential components of the System's plan for accumulating the funds needed to finance future retirement benefits. In this regard, fiscal year 2006 showed continued positive returns for both the financial markets and the economy as a whole.

#### **Fiscal Year 2006 compared to 2005**

Cash and cash equivalents and investments, at fair value, comprised 98.1% and 98.9% of the total assets of the Plan as of June 30, 2006 and 2005 respectively.

The schedule below indicates an increase of 6.9% in the managed assets of the System. Cash and cash equivalents increased by 51.8% primarily due to the reallocation of available cash by external investment managers. International stock increased as a result of an asset allocation change from domestic to global securities. The shift in international obligations and increase in mortgages and mortgage related securities is primarily due to a shift in the investment strategy of the external investment managers. The Alternative investments' strong performance along with additional investments during fiscal year 2006 drove the increase in this asset class.

A schedule of the System's investments and changes (by type) from fiscal year 2005 to 2006 is as follows (expressed in millions):

	June 30,		Change	
	2006	2005	Amount	%
Cash & cash equivalents	\$1,417.8	\$934.0	\$483.8	51.8%
U.S. Government obligations	1,666.6	1,761.4	(94.8)	-5.4%
Domestic corporate obligations	6,721.9	5,989.6	732.3	12.2%
International obligations	190.4	310.9	(120.5)	-38.8%
Domestic stocks	15,013.9	16,303.3	(1,289.4)	-7.9%
International stocks	7,020.2	4,982.9	2,037.3	40.9%
Mortgages & mortgage related securities	2,143.9	1,746.8	397.1	22.7%
Real estate	836.4	751.7	84.7	11.3%
Alternative investments	287.3	242.5	44.8	18.5%
<b>Total managed investments</b>	<u>35,298.4</u>	<u>33,023.1</u>	<u>2,275.3</u>	6.9%
Collateral for loaned securities	2,148.7	2,485.4	(336.7)	-13.5%
<b>Total investments and cash &amp; cash equivalents</b>	<u>37,447.1</u>	<u>35,508.5</u>	<u>1,938.6</u>	5.5%
Receivables	713.6	383.0	330.6	86.3%
<b>Total Assets</b>	<u>38,160.7</u>	<u>35,891.5</u>	<u>2,269.2</u>	6.3%
Liabilities	3,789.9	3,817.8	(27.9)	-0.7%
<b>Total net assets</b>	<u>\$34,370.8</u>	<u>\$32,073.7</u>	<u>\$2,297.1</u>	7.2%

As depicted in the schedule below, contributions collected by the System increased modestly during fiscal year 2006. Additionally, the system experienced an investment return of 10.4%, an increase from the prior year. The fund, as expected, continues to pay out more in benefits than it collects in contributions and that, coupled with an increase of \$132 million in benefits paid to retirees, negated a portion of the investment gain enjoyed by the System in fiscal year 2006.

A schedule of the System's additions to and deductions from plan net assets and related changes (by major category) from fiscal year 2005 to 2006 is as follows (expressed in millions):

	June 30,		Change	
	2006	2005	Amount	%
Employer contributions	\$285.3	\$239.8	\$45.5	19.0%
Member contributions	215.1	209.0	6.1	2.9%
Other & contribution interest	435.6	430.7	4.9	1.1%
Net investment income	<u>3,225.6</u>	<u>2,766.4</u>	<u>459.2</u>	16.6%
<b>Total additions</b>	<u>4,161.6</u>	<u>3,645.9</u>	<u>515.7</u>	14.1%
Benefit payments	1,829.5	1,697.4	132.1	7.8%
Refunds	16.4	19.1	(2.7)	-14.1%
Administrative expenses	18.6	22.4	(3.8)	-17.0%
<b>Total deductions</b>	<u>1,864.5</u>	<u>1,738.9</u>	<u>125.6</u>	7.2%
<b>Net increase (decrease) in plan net assets</b>	<u>\$2,297.1</u>	<u>\$1,907.0</u>	<u>\$390.1</u>	20.5%

**Fiscal Year 2005 compared to 2004**

Cash and cash equivalents decreased by 43.7% primarily due to the reallocation of available cash along with an allocation policy which targets maintaining a minimal cash balance. Increases in U.S. Government Obligations as well as Mortgage and mortgage related securities during fiscal year 2005 was primarily due to portfolio restructuring and modest performance increases. The Alternative investments' strong performance along with additional investments during fiscal year 2005 drove the increase in this asset class.

A schedule of the System's investments and changes (by type) from fiscal year 2004 to 2005 is as follows (*expressed in millions*):

	June 30,		Change	
	2005	2004	Amount	%
Cash & cash equivalents	\$934.0	\$1,660.2	\$(726.2)	-43.7%
U.S. Government obligations	1,761.4	843.1	918.3	108.9%
Domestic corporate obligations	5,989.6	5,915.1	74.5	1.3%
International obligations	310.9	186.0	124.9	67.2%
Domestic stocks	16,303.3	15,534.4	768.9	4.9%
International stocks	4,982.9	4,574.1	408.8	8.9%
Mortgages & mortgage related securities	1,746.8	1,255.1	491.7	39.2%
Real estate	751.7	780.2	(28.5)	-3.7%
Alternative investments	242.5	174.3	68.2	39.1%
<b>Total managed investments</b>	<u>33,023.1</u>	<u>30,922.5</u>	<u>2,100.6</u>	<u>6.8%</u>
Collateral for loaned securities	2,485.4	1,575.6	909.8	57.7%
<b>Total investments and cash &amp; cash equivalents</b>	<u>\$35,508.5</u>	<u>\$32,498.1</u>	<u>\$3,010.4</u>	<u>9.3%</u>

Contributions collected by the System increased modestly during fiscal year 2005. The system experienced a positive investment return of 9.5% after experiencing a strong recovery the prior year. The fund, as expected, continued to pay out more in benefits than it collected in contributions and that, coupled with an increase of almost \$127 million in benefits paid to retirees, negated a portion of the investment gain enjoyed by the System in fiscal year 2005.

A schedule of the System's additions to and deductions from plan net assets and related changes (by major category) from fiscal year 2004 to 2005 is as follows (*expressed in millions*):

	June 30,		Change	
	2005	2004	Amount	%
Employer contributions	\$239.8	\$221.0	\$18.8	8.5%
Member contributions	209.0	204.2	4.8	2.4%
Other & contribution interest	430.7	411.0	19.7	4.8%
Net investment income	2,766.4	4,202.6	(1,436.2)	-34.2%
<b>Total additions</b>	<u>3,645.9</u>	<u>5,038.8</u>	<u>(1,392.9)</u>	<u>-27.6%</u>
Benefit payments	1,697.4	1,570.6	126.8	8.1%
Refunds	19.1	11.9	7.2	60.5%
Administrative expenses	22.4	17.4	5.0	28.7%
<b>Total deductions</b>	<u>1,738.9</u>	<u>1,599.9</u>	<u>139.0</u>	<u>8.7%</u>
<b>Net increase (decrease) in plan net assets</b>	<u>\$1,907.0</u>	<u>\$3,438.9</u>	<u>\$(1,531.9)</u>	<u>-44.5%</u>

## ANALYSIS OF FUNDED STATUS

The System remains financially sound as of June 30, 2006 and significantly ahead of its original actuarial funding schedule, which projected the June 30, 2000 Unfunded Actuarial Accrued Liability (UAAL) to be fully funded by the year 2020. As provided by law, any new unfunded liabilities arising during the fiscal year ended June 30, 2001, or any fiscal year thereafter, will be funded over a 25-year period.

In analyzing the System's overall funded status, it is important to remember that a retirement system's funding plan is based on a long time horizon, where temporary ups and downs in the market are expected. The more critical factor is that the System be able to meet the current expected earnings yield of, on average, a 7.75% annual return on investments.

## REQUESTS FOR INFORMATION

Members of the System's Board of Trustees and senior management are fiduciaries of the pension trust fund and, as such, are charged with the responsibility of ensuring that the System's assets are used exclusively for the benefit of plan participants and their beneficiaries. This financial report is designed to provide an overview of the System's finances and to demonstrate accountability for the resources entrusted to the System for the benefit of all of the System's stakeholders. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to:

State Retirement and Pension System of Maryland  
Attn: Melody Countess, CPA  
120 E. Baltimore Street, Suite 1601  
Baltimore, Maryland 21202-1600

## STATE RETIREMENT AND PENSION SYSTEM OF MARYLAND

## STATEMENTS OF PLAN NET ASSETS

As of June 30, 2006 and 2005

(Expressed in Thousands)

	2006	2005
<b>Assets:</b>		
<b>Cash &amp; cash equivalents</b> (note 3)	\$ 1,417,792	\$ 933,993
<b>Receivables:</b>		
Contributions:		
Employers	5,988	4,888
Employers – long term (note 5)	59,415	62,230
Members	991	1,134
Accrued investment income	60,202	63,736
Investment sales proceeds	586,980	251,070
Total receivables	<u>713,576</u>	<u>383,058</u>
<b>Investments, at fair value</b> (notes 2 & 3):		
U.S. Government obligations	1,666,613	1,761,411
Domestic corporate obligations	6,721,939	5,989,617
International obligations	190,383	310,876
Domestic stocks	15,013,876	16,303,305
International stocks	7,020,180	4,982,880
Mortgages & mortgage related securities	2,143,898	1,746,849
Real estate	836,429	751,660
Alternative investments	287,348	242,506
Collateral for loaned securities	2,148,668	2,485,395
Total investments	<u>36,029,334</u>	<u>34,574,499</u>
<b>Total assets</b>	<u>38,160,702</u>	<u>35,891,550</u>
<b>Liabilities:</b>		
Accounts payable & accrued expenses (note 7)	65,742	58,820
Investment commitments payable	1,574,002	1,272,224
Obligation for collateral for loaned securities	2,148,668	2,485,395
Other liabilities	1,471	1,392
<b>Total liabilities</b>	<u>3,789,883</u>	<u>3,817,831</u>
<b>Net assets held in trust for pension benefits</b>	<u>\$34,370,819</u>	<u>\$32,073,719</u>
<i>(A schedule of funding progress is presented on page 35)</i>		

The accompanying notes are an integral part of these financial statements.

## STATE RETIREMENT AND PENSION SYSTEM OF MARYLAND

### STATEMENTS OF CHANGES IN PLAN NET ASSETS

**for the Fiscal Years Ended June 30, 2006 and 2005**

*(Expressed in Thousands)*

	2006	2005
<b>Additions:</b>		
<b>Contributions</b> (note 4):		
Employers	\$285,275	\$239,855
Members	215,077	208,997
Other	431,415	426,191
Contribution interest (note 5)	4,186	4,508
Total contributions	<u>935,953</u>	<u>879,551</u>
<b>Investment income:</b>		
Net appreciation in fair value of investments	2,804,854	2,351,524
Interest	247,352	212,027
Dividends	200,633	221,500
Real estate operating net income	33,496	32,453
Income before securities lending activity	<u>3,286,335</u>	<u>2,817,504</u>
Gross income from securities lending activity	84,122	51,691
Securities lending borrower rebates	(77,218)	(44,435)
Securities lending agent fees	(1,121)	(1,161)
Net income from securities lending activity	<u>5,783</u>	<u>6,095</u>
Total investment income	3,292,118	2,823,599
Investment expenses (note 2E)	(66,469)	(57,210)
Net investment income	<u>3,225,649</u>	<u>2,766,389</u>
<b>Total additions</b>	<u>4,161,602</u>	<u>3,645,940</u>
<b>Deductions:</b>		
Benefit payments	1,829,468	1,697,397
Refunds (note 6)	16,455	19,162
Administrative expenses (note 2E)	18,579	22,386
<b>Total deductions</b>	<u>1,864,502</u>	<u>1,783,945</u>
<i>Net increase in plan assets</i>	2,297,100	1,906,995
<b>Net assets held in trust for pension benefits:</b>		
Beginning of the fiscal year	<u>32,073,719</u>	<u>30,166,724</u>
End of the fiscal year	<u>\$34,370,819</u>	<u>\$32,073,719</u>

*The accompanying notes are an integral part of these financial statements.*

## NOTES TO THE FINANCIAL STATEMENTS

### 1. GENERAL DESCRIPTION OF THE SYSTEM

#### A. Organization

The State Retirement Agency (the “Agency”) is the administrator of the State Retirement and Pension System of Maryland (the “System”), a Cost-sharing multiple-employer public employee retirement system. The System was established by the State Personnel and Pensions Article of the Annotated Code of Maryland to provide retirement allowances and other benefits to State employees, teachers, police, judges, legislators and employees of participating governmental units. Responsibility for the System’s administration and operation is vested in a 14-member Board of Trustees.

The State of Maryland is the statutory guarantor for the payment of all pensions, annuities, retirement allowances, refunds, reserves and other benefits of the System. The Agency is legally authorized to use all assets accumulated for the payment of benefits to pay such obligations to any plan member or beneficiary as defined by the terms of the plan. Consequently, the System is accounted for as a single plan as defined in Governmental Accounting Standards Board (GASB) Statement No. 25, “*Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans.*” Additionally, the System is fiscally dependent on the State by virtue of the legislative and executive controls exercised with respect to its operations, policies and administrative budget. Accordingly, the System is included in the State’s reporting entity and disclosed in its financial statements as a pension trust fund.

The System comprises the Teachers’ Retirement and Pension Systems, Employees’ Retirement and Pension Systems, State Police Retirement System, Judges’ Retirement System, Law Enforcement Officers’ Pension System and the Local Fire and Police System.

#### B. Covered Members

The Teachers’ Retirement System was established on August 1, 1927 to provide retirement allowances and other benefits to teachers in the State. Effective January 1, 1980, the Teachers’ Retirement System was closed to new members and the Teachers’ Pension System was established. As a result, teachers hired after December 31, 1979 became members of the Teachers’ Pension System as a condition of employment. On or after January 1, 2005, an individual who is a member of the Teachers’ Retirement System may not transfer membership to the Teachers’ Pension System.

On October 1, 1941, the Employees’ Retirement System was established to provide retirement allowances and other benefits to State employees, elected and appointed officials and the employees of participating governmental units. Effective January 1, 1980, the Employees’ Retirement System was essentially closed to new members and the Employees’ Pension System was established. As a result, State employees (other than correctional officers) and employees of participating governmental units hired after December 31, 1979 became members of the Employees’ Pension System as a condition of employment, while all State correctional officers and members of the Maryland General Assembly continue to be enrolled as members of the Employees’ Retirement System. On or after January 1, 2005, an individual who is a member of the Employees’ Retirement System may not transfer membership to the Employees’ Pension System. Currently, 144 governmental units participate in the Employees’ Systems.

The State Police Retirement System was established on July 1, 1949 to provide retirement allowances and other benefits to any police employee or cadet of the Maryland State Police.

The Judges’ Retirement System was established on June 30, 1969 to provide retirement allowances and other benefits for State and local, appointed, or elected judges.

The Law Enforcement Officers’ Pension System was established on July 2, 1990 to provide retirement allowances and other benefits for certain State and local law enforcement officers. This System includes both retirement plan and pension plan provisions which are applicable to separate portions of this System’s membership. The retirement plan provisions are only applicable to those members who, on the date they elected to participate in this System, were members of the Employees’ Retirement System. This System’s pension plan provisions are applicable to all other participating law enforcement officers.

The Local Fire and Police System was established on July 1, 1989 to provide retirement allowances and other benefits for law enforcement officers and fire fighters employed by participating governmental units. This System includes both retirement plan and pension plan provisions which are applicable to separate portions of this System's membership. The retirement plan provisions are only applicable to those officers and fire fighters who, on the date they elected to participate in this System, were members of the Employees' Retirement System. This System's pension plan provisions are applicable to all other participating governmental unit law enforcement officers and fire fighters. As of January 1, 2005, this system was closed to future participants.

The following table presents a summary of membership by system as of June 30, 2006, with comparative 2005 totals:

	Inactive & Deferred Vested	Retirees & Beneficiaries	Active Plan Participants		
			Vested	Non-vested	Total
Teachers' Retirement & Pension Systems	21,053	50,279	69,413	30,905	100,318
Employees' Retirement & Pension Systems	28,063	50,487	66,948	20,152	87,100
Judges' Retirement System	14	330	296	-	296
State Police Retirement System	58	1,937	1,109	332	1,441
Local Fire and Police System	7	16	36	19	55
Law Enforcement Officers' Pension System	115	782	1,546	517	2,063
Totals as of June 30, 2006	49,310	103,831	139,348	51,925	191,273
Totals as of June 30, 2005	47,664	100,196	129,091	58,959	188,050

### C. Summary of Significant Plan Provisions

All plan benefits are specified by the State Personnel and Pensions Article of the Annotated Code of Maryland. Retirement allowances are computed using both the highest three years' average final salary (AFS) and the actual number of years of accumulated creditable service. Pension allowances are computed using both the highest three consecutive years' AFS and the actual number of years of accumulated creditable service. Various retirement options are available under each system which ultimately determines how a retiree's benefit allowance will be computed. Some of these options require actuarial reductions based on the retiree's and/or designated beneficiary's attained age and similar actuarial factors. A brief summary of the retirement eligibility requirements of, and the benefits available under, the various systems follows:

#### Service Retirement Allowances

A member of either the Teachers' or Employees' Retirement System is generally eligible for full retirement benefits upon the earlier of attaining age 60 or accumulating 30 years of eligibility service regardless of age. The annual retirement allowance equals 1/55 (1.8%) of the member's AFS multiplied by the number of years of accumulated creditable service.

A member of either the Teachers' or Employees' Pension System is eligible for full retirement benefits upon the earlier of attaining age 62, with specified years of eligibility service, or accumulating 30 years of eligibility service regardless of age. Generally, the annual pension allowance for a member of either the Teachers' or Employees' Pension System equals 1.2% of the member's AFS, multiplied by the number of years of creditable service accumulated prior to July 1, 1998, plus 1.4% of the member's AFS, multiplied by the number of years of creditable service accumulated subsequent to June 30, 1998. However, the annual pension allowance for a member of the Employees' Pension System, who is employed by a participating governmental unit that does not provide the enhanced pension benefits, equals 0.8% of the member's AFS up to the social security integration level (SSIL), plus 1.5% of the member's AFS in excess of the SSIL, multiplied by the number of years of accumulated creditable service. For the purpose of computing pension allowances, the SSIL is the average of the social security wage bases for the past 35 calendar years ending with the year the retiree separated from service. On April 25, 2006, new legislation was enacted with an effective date of July 1, 2006, that enhanced the pension benefits for active members, of June 30, 2006, of the Pension Retirement System. According to the State Employees' and Teachers' Pension Enhancement Benefit Act of 2006, the annual service retirement allowance remains equal to 1.2% of average final compensation times service credit to June 30, 1998 and increases to 1.8% of average final compensation times service credit from July 1, 1998 forward.

A member of the State Police Retirement System is eligible for full retirement benefits upon the earlier of attaining age 50 or accumulating 22 years of eligibility service regardless of age. The annual retirement allowance equals 2.55% of the member's AFS multiplied by the number of years of accumulated creditable service and may not exceed 71.4% of the member's AFS.

A member of the Judges' Retirement System is eligible for full retirement benefits upon attaining age 60. The annual retirement allowance for a member with at least 16 years of accumulated creditable service equals  $\frac{2}{3}$  (66.7%) of the salary of an active judge holding a comparable position. The annual retirement allowance is prorated if the member retires with fewer than 16 years of accumulated creditable service.

A member of the Law Enforcement Officers' Pension System is eligible for full retirement benefits upon the earlier of attaining age 50 or accumulating 25 years of eligibility service regardless of age. The annual retirement allowance for a member who is covered under the retirement plan provisions equals  $\frac{1}{50}$  (2.0%) of the member's AFS multiplied by the number of years of accumulated creditable service up to 30 years, plus  $\frac{1}{100}$  (1.0%) of the member's AFS multiplied by the number of years of accumulated creditable service in excess of 30 years. For members subject to the pension provisions, full service pension allowances equal 2.0% of AFS up to a maximum benefit of 60% (30 years of credit).

A member of the Local Fire and Police System who is covered under the retirement plan provisions is eligible for full retirement benefits upon the earlier of attaining age 60 or accumulating 25 years of eligibility service regardless of age. The annual retirement allowance equals  $\frac{1}{50}$  (2.0%) of the member's AFS multiplied by the number of years of accumulated creditable service up to 30 years, plus  $\frac{1}{100}$  (1.0%) of the member's AFS multiplied by the number of years of accumulated creditable service in excess of 30 years. A member who is covered under the pension plan provisions is eligible for full pension benefits upon the earlier of attaining age 62 or accumulating 25 years of eligibility service regardless of age. The annual pension allowance equals 1.0% of the member's AFS up to the SSIL, plus 1.5% of the member's AFS in excess of the SSIL, multiplied by the number of years of accumulated creditable service.

### **Vested Allowances**

Any member (other than a judge) who terminates employment before attaining retirement age but after accumulating 5 years of eligibility service is eligible for a vested retirement allowance. Judges have no minimum service requirements prior to vesting. A member who terminates employment prior to attaining retirement age and before accumulating 5 years of eligibility service receives a refund of all member contributions and interest.

### **Early Service Retirement**

A member of either the Teachers' or Employees' Retirement System may retire with reduced benefits after completing 25 years of eligibility service. Benefits are reduced by 0.5% per month for each month remaining until the retiree either attains age 60 or would have accumulated 30 years of eligibility service, whichever is less. The maximum reduction for a Teachers' or Employees' Retirement System member is 30 percent. A member of either the Teachers' or Employees' Pension System may retire with reduced benefits upon attaining age 55 with at least 15 years of eligibility service. Benefits are reduced by 0.5% per month for each month remaining until the retiree attains age 62. The maximum reduction for a Teachers' or Employees' Pension System member is 42%. Members of the State Police, Judges', Law Enforcement Officers' and Local Fire and Police Systems are not eligible for early service benefits.

### **Disability and Death Benefits**

Generally, a member covered under retirement plan provisions who is permanently disabled after 5 years of service receives a service allowance based on a minimum percentage (usually 25%) of the member's AFS. A member covered under pension plan provisions who is permanently disabled after accumulating 5 years of eligibility service receives a service allowance computed as if service had continued with no change in salary until the retiree attained age 62. A member (other than a member of the Maryland General Assembly or a judge, both of which are ineligible for accidental disability benefits) who is permanently and totally disabled as the result of an accident occurring in the line of duty receives  $\frac{2}{3}$  (66.7%) of the member's AFS plus an annuity based on all member contributions and interest. Death benefits are equal to a member's annual salary as of the date of death plus all member contributions and interest.

### Adjusted Retirement Allowances

Retirement and pension allowances are increased annually to provide for changes in the cost of living according to prescribed formulae. Such adjustments for retirees are based on the annual change in the consumer price index. Generally, for Teachers' and Employees' Pension System retirees, the pension allowance adjustments are limited to 3% of the preceding year's allowance. However, annual increases to pension allowances for Employees' Pension System retirees who were employed by a participating governmental unit that does not provide enhanced pension benefits are limited to 3% of the initial allowance. Retirement allowances for legislators and judges are recalculated when the salary of an active member holding a comparable position is increased.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### A. Basis of Accounting

The System's financial statements are prepared on the accrual basis of accounting. Accordingly, investment purchases and sales are recorded as of their respective trade dates and all contributions, benefits and refunds are recognized in the period when due. In accordance with GASB Statement No. 20, *"Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting,"* the System has elected to apply all applicable GASB pronouncements and only Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins issued on or before November 30, 1989.

### B. Investment Limitations

The State Personnel and Pensions Article of the Annotated Code of Maryland authorizes the System to invest plan assets in stocks, bonds, notes, certificates of indebtedness, mortgage notes, real estate, debentures or other obligations, subject to the terms, conditions, limitations and restrictions imposed by the Board of Trustees of the State Retirement and Pension System of Maryland. As such, no more than 25% of the assets invested in common stocks may be invested in non-dividend paying common stocks. In addition, no investment in any one organization may constitute more than 5% of the total assets of the System (valued at cost). The System did not exceed either of these investment limits.

### C. Portfolio Valuation Method

The System investments are reported at fair value. For fixed income securities, fair value is based on quoted market prices provided by independent pricing services. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Mortgages and mortgage related securities are valued on the basis of future principal and interest payments and are discounted at prevailing interest rates for similar instruments. Fair value for real estate investments is based on estimated current values and independent appraisals. Fair value for alternative investments and mutual funds (other than those funds traded on a national or international exchange) is based on information provided by the applicable fund managers. Investment amounts presented in the Statements of Plan Net Assets represent the fair value of the respective portfolios as of the fiscal year-end. Similarly, investment income amounts reported in the Statements of Changes in Plan Net Assets represent the income or loss derived from such investments for the year then ended. Accordingly, significant market fluctuations could periodically occur subsequent to the financial statement valuation date, which are not reflected in either the fair value of investments or the related investment income presented in these financial statements.

### D. Derivatives

The System may invest in derivatives as permitted by guidelines established by the Board of Trustees. Compliance with these guidelines is monitored by Agency staff. Pursuant to such authority, the System invests in foreign currency forward contracts, options, futures, swaps, collateralized mortgage obligations, mortgage related securities, interest-only and principal-only securities. No derivatives were purchased with borrowed funds.

Derivatives are generally used to hedge against foreign currency risk and changes in interest rates, improve yield and adjust the duration of the System's fixed income portfolio. These securities are subject to changes in value due to changes in interest rates or currency valuations. Additionally, mortgage related securities are subject to prepayment risk

when interest rates are falling. Credit risk for derivatives results from the same considerations as other counterparty risk assumed by the System, which is the risk that the counterparty might be unable to meet its obligations.

The System enters into forward foreign currency exchange contracts for hedging purposes to minimize the short-term impact of foreign currency fluctuations on the asset positions of foreign investments. These foreign currency exchange contracts are reported at fair value based on published market prices and quotations from major investment firms. The System could be exposed to risk if the counterparties to the contracts are unable to meet the terms of the contracts. The System seeks to minimize risk from counterparties by establishing minimum credit quality standards.

#### **E. Administrative and Investment Expenses**

All of the System's administrative and investment expenses (e.g., salaries of Agency employees, investment advisory fees) are incurred centrally and charged to each individual retirement or pension system on the basis of its percentage ownership in the System's net assets. All of the System's administrative and investment expenses are funded from investment income. See page 39 for detailed Schedules of Administrative and Investment Expenses.

#### **F. Federal Income Tax Status**

During the fiscal years ended June 30, 2006 and 2005, the System qualified under Section 401(a) of the Internal Revenue Code and was exempt from federal income taxes under Section 501(a) of the Code.

### **3. CASH, CASH EQUIVALENTS, AND INVESTMENTS**

#### **A. Legal Provisions**

The Board of Trustees is authorized by Section 21-116(c), Annotated Code of Maryland, to establish and maintain the investment policy manual, which authorizes investing in all major sectors of the capital market in order to diversify and minimize total investment program risk. Such sectors include, but are not limited to the following:

- Common stock, preferred stock, convertible securities, warrants, and similar rights of U.S. and non-U.S. companies, wherever organized shares in investment funds and trusts may be purchased.
- Private Equity-Direct/Partnerships/Funds – The System currently has a 2% target and employs a consultant to advise them on selecting partnerships.
- Real Estate Investment Trusts (REITS) – The System employs an investment manager who specializes in this area.
- Commingled Real Estate Funds – May be open or close ended. Earnings may be reinvested in the fund or distributed.
- Directly Owned Real Estate – Affords the System greater control over the portfolio composition; ability to evaluate property prior to acquisition; greater control over managers' compensation levels and fee structures; and greater assurance that the investment objectives of SRPS are the primary guiding force of manager activities rather than investment objectives suitable to multiple investors.
- Fixed income obligations of the U.S. government and its states and local subdivisions, non-U.S. governments and their states and local subdivisions, U.S. and non-U.S. companies, wherever organized, and supra-national organizations. Any limits are governed by the System's contract with each manager.
- Commingled funds offered by the Manager, or affiliates thereof, that invest in permissible investments.
- Futures and other Derivatives - The System may employ financial futures and other derivatives that are traded on a recognized exchange. Allowable instruments will include, but will not be limited to: fixed income, domestic and international equity futures, and forward currency contracts. Futures and other derivatives may not be used to take asset allocation outside the target ranges or to leverage the portfolio.
- The System will begin investing in Emerging Managers as well as Global REITS in FY2007.

The Systems' policy is to consider all major sectors of the capital market in order to diversify and minimize total investment program risk.

### **Investment Restrictions**

The System may not invest more than 25% of total assets (at market value) committed by the System to common stocks in non-dividend-paying common stocks, since prohibited under State Personnel & Pensions' Article section 21-123 c.ii.

Unless the Board of Trustees grants prior authorization, the System may not:

- Invest more than 5% of the total assets of the System in any one company.
- Invest any funds of the System in any one company in excess of 5% of that company's total capital.
- Borrow money.
- Purchase securities on margin when the notional value of open positions exceeds the market value of the account.
- Effect short sales of equities, other than those executed by external managers or for the implementation of tactical asset allocation on a market sector.
- Pledge or hypothecate securities with the exception of fully collateralized security lending agreements and reverse repurchase agreements.
- Employ derivatives to reduce portfolio duration to less than that of cash equivalents or to increase duration to more than that available from owning long term U.S. Treasury Bonds.

The System is also authorized by its Board of Trustees to operate a securities lending program, and has contracted with its custodian bank to reinvest cash collateral received from the transfer of securities in any investment instrument authorized by the investment policy. The System's Board of Trustees has determined the collateralization percentages necessary for both foreign and domestic demand deposits. The Board of Trustees has established a policy to require collateral equal to 105% for international equity securities and 102% for all other securities, which is marked to market daily.

### **B. Cash and Cash Equivalents**

For cash deposits and cash equivalents, custodial credit risk is the risk that, in the event of a bank failure, the government's deposits may not be returned to it.

The amount of the System's total cash and cash equivalents at June 30, 2006, was \$1,417,791,562. Cash deposits in bank accounts totaled \$10,860,817 which was uninsured and uncollateralized. As of June 30, 2006, the system held \$1,524,866,283 in cash equivalents. Cash equivalents are created through daily sweeps of excess cash by the System's custodial bank into bank sponsored short-term securities backed by the U.S. government, by the agencies sweep into commercial paper, and by the System's operational bank's sweep into a U.S. government money market fund. The System also held (\$117,935,538) in open sales which were reported net of cash and cash equivalents due to the timing of their clearing.

### **C. Investments**

All of the investment assets of the system are invested in short-term, fixed income, equity, and real estate securities. These investments are accounted for as the System and are allocated to Teachers' Retirement and Pension, Employee Retirement and Pension, Judges Retirement, State Police Retirement, Law Enforcement Officers' Pension, and the Local Fire and Police Systems.

All investments are governed by the prudent person rule described in Section 21-203 of the Annotated Code of Maryland. The prudent person rule established a standard for all fiduciaries, to act as a prudent person would be expected to act, with discretion and intelligence, while investing for income and preservation of principal.

The following table presents the fair value of investments as of June 30, 2006 and 2005 (*in thousands*):

Investment Type	Fair Value	
	2006	2005
Alternative investments (domestic)	\$260,336	\$242,506
Alternative investments (international)	27,012	0
Asset backed securities	447,617	299,151
Collateralized mortgage obligations	432,489	393,308
Convertibles	1,506	1,473
Domestic corporate obligations	724,082	747,401
Domestic equities	5,577,739	5,274,781
International obligations	56,392	85,079
International equities	3,395,769	3,770,562
Mortgage pass-throughs	1,711,409	1,353,541
Municipal	14,989	27,093
Mutual funds	18,541,250	17,176,326
Options	3,903	583
Private placement	20,393	1,701
Real estate	836,429	751,660
Security lending short-term collateral investment pool	2,148,668	2,485,395
Swaps	-18,591	0
U. S. government agency	245,724	122,336
U.S. treasury bonds	400,824	222,363
U.S. treasury notes	1,009,114	1,401,593
U.S. treasury strips	10,951	15,119
Yankee bonds	181,329	202,528
Total	<u>\$36,029,334</u>	<u>\$34,574,499</u>

## D. Interest Rate Risk

As of June 30, 2006, the System had the following investments listed by specific identifier with the exception of the Mutual Funds, which are based on their average maturity:

Investment Type:	Fair Value (in thousands)	Investment Maturities (in years)			
		Less than 1	1 thru 5	5+ thru 10	More than 10
Asset backed securities	\$ 447,617	\$	\$ 115,075	\$ 69,088	\$ 263,454
Bond mutual funds	5,480,701	827,876	4,225,512	276,436	150,877
Collateralized mortgage obligations	432,489		12,462		420,02
Convertible bonds	1,506				1,506
Domestic corporate obligations	724,082	72,149	329,842	258,415	63,676
International obligations	56,392	19,532	32,662		4,198
Mortgage pass-throughs	1,711,409	170	14,156	2,135	1,694,948
Municipals	14,989		4,338	10,651	
Private Placement	20,393		17,182	1,645	1,566
Short term	1,524,866	1,524,866			
Swaps	-18,591	-3,014	-10,049	-8,886	3,358
U.S. government agency	245,724	34,786	87,674	70,521	52,743
U.S. treasury bonds	400,824				400,824
U.S. treasury notes	1,009,114	35,592	564,442	409,080	
U.S. treasury strips	10,951				10,951
Yankee bonds	181,329	6,900	44,763	51,491	78,175
Totals	<u>\$12,243,795</u>	<u>\$ 2,518,857</u>	<u>\$ 5,438,059</u>	<u>\$ 1,140,576</u>	<u>\$ 3,146,303</u>

The portfolio is restricted to maintaining an effective duration of plus or minus one year of the benchmark. Market or interest rate risk is the greatest risk faced by an investor in the fixed income market. The price of a fixed income security typically moves in the opposite direction of the change in interest rates. Derivative securities, variable rate investments with coupon multipliers greater than one, and securities with long terms to maturity are examples of investments whose fair values may be highly sensitive to interest rate changes. These securities are reported at fair value in the statement of plan net assets.

Futures, options, swaps, and forward contracts are allowed to the extent that they are used in a manner that does not materially increase total portfolio volatility or relate to speculative activities. Unleveraged derivatives are permitted for the purpose of hedging investment risk, to replicate an investment that would otherwise be made directly in the cash market or to modify asset exposure in tactical portfolio shifts. Use of derivatives should not materially alter the characteristics, including the investment risk, of the Account. The Manager must at all times have, in place and use, procedures that subject derivative based strategies to rigorous scenario and volatility analysis. No single derivative based strategy should subject the account to greater variance than would be typical of the manager's physical portfolio strategy under a worst-case scenario.

Mortgage-backed securities that the Manager, with the Agency's approval, classifies as exhibiting unusually high interest rate sensitivity relative to U.S. Government agency mortgage pass-through issues shall not exceed 5% of the total account. Examples of securities that would qualify as "highly interest rate sensitive" include Interest Only Securities, Principal Only Securities and inverse floaters, of which the System held less than \$4 million as of June 30, 2006.

As of June 30, 2006, the System had \$1.7 billion invested in mortgage pass-through securities issued by the Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, and Government National Mortgage Association. These investments are moderately sensitive to changes in interest rates because they are backed by mortgage loans in which the borrowers have the option of prepaying.

**E. Credit Risk**

The System's exposure to credit risk as of June 30, 2006 is as follows:

**Credit Quality Distribution for Securities with Credit Exposure  
as a Percentage of Total Investments**

Investment Type	Quality Rating	% of Portfolio
Asset Backed Securities	AAA	0.985%
Asset Backed Securities	AA	0.055%
Asset Backed Securities	A	0.077%
Asset Backed Securities	BBB	0.125%
Short term	AAA	1.513%
Short term	A	2.719%
Collateralized Mortgage Obligation	AAA	1.143%
Collateralized Mortgage Obligation	AA	0.017%
Collateralized Mortgage Obligation	A	0.024%
Collateralized Mortgage Obligation	BAA	0.004%
Collateralized Mortgage Obligation	BBB	0.003%
Collateralized Mortgage Obligation	NR	0.009%
Convertible Bonds	B	0.004%
Corporate Bonds	AAA	0.085%
Corporate Bonds	AA	0.171%
Corporate Bonds	A	0.463%
Corporate Bonds	BAA	0.120%
Corporate Bonds	BBB	0.460%
Corporate Bonds	BB	0.337%
Corporate Bonds	B	0.347%
Corporate Bonds	CAA	0.021%
Corporate Bonds	CA	0.001%
Corporate Bonds	CCC	0.003%
Corporate Bonds	NR	0.003%
International Obligation	AAA	0.007%
International Obligation	AA	0.096%
International Obligation	BB	0.012%
International Obligation	NR	0.042%
Mortgage Pass Through	AAA	4.735%
Mortgage Pass Through	NR	0.015%
Municipal Bonds	AAA	0.026%
Municipal Bonds	AA	0.014%
Municipal Bonds	BB	0.001%
Mutual Funds	NR	15.212%
Private Placement	BBB	0.002%
Private Placement	NR	0.055%
Agency	AAA	0.558%
Agency	AA	0.014%
Agency	BAA	0.001%
Agency	BB	0.040%
Agency	NR	0.069%
Yankee Bonds	AAA	0.039%
Yankee Bonds	AA	0.043%
Yankee Bonds	A	0.095%
Yankee Bonds	BAA	0.008%
Yankee Bonds	BBB	0.181%
Yankee Bonds	BB	0.106%
Yankee Bonds	NR	0.031%

The current policy regarding credit risk requires each fixed income investment manager to maintain a minimum average credit quality of "A" for their total account. The above-listed ratings are based on the most conservative rating when multiple ratings were offered.

## F. Foreign Currency Risk

The System's exposure to foreign currency risk as of June 30, 2006 is as follows:

Investment Type	Currency	Maturity	Fair Value (in thousands)
Cash	Australian dollar		\$198
Common stock	Australian dollar		61,000
Common stock	Brazilian real		185
Cash	Canadian dollar		891
Common stock	Canadian dollar		113,179
Cash	Danish krone		29
Common stock	Danish krone		27,241
Credit Suisse Shirley & Charl Alternative Investments	Egyptian pound	01/16/07	2,087
Cash	Euro currency		16,926
Common stock	Euro currency		862
Bundesrepublik Deutschland	Euro currency	10/18/06	1,058,209
Swaps	Euro currency		13,057
Cash	Euro currency		-171
Common stock	Hong kong dollar		110
Common stock	Hong kong dollar		118,802
Common stock	Indonesian rupiah		4,046
Cash	Japanese yen		2,842
Common stock	Japanese yen		599,038
Euro Investment Bank	Japanese yen	09/20/06	2,623
Republic of Italy	Japanese yen	03/27/08	30,575
Republic of Italy	Japanese yen	10/10/06	3,852
Common stock	Malaysian ringgit		7,185
Cash	Malaysian ringgit		55
Cash	Mexican peso		198
Common stock	Mexican peso		13,174
Cash	New Taiwan dollar		1,883
Common stock	New Taiwan dollar		12,643
Common stock	New Turkish lira		20,973
Cash	Norwegian krone		212
Common stock	Norwegian krone		52,357
Cash	Polish Zloty		6
Common stock	Polish Zloty		2,017
Alternative Investments	Pound sterling		10,086
Cash	Pound sterling		909
Common stock	Pound sterling		509,040
Swaps	Pound sterling		159
Cash	Singapore dollar		737
Common stock	Singapore dollar		49,999
Cash	South African rand		259
Common stock	South African rand		44,599
Common stock	South Korean won		56,077
Cash	Swedish krona		268
Common stock	Swedish krona		37,986
Cash	Swiss franc		530
Common stock	Swiss franc		218,642
Mutual funds	Not applicable		3,758,414
Total			<u>\$6,853,989</u>

The majority foreign currency-denominated investments are in non-U.S. stocks, which the System's current asset allocation policy has a target of 13% International and 10% Global.

*Note: This schedule does not agree with the total International obligations and International equities as listed on the Statement of Plan Net Assets due to ADR's and International obligations valued in U.S. dollars but classified as International.*

## G. Security Lending Transactions

The System accounts for securities lending transactions in accordance with (GASB) Statement No. 28 "Accounting and Financial Reporting for Securities Lending Transactions," which established standards of accounting and financial reporting for securities lending transactions.

The following table details the net income from securities lending for the year ending June 30, 2006 (*in thousands*):

	<u>2006</u>	<u>2005</u>
Gross income from securities lending activity	\$84,122	\$51,691
Less:		
Securities lending borrower rebates	77,218	44,435
Securities lending agent fees	<u>1,121</u>	<u>1,161</u>
Expenses from securities lending activity	78,339	45,596
Net income from securities lending activity	<u>\$ 5,783</u>	<u>\$ 6,095</u>

The Board of Trustees has authorized the System to lend its securities to broker-dealers with a simultaneous agreement to return the collateral for the same securities in the future. The System's custodian, pursuant to a written agreement, is permitted to lend all long-term securities to authorized broker-dealers subject to the receipt of acceptable collateral. There have been no significant violations of the provisions of the agreement during the period of these financial statements. The System lends securities for collateral in the form of either cash or other securities. The types of securities on loan at June 30, 2006 are long-term U.S. government and agency obligations, domestic and international equities as well as domestic and international obligations. At the initiation of a loan, borrowers are required to provide collateral amounts of 102% (domestic equities and bonds) and 105% (international equities) of the fair value of the securities lent. In the event the collateral fair value falls below the respective collateral percentages, the borrower is required to provide additional collateral by the end of the next business day. The contractual agreement with the System's custodian provides indemnification in the event the borrower fails to return the securities lent or fails to pay the System income distributions by the securities' issuers while the securities are on loan.

Although the average term of the System's security loans is one week, each loan can be terminated at will by either the System or the borrower. Cash collateral is invested in one of the lending agent's short-term investment pools, which at June 30, 2006 had a weighted average maturity of fifty days and an average expected maturity of one hundred ninety-one days. The System cannot pledge or sell collateral securities received unless and until a borrower defaults. Investments made with cash received as collateral and the corresponding liabilities are reported in the Statement of Net Assets. Because the relationship between the maturities of the investment pools and the System's security loans is affected by the maturities of the loans made by other entities that use the agent's pools, the System cannot match maturities. At year-end, the System had no credit risk exposure to borrowers because the amount the System owed the borrowers exceeded the amount the borrowers owed the System.

The following table presents the fair values of the underlying securities, and the value of the collateral pledged as of June 30, 2006 (*in thousands*):

<b>Securities Lent</b>	<b>Fair Value Loaned Securities</b>	<b>Collateral Fair Value</b>	<b>Percent Collateralized</b>
<b>Lent for cash collateral:</b>			
U.S. government and agency	\$ 828,699	\$ 841,326	102%
Domestic fixed income	87,826	88,844	101%
International fixed income	53,688	54,111	101%
Domestic equity	654,147	666,489	102%
International equity	<u>485,779</u>	<u>497,898</u>	102%
<b>Lent for noncash collateral:</b>			
U.S. government and agency	7,800	7,978	102%
Domestic fixed income	<u>120</u>	<u>142</u>	118%
<b>Total securities lent</b>	<u><u>\$2,118,059</u></u>	<u><u>\$2,156,788</u></u>	102%

The securities collateral value is based on the System's pro rata share of the value of the securities collateral maintained in a pool at State Street Bank for all lending clients participating in the lending program. Collateral value listed above includes all collateral for securities on loan; whereas, collateral for loaned securities disclosed on the Statements of Plan Net Assets includes only cash collateral, per GASB Statement No. 28.

#### H. Commission Recapture Program

The Board of Trustees has authorized the System to enter into a commission recapture program. This program allows the System to recapture a portion of the commissions paid to broker/dealers with which the System has entered into an agreement. Earnings credited to commission recapture income for the fiscal years ended June 30, 2006 and June 30, 2005 were \$92 and \$208 (expressed in thousands) respectively.

#### I. Reclassification

Certain amounts in the prior year's financial statements have been reclassified to conform to the presentation in the current year's financial statements.

### 4. CONTRIBUTIONS

The State Personnel and Pensions Article requires both active members and their respective employers to make contributions to the System. Rates for required contributions by active members are established by law. Members of the Teachers' and Employees' Retirement Systems are required to contribute 7% or 5% of earnable compensation depending upon the retirement option selected. Members of the State Police and Judges' Retirement Systems are required to contribute 8% and 6% of earnable compensation, respectively. Generally, members of the Teachers' and Employees' Pension Systems are required to contribute 2% of earnable compensation. However, members of the Employees' Pension System who are employed by a participating governmental unit that does not provide the enhanced pension benefits are required to contribute 5% of earnable compensation in excess of the social security taxable wage base. The contribution rate under the state Employees' and Teachers' Pension Enhancement Benefit Act of 2006, which becomes effective July 1, 2006, will increase to 3% of the member's earnable compensation for fiscal year 2007, 4% for fiscal year 2008 and will be 5% of earnable compensation thereafter.

Contribution rates for employer and other "nonemployer" contributing entities are established by annual actuarial valuations using the entry age normal cost method with projection and other actuarial assumptions adopted by the Board of Trustees. These contribution rates have been established as the rates necessary to fully fund normal costs and amortize the unfunded actuarial accrued liability.

The unfunded actuarial liability is being amortized in distinct layers. The unfunded actuarial accrued liability which existed as of the June 30, 2000 actuarial valuation is being amortized over a 40-year period (as provided by law) from July 1, 1980. Also as provided by law, any new unfunded liabilities or surpluses arising during the fiscal year ended June 30, 2001, or any fiscal year thereafter, will be amortized over a 25-year period from the end of the fiscal year in which the liability or surplus arose.

Effective July 1, 2002, the law provides that the contribution rates may be more or less than the actuarially determined rates as described above for the Employees' Retirement and Pension Systems and the Teachers' Retirement and Pension Systems. When the funding ratio for each of the combined Systems is at least 90% but not more than 110%, the contribution rate will be the rate certified by the Board of Trustees for the previous fiscal year, adjusted to reflect legislative changes that result in changes to the normal cost. If the funding ratio is below 90%, the contribution rate will be the sum of the contribution rate for the previous fiscal year and 20% of the difference between the full funding rate for the current fiscal year and the contribution rate for the previous fiscal year. If the funding ratio is above 110%, the contribution rate will be the difference between the contribution rate for the previous fiscal year and 20% of the difference between the contribution rate for the previous fiscal year and the full funding rate for the current fiscal year.

The State of Maryland (which is also a non-employer contributor to the Teachers' Retirement and Pension Systems and the Judges' Retirement System), the Maryland Automobile Insurance Fund, the Injured Workers' Insurance Fund and 144 participating governmental units make all of the employer and other (non-employer) contributions to the System.

## 5. LONG-TERM CONTRIBUTIONS RECEIVABLE

In addition to actuarially determined contributions, certain withdrawn employers also make annual installment payments, including interest at the actuarially assumed rate of return in effect at the time of withdrawal (7% or 7.5% per year), for liabilities associated with employees that have elected to stay in the System when their employer elected to withdraw. As of June 30, 2006 and 2005, the outstanding balances were \$59,415 and \$62,230 (*expressed in thousands*), respectively. These payments are due over various time periods, based on the date of the employer's withdrawal, and all are scheduled to culminate with their final payment in fiscal year 2020.

## 6. REFUNDS

Member contributions plus interest may be refunded to a member who withdraws from the System, or to the designated beneficiary following a member's death. Employer contributions may also be refunded with interest to any participating governmental unit electing to withdraw from the System. For the fiscal years ended June 30, 2006 and 2005, refunds to members and withdrawing employers were as follows (*expressed in thousands*):

	<u>2006</u>	<u>2005</u>
Member refunds	\$ 16,455	\$ 13,424
Employer refunds	<u>0</u>	<u>5,738</u>
Total refunds	<u>\$ 16,455</u>	<u>\$ 19,162</u>

## 7. ACCOUNTS PAYABLE AND ACCRUED EXPENSES

For the fiscal years ended June 30, 2006 and 2005, accounts payable and accrued expenses consisted of the following components (*expressed in thousands*):

	<u>2006</u>	<u>2005</u>
Administrative expenses	\$ 6,892	\$ 11,748
Investment management fees	28,636	24,340
Tax and other withholdings	<u>30,214</u>	<u>22,732</u>
Total	<u>\$ 65,742</u>	<u>\$ 58,820</u>

REQUIRED SUPPLEMENTARY INFORMATION

SCHEDULE OF FUNDING PROGRESS  
(Expressed in Thousands)

Actuarial Valuation Date June 30,	Actuarial Value of Assets a	Actuarial Accrued Liability (AAL) b	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a / b)	Covered Payroll c	UAAL as a Percentage of Covered Payroll [(b - a) / c]
1997	\$21,920,696	\$25,383,206	\$3,462,510	86.36%	\$5,657,385	61%
1998	24,850,355	27,416,935	2,566,580	90.64	5,900,456	43
1999 *	27,646,579	28,475,380	828,801	97.09	6,312,417	13
2000	30,649,380	30,279,866	(369,514)	101.22	6,725,870	(5)
2001	31,914,778	32,469,942	555,164	98.29	7,255,036	8
2002	32,323,263	34,131,284	1,808,021	94.70	7,867,794	23
2003	32,631,465	34,974,601	2,343,136	93.30	8,134,419	29
2004	33,484,657	36,325,704	2,841,047	92.18	8,069,481	35
2005	34,519,500	39,133,450	4,613,950	88.21	8,603,761	54
2006	35,795,025	43,243,492	7,448,467	82.78	9,287,576	80

\* The 1999 actuarial accrued liability does not include an additional \$153 million liability due to municipal employers voluntarily electing enhanced benefits during the period July 1, 1999 to December 31, 1999.

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYERS AND OTHER CONTRIBUTING ENTITY

(Expressed in Thousands)

Fiscal Year Ended June 30,	Annual Required Contributions	Percentage Contributed
1997	\$740,258	100%
1998	735,788	100
1999	693,353	100
2000	682,422	100
2001	634,309	100
2002	574,019	100
2003	654,578	92
2004	710,632	89
2005	805,564	83
2006	874,079	82

## NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION

### 1. DESCRIPTION OF SCHEDULE OF FUNDING PROGRESS

The Schedule of Funding Progress summarizes the actuarial value of the System's assets and actuarial accrued liability as of June 30, 2006 and each of the nine preceding fiscal years. The data presented in the schedule were obtained from the System's independent actuary's annual valuation report for each year presented.

The schedule is presented to provide a consistent basis for measuring the System's annual progress toward funding its actuarial accrued liability in accordance with its actuarial funding method. The primary measure of funding progress is the System's funded ratio (i.e., actuarial value of assets expressed as a percentage of the actuarial accrued liability). An increase in the funded ratio indicates improvement in the System's ability to pay all projected benefits as they become due. The System is fully funded if the funded ratio is greater than or equal to 100%. During the year ended June 30, 2006, the System's funded ratio decreased from 88.21% to 82.79%.

The Schedule of Funding Progress also discloses the relationship between the System's covered payroll (i.e., all elements included in compensation paid to active members on which contributions are based) and the unfunded actuarial accrued liability. This relationship, expressed as a ratio, is a measure of the significance of the unfunded actuarial accrued liability relative to the capacity to pay all contributions required to fund the liability. During the year ended June 30, 2006, the System's ratio of the unfunded actuarial accrued liability to its covered payroll went from 54% to 80%.

### 2. ACTUARIAL METHODS AND ASSUMPTIONS

#### A. Funding Method

The System uses the entry age normal cost method with projection to determine the actuarial accrued liability on which future employer contribution rates will be based. Under this funding method, a total contribution rate is determined which consists of two elements, the normal cost rate and the unfunded actuarial liability rate (see note 4).

The unfunded actuarial accrued liability (UAAL) is being amortized, as a level percentage of payroll, in distinct pieces. The UAAL which existed as of the June 30, 2000 actuarial valuation is being amortized over the remaining 14-year period to June 30, 2020. Each new layer of UAAL arising subsequent to the year ended June 30, 2000 is being amortized in separate annual layers over a 25-year period. Each separate amortized layer has a closed amortization period. The equivalent single amortization period is 30 years.

#### B. Asset Valuation Method

Assets are valued for funding purposes using a five-year moving average. Under this method, the year end actuarial asset value equals 1/5 of the current fiscal year end fair value, as reported in the financial statements, plus 4/5 of the "expected market value." For purposes of this calculation, the "expected market value" is the preceding fiscal year's actuarial asset value, adjusted for the current fiscal year's cash flows with interest accumulated at the actuarial assumed rate of return on investments.

#### C. Actuarial Assumptions

The assumptions used for the actuarial valuation were recommended by the System's independent actuary, based upon periodic analyses of the System's experience, and adopted by the Board of Trustees. Differences between assumed and actuarial experience (i.e., actuarial gains and losses) are part of the unfunded actuarial liability. The following significant assumptions were used in the actuarial valuation as of June 30, 2006:

- a rate of return on investments of 7.75% compounded annually (adopted June 30, 2003);
- projected salary increases of 4% compounded annually, attributable to inflation (adopted June 30, 2003);

- additional projected salary increases ranging from 0.00% to 11.96% per year attributable to seniority and merit (adopted June 30, 2003);
- post-retirement benefit increases ranging from 3% to 4% per year depending on the system (adopted June 30, 2003);
- rates of mortality, termination of service, disablement and retirement based on actual experience during the period from 1981 through 2002 (adopted June 30, 2003); and
- an increase in the aggregate active member payroll of 4% annually (adopted June 30, 2003).

## OTHER SUPPLEMENTARY INFORMATION

### FUND BALANCE ACCOUNTS

As provided by law, all System assets must be credited, according to the purpose for which they are held, to either the Annuity Savings Fund, the Accumulation Fund or the Expense Fund. These funds are classified as accounts for financial reporting purposes and are further explained as follows:

#### **A. Annuity Savings Fund**

Members' contributions together with interest thereon, at statutory interest rates, are credited to the Annuity Savings Fund. Upon retirement, members' accumulated contributions and interest are transferred from the Annuity Savings Fund to the Accumulation Fund.

#### **B. Accumulation Fund**

Contributions made by employers, other contributions and investment income are credited to the Accumulation Fund. All retirement, disability and death benefits are paid from this Fund.

#### **C. Expense Fund**

All expenses for the administration and operation of the System are recorded in the Expense Fund. During the year, funds are transferred from the Accumulation Fund to the Expense Fund to cover expenses incurred.

## STATE RETIREMENT AND PENSION SYSTEM OF MARYLAND

### SCHEDULE OF FUND BALANCES

for the Fiscal Year Ended June 30, 2006 (with Comparative 2005 Totals)

*(Expressed in Thousands)*

	Annuity Savings Fund	Accumulation Fund	Expense Fund	Totals	
				2006	2005
<b>Fund Balances, Beginning of Year</b>	\$2,148,063	\$29,925,656	\$ -	\$32,073,719	\$30,166,724
<b>Additions</b>					
Net investment income	-	3,292,118	(66,469)	3,225,649	2,766,389
Contributions (note 4):					
Employers	-	285,275	-	285,275	239,855
Members	215,077	-	-	215,077	208,997
Other	-	431,415	-	431,415	426,191
Contribution interest	-	4,186	-	4,186	4,508
<b>Deductions</b>					
Benefit payments	-	(1,829,468)	-	(1,829,468)	(1,697,397)
Refunds (note 6)	(17,089)	634	-	(16,455)	(19,162)
Administrative expenses (note 2E)	-	-	(18,579)	(18,579)	(22,386)
<b>Transfers</b>					
From the Accumulation Fund to the Annuity Savings Fund for interest credited to members' accounts	92,783	(92,783)	-	-	-
To the Accumulation Fund from the Annuity Savings Fund for contributions of retiring members	(188,285)	188,285	-	-	-
From the Accumulation Fund to the Expense Fund for administrative and investment expenses	-	(85,048)	85,048	-	-
Net changes in fund balances	102,486	2,194,614	-	2,297,100	1,906,995
<b>Fund Balances, End of Year</b>	<u>\$2,250,549</u>	<u>\$32,120,270</u>	<u>\$ -</u>	<u>\$34,370,819</u>	<u>\$32,073,719</u>

SCHEDULE OF ADMINISTRATIVE EXPENSES  
for the Fiscal Years Ended June 30, 2006 and 2005  
(Expressed in Thousands)

	<b>2006</b>	<b>2005</b>
<b>Personnel services:</b>		
Staff salaries	\$ 9,613	\$ 9,231
Fringe benefits	<u>3,048</u>	<u>2,617</u>
Total personnel services	<u>12,661</u>	<u>11,848</u>
<b>Professional and contractual services:</b>		
Actuarial	275	126
Legal and financial	405	476
Consulting services	21	57
Data processing	964	1,621
Other contractual services	<u>386</u>	<u>448</u>
Total professional and contractual services	<u>2,051</u>	<u>2,728</u>
<b>Miscellaneous:</b>		
Communications	1,309	935
Rent	1,591	5,563
Equipment and supplies	336	615
Other	<u>631</u>	<u>697</u>
Total miscellaneous	<u>3,867</u>	<u>7,810</u>
<b>Total Administrative Expenses</b>	<u><u>\$18,579</u></u>	<u><u>\$22,386</u></u>

SCHEDULE OF INVESTMENT EXPENSES  
for the Fiscal Years Ended June 30, 2006 and 2005  
(Expressed in Thousands)

	<b>2006</b>	<b>2005</b>
<b>Investment advisors:</b>		
Equity managers	\$43,271	\$36,625
Fixed managers	9,975	9,090
Real estate managers	<u>11,061</u>	<u>9,505</u>
Total investment advisory fees	<u>64,307</u>	<u>55,220</u>
<b>Other investment service fees</b>		
Master custody	1,042	964
Income verification services	295	295
Investment consultant	504	460
Other investment expenses	<u>321</u>	<u>271</u>
Total other investment service fees	<u>2,162</u>	<u>1,990</u>
<b>Total Investment Expenses</b>	<u><u>\$66,469</u></u>	<u><u>\$57,210</u></u>

**STATE RETIREMENT AND**  
**SCHEDULE OF PLAN NET**  
as of June 30, 2006  
*(Expressed in Thousands)*

	<u>Teachers' Retirement and Pension Systems</u>	<u>Employees' Retirement and Pension Systems</u>	<u>Judges' Retirement System</u>
<b>Assets:</b>			
<b>Cash and cash equivalents</b> (Note 3)	\$ 830,493	\$ 492,934	\$ 16,876
<b>Receivables:</b>			
Contributions			
Employers	1	4,977	12
Employers - Long Term (Note 5)	-	59,415	-
Members	343	621	-
Accrued investment income	36,513	20,565	448
Investment sales proceeds	356,474	200,117	4,372
Due from other systems	77	3,759	-
Total receivables	<u>393,408</u>	<u>289,454</u>	<u>4,832</u>
<b>Investments, at fair value</b> (Notes 2 & 3):			
U.S. Government obligations	1,012,511	567,879	12,418
Domestic corporate obligations	4,082,834	2,291,194	50,076
International obligations	115,656	64,876	1,419
Domestic stocks	9,076,952	5,153,111	111,355
International stocks	4,244,195	2,409,486	52,068
Mortgages & mortgage related securities	1,301,458	731,362	15,963
Real estate	505,683	287,087	6,203
Alternative investments	173,722	98,625	2,131
Collateral for loaned securities	1,305,371	732,134	16,010
Total investments	<u>21,818,382</u>	<u>12,335,754</u>	<u>267,643</u>
Inter-fund transfers	(768)	645	(9)
<b>Total assets</b>	<u>23,041,515</u>	<u>13,118,787</u>	<u>289,342</u>
<b>Liabilities:</b>			
Accounts payable & accrued expenses	38,579	23,668	546
Investment commitments payable	955,015	537,359	11,714
Obligation for collateral loaned securities	1,305,371	732,134	16,010
Other liabilities	890	505	11
Due to other systems	142	3,755	-
<b>Total liabilities</b>	<u>2,299,997</u>	<u>1,297,421</u>	<u>28,281</u>
<b>Net assets held in trust for pension benefits</b> (A schedule of funding progress is presented on page 35)	<u>\$20,741,518</u>	<u>\$11,821,366</u>	<u>\$ 261,061</u>

\* Intersystem transfers have been eliminated in the financial statements.

**PENSION SYSTEM OF MARYLAND**

ASSETS BY SYSTEM

<u>State Police Retirement System</u>	<u>Local Fire and Police System</u>	<u>Law Enforcement Officers' Pension System</u>	<u>Subtotal</u>	<u>Eliminations*</u>	<u>Combined Total</u>
\$ 59,315	\$ 876	\$ 17,298	\$ 1,417,792	\$ -	\$ 1,417,792
302	-	696	5,988	-	5,988
-	-	-	59,415	-	59,415
-	4	23	991	-	991
2,089	5	582	60,202	-	60,202
20,259	44	5,714	586,980	-	586,980
-	-	61	3,897	(3,897)	-
<u>22,650</u>	<u>53</u>	<u>7,076</u>	<u>717,473</u>	<u>(3,897)</u>	<u>713,576</u>
57,428	122	16,255	1,666,613	-	1,666,613
231,851	499	65,485	6,721,939	-	6,721,939
6,562	14	1,856	190,383	-	190,383
528,295	1,413	142,750	15,013,876	-	15,013,876
247,022	661	66,748	7,020,180	-	7,020,180
74,125	164	20,826	2,143,898	-	2,143,898
29,428	78	7,950	836,429	-	836,429
10,111	27	2,732	287,348	-	287,348
74,039	157	20,957	2,148,668	-	2,148,668
<u>1,258,861</u>	<u>3,135</u>	<u>345,559</u>	<u>36,029,334</u>	<u>-</u>	<u>36,029,334</u>
190	6	(64)	-	-	-
<u>1,341,016</u>	<u>4,070</u>	<u>369,869</u>	<u>38,164,599</u>	<u>(3,897)</u>	<u>38,160,702</u>
2,311	13	625	65,742	-	65,742
54,541	124	15,249	1,574,002	-	1,574,002
74,039	157	20,957	2,148,668	-	2,148,668
51	-	14	1,471	-	1,471
-	-	-	3,897	(3,897)	-
<u>130,942</u>	<u>294</u>	<u>36,845</u>	<u>3,793,780</u>	<u>(3,897)</u>	<u>3,789,883</u>
<u>\$ 1,210,074</u>	<u>\$ 3,776</u>	<u>\$ 333,024</u>	<u>\$ 34,370,819</u>	<u>\$ -</u>	<u>\$34,370,819</u>

**STATE RETIREMENT AND  
SCHEDULE OF CHANGES IN**  
for the Fiscal Year Ended  
(Expressed in Thousands)

	<b>Teachers' Retirement and Pension Systems</b>	<b>Employees' Retirement and Pension Systems</b>	<b>Judges' Retirement System</b>
<b>Additions:</b>			
<b>Contributions</b> (note 4):			
Employers	\$ 10,811	\$ 217,747	\$ 14,277
Members	118,531	83,600	1,502
Other	431,250	-	165
Contribution interest	-	4,186	-
Total contributions	<u>560,592</u>	<u>305,533</u>	<u>15,944</u>
<b>Investment income:</b>			
Net appreciation (depreciation) in fair value of investments	1,699,380	960,566	20,369
Interest	145,861	86,755	2,140
Dividends	121,352	68,847	1,455
Real estate operating net income	20,261	11,491	245
Income before securities lending activity	<u>1,986,854</u>	<u>1,127,659</u>	<u>24,209</u>
Gross income from securities lending activity	50,430	29,171	601
Securities lending borrower rebates	(46,281)	(26,784)	(551)
Securities lending agent fees	(673)	(388)	(8)
Net income from securities lending activity	<u>3,476</u>	<u>1,999</u>	<u>42</u>
Total investment income	<u>1,990,098</u>	<u>1,129,658</u>	<u>24,251</u>
<b>Less investment expenses</b>			
Investment advisory fees	(39,536)	(22,420)	(476)
Other investment expenses	(580)	(520)	(2)
Total investment expenses	<u>(40,116)</u>	<u>(22,940)</u>	<u>(478)</u>
Net investment income	<u>1,950,214</u>	<u>1,106,718</u>	<u>23,773</u>
Transfers from other systems	<u>439</u>	<u>9,285</u>	<u>2</u>
Total additions	<u>2,511,245</u>	<u>1,421,536</u>	<u>39,719</u>
<b>Deductions:</b>			
Benefit payments	1,110,016	608,037	18,766
Refunds (note 6)	7,499	8,322	-
Administrative expenses (note 2E)	9,627	8,605	27
Transfers to other systems	457	7,248	-
<b>Total deductions</b>	<u>1,127,599</u>	<u>632,212</u>	<u>18,793</u>
<b>Net increase (decrease) in plan assets</b>	1,384,414	788,679	20,935
<b>Net assets held in trust for pension benefits:</b>			
Beginning of the fiscal year	19,357,872	11,032,042	240,135
End of the fiscal year	<u>\$ 20,741,518</u>	<u>\$ 11,821,366</u>	<u>\$ 261,061</u>

\* Intersystem due from/due to have been eliminated in the financial statements

**PENSION SYSTEM OF MARYLAND**

**PLAN NET ASSETS BY SYSTEM**

June 30, 2006

State Police Retirement System	Local Fire and Police System	Law Enforcement Officers' Pension System	Subtotal	Eliminations*	Combined Total
\$ 6,681	\$ 542	\$ 35,217	\$ 285,275	\$ -	\$ 285,275
6,438	-	5,006	215,077	-	215,077
-	-	-	431,415	-	431,415
-	-	-	4,186	-	4,186
<u>13,119</u>	<u>542</u>	<u>40,223</u>	<u>935,953</u>	<u>-</u>	<u>935,953</u>
99,742	668	24,129	2,804,854	-	2,804,854
9,559	117	2,920	247,352	-	247,352
7,154	47	1,778	200,633	-	200,633
1,179	7	313	33,496	-	33,496
<u>117,634</u>	<u>839</u>	<u>29,140</u>	<u>3,286,335</u>	<u>-</u>	<u>3,286,335</u>
3,073	22	825	84,122	-	84,122
(2,822)	(20)	(760)	(77,218)	-	(77,218)
(41)	-	(11)	(1,121)	-	(1,121)
<u>210</u>	<u>2</u>	<u>54</u>	<u>5,783</u>	<u>-</u>	<u>5,783</u>
<u>117,844</u>	<u>841</u>	<u>29,194</u>	<u>3,292,118</u>	<u>-</u>	<u>3,292,118</u>
(2,309)	(10)	(597)	(63,348)	-	(63,348)
(8)	-	(11)	(1,121)	-	(1,121)
<u>(2,317)</u>	<u>(10)</u>	<u>(608)</u>	<u>(66,469)</u>	<u>-</u>	<u>(66,469)</u>
<u>115,527</u>	<u>831</u>	<u>28,586</u>	<u>3,225,649</u>	<u>-</u>	<u>3,225,649</u>
85	4	2,905	12,720	(12,720)	-
<u>128,731</u>	<u>1,377</u>	<u>71,714</u>	<u>4,174,322</u>	<u>(12,720)</u>	<u>4,161,602</u>
72,520	231	19,898	1,829,468	-	1,829,468
312	-	322	16,455	-	16,455
137	6	177	18,579	-	18,579
-	4,979	36	12,720	(12,720)	-
<u>72,969</u>	<u>5,216</u>	<u>20,433</u>	<u>1,877,222</u>	<u>(12,720)</u>	<u>1,864,502</u>
55,572	(3,845)	51,345	2,297,100	-	2,297,100
<u>1,154,312</u>	<u>7,615</u>	<u>281,743</u>	<u>32,073,719</u>	<u>-</u>	<u>32,073,719</u>
<u>\$ 1,210,074</u>	<u>\$ 3,776</u>	<u>\$ 333,024</u>	<u>\$34,370,819</u>	<u>\$ -</u>	<u>\$ 34,370,819</u>



This page intentionally left blank

## **STATE POLICE RETIREMENT SYSTEM**

The General Assembly added a third benefit system, the State Police Retirement System, in 1949. Membership in the police system is restricted to uniformed employees of the Maryland State Police. The mission of the Maryland State Police is to fulfill its role as the state's lead coordinating law enforcement organization with commitment to pride, equality, respect and dignity. More than 1,400 officers throughout 23 counties strive to improve the quality of life for the citizens of Maryland by ensuring public safety.

## CHIEF INVESTMENT OFFICERS REPORT

### OVERVIEW

The State Retirement and Pension System (“SRPS” or the “System”) returned 10.4 percent for the fiscal year ended June 30, 2006 and the market value of the System’s assets increased from \$32.1 billion on June 30, 2005 to \$34.4 billion on June 30, 2006. This was the third straight year of strong returns, with domestic equity achieving a high single digit return, and international equity, real estate, and private equity each recognizing double digit returns.

The domestic equity market continued to perform well despite ongoing economic uncertainty and rising short-term interest rates. The System’s U.S. public equity portfolio earned 9.0 percent. For the current fiscal year, the Wilshire 5000 stock index returned 9.9 percent, an increase of 1.7 percent over last fiscal year. Domestic equities underperformed international equities due to concerns regarding the domestic economy and relative valuation levels.

For the fiscal year, the international equities market returned 27.9 percent, as measured by the Morgan Stanley Capital International All Country World ex U.S. index (MSCI ACWI ex US). International equity was the System’s top performing asset class, earning a 28.2 percent return. This has been a durable asset class in the face of pressure stemming from inflation concerns, rising interest rates, and high oil prices. Many international economies have improved; in particular, the Japanese economy showed signs of improved growth after years of slow growth.

Private equity also had a very positive year, returning 22.7 percent, exceeding the System’s benchmark for private equity (Russell 3000 + 400 basis points) of 13.6 percent. The System’s private equity program continues to move toward the 2 percent strategic target approved by the Board of Trustees of the System (“Board of Trustees”) in 2004.

Generally, it was a challenging environment for fixed income securities, as the Federal Open Market Committee continued to tighten monetary policy and inflation trended upward. As such, U.S. government yields rose significantly across the maturity spectrum. The System’s fixed income return of -0.2 percent is comparable to the overall fixed income market, as measured by the Lehman Brothers U.S. Universal Bond Index, which returned -0.3 percent.

Despite a weakening U.S. housing market, real estate had another successful year with double digit returns. The System’s real estate program posted very strong results, return-

ing 23.8 percent for the fiscal year. Performance for the National Council of Real Estate Investment Fiduciaries Property Index was 20.2 percent and the Wilshire Real Estate Securities Index was 21.9 percent.

During fiscal year 2006, the fiscal year 2005 changes to the strategic asset allocation authorized by the Board of Trustees were implemented. Global equity, small cap international equity, enhanced index equity, and real return fixed income mandates were funded. Additionally, the Board-approved Tactical Asset Allocation program was utilized. The Tactical Asset Allocation program is designed to provide flexibility in adjusting asset classes for tactical rebalancing. The Tactical Asset Allocation program returned 11 basis points at the total plan level during the 2006 fiscal year.

### INVESTMENT POLICY AND OBJECTIVES

The Board of Trustees is charged with the responsibility of managing the assets of the State Retirement and Pension System. The Board of Trustees is required to exercise its fiduciary duties solely in the interest of the participants, with the care, skill and diligence that a prudent person would exercise under similar circumstances. This standard of care not only permits but also encourages diversifying investments across various asset classes.

Investment objectives are designed to support fulfillment of the Agency’s mission, which is to optimize risk-adjusted returns in order to ensure that sufficient assets are available to fund the payment of benefits to members and beneficiaries when due. SRPS is a long-term investor, and consequently, long-term results are emphasized, with recognition that short-term results may be volatile.

Investment objectives are implemented according to investment policies developed by the Board of Trustees. The “prudent person standard” allows the Board of Trustees to establish investment policies based on investment criteria that it defines, and it provides for the delegation of investment authority to investment professionals. System assets are managed by external investment management firms who employ both active and passive strategies. Firms retained must have a demonstrated performance record, and a clearly defined and consistently applied investment process.

The Board of Trustees has managed the SRPS’ assets with the goal of achieving an annualized investment return that over a longer term timeframe:

1. **Meets or exceeds the System's static investment policy benchmark.** The static policy benchmark is the weighted average of the benchmarks for each asset class, using the target weightings for each asset class. The static policy benchmark enables a comparison to be made of the System's actual performance to a passively managed proxy, and facilitates measurement of the value added from active management and policy implementation.
2. **Provides at least a 3 percent real rate of return (return in excess of U.S. inflation).** The inflation related objective compares the investment performance against the rate of inflation as measured by the Consumer Price Index (CPI) plus 3.0 percent. The inflation measure provides a link to SRPS' liabilities, as they are indexed to inflation through cost-of-living adjustments.
3. **Equals or exceeds the actuarial investment return assumption of the System adopted by the Board of Trustees.** The actuarial investment return assumption is reviewed and monitored as a measure of the expected long-term rate of growth of SRPS' assets. The actuarial return assumption as of June 30, 2006 was 7.75 percent. When adopting this actuarial assumption, the Board of Trustees anticipates, and fully expects, that the investment portfolio will achieve higher returns in some years and lower returns in other years.

The Board of Trustees also weighs three liability-oriented objectives when making asset allocation determinations. The liability-oriented objectives are:

1. To achieve and maintain a fully funded pension plan.
2. To minimize contribution volatility year to year.
3. To achieve surplus assets.

Asset allocation is a key determinant of a successful investment program, and may be responsible for determining as much as 90 percent of a fund's return in a given year. The Board of Trustees considers both the assets and liabilities when determining its asset allocation policy.

Asset allocation policy targets are determined by recognizing that liabilities (future benefit payments to SRPS' participants and beneficiaries) must be paid in full and on time. To ensure this, there is a dual focus. First, there is a focus on long-term return, to ensure an attractive rate of return

on plan assets can be earned over the period that benefits must be paid. Secondly, there is a focus on risk. This involves diversifying assets with a recognition that while individual asset classes can be volatile over short time horizons, diversification will often serve to lower overall portfolio volatility.

The SRPS portfolio continues to be well diversified. During the fiscal year, a 10 percent allocation to global equities and a 2 percent allocation to real return strategies were funded though a corresponding reduction in the allocation to domestic equities, international equities and fixed income.

As of June 30, 2006, the Board-approved policy targets and ranges were:

ASSET CLASS	TARGET	RANGE
U.S. Equity	40%	35 - 45%
Non-U.S. Equity	13%	10 - 16%
Global Equity	10%	8 - 12%
Private Equity	2%	0 - 3%
<b>Total Equity</b>	<b>65%</b>	<b>60 - 70%</b>
Fixed Income	28%	23 - 33%
Real Estate	5%	3 - 7%
Real Return	2%	1 - 3%
<b>Total Assets</b>	<b>100%</b>	

#### INVESTMENT PERFORMANCE

Investment performance is calculated using time-weighted rates of return. Total return includes interest and dividends, as well as capital appreciation.

The investment program realized a return of 10.4 percent for fiscal year 2006. Annualized returns for the 3, 5, and 10-year periods ending June 30 were 12.0 percent, 6.0 percent and 7.3 percent, respectively.

The System attained all three of its broad investment objectives this fiscal year -- exceeding a 3.0 percent real rate of return (after inflation), exceeding the actuarial assumed rate of 7.75 percent, and exceeding the return of the static policy benchmark by 0.2 percent.

Returns and Exposures were as follows:

	FY 2006 SRPS Performance	FY 2005 Benchmark Performance	SRPS Exposure June 30, 2006
<b>Public Equity</b>	14.4%		64.5%
<b>U.S. Equity</b>	9.0%		40.1%
Wilshire 5000		9.9%	
S&P 500		8.6%	
Russell 3000		9.6%	
<b>International Equity</b>	28.2%		13.1%
MSCI ACWI Ex. US		27.9%	
MSCI EAFE		26.6%	
<b>Global Equity</b> <sup>1</sup>	N/A		
MSCI AC World		18.0%	10.6
<b>Private Equity</b>	22.7%		0.7%
Russell 3000+400 bps		13.6%	
<b>Fixed Income</b>	-0.2%		28.3%
Lehman Brothers Universal Bond Index		-0.3%	
Lehman Brothers Aggregate Bond Index		-0.8%	
<b>Real Estate</b>	23.8%		5.3%
NCREIF Property (1 quarter lag)		20.2%	
Wilshire Real Estate Securities		21.9%	
<b>Real Return</b>	N/A		1.9%
Lehman Brothers U.S. TIPS		-1.6%	
<b>TOTAL FUND</b>	10.4%	10.2%	100%

<sup>1</sup> Global Equity inception date was October 1, 2005. Therefore, fiscal year 2006 performance figures are not shown. During the period January 1, 2006 – June 30, 2006, (a) Global Equity returned 7.7% and (b) the benchmark (MSCI ACWI) return was 6.1%.

## ECONOMIC AND CAPITAL MARKET OVERVIEW

U.S. economic growth was moderate during fiscal year 2006. The impact of higher energy prices, persistent Federal Reserve tightening, and a declining housing market did not slow the U.S. economy as much as some economists expected. On a year-over-year basis, U.S. real GDP grew in excess of 3.0 percent. Inflation remained reasonably well contained. Overall consumer price inflation each quarter of fiscal year 2006 was close to 4.0 percent (year-over-year) and core consumer price inflation was over 2.0 percent (year-over-year).

Throughout the 2006 fiscal year, the Federal Open Market Committee maintained its measured pace of increasing the target on the federal funds rate. At the beginning of the fiscal year, the benchmark rate stood at 3.25 percent. This rate was gradually increased by 25 basis points at each meeting during the fiscal year, resulting in a rate of 5.25 percent at June 30, 2006.

In fiscal year 2006, global equity markets were more volatile than in preceding years but volatility remained contained. In general, smaller cap stocks outperformed larger cap stocks and value stocks outperformed growth stocks. As a result of a slight rise in inflation, commodity producing countries performed well. A weaker dollar spurred cross-border mergers and acquisitions. European equities offered better value than U.S. equities as a result of the superior yield on European stocks and lower valuations. Overall, emerging markets also had a good year, although several markets suffered a correction in the first quarter of 2006, after several years of strong gains.

The yield curve finished the 2006 fiscal year essentially flat, with a yield differential between 2-year and 30-year Treasury securities of just 4 basis points. At the end of December 2005, for the first time in nearly five years, the Treasury yield curve inverted.

## PUBLIC EQUITY

As of June 30, 2006, SRPS had \$21.9 billion invested in public equities, representing 63.8 percent of the System's total assets. Public equity investments increased by \$1.2 billion over the fiscal year due to a shift in asset allocation and market appreciation. Funding for the global, small cap international and enhanced index equity mandates was completed during the year, leading to a planned decrease in U.S. exposure on a percentage basis. U.S. equities (including the new enhanced index equity allocation) totaled \$13.7 billion, a decrease of \$1.8 billion from the previous year. International equities totaled \$4.5 billion, a

U.S. Equity	\$ Millions	% of Total Plan
Passively Managed		
Equity Growth	774.7	2.25%
Russell 3000	8,656.9	25.18%
Total Passive	\$9,431.6	27.44%
Actively Managed		
Enhanced Equity	1,282.8	3.73%
Large cap value	877.6	2.55%
Large cap growth	929.5	2.70%
Large cap core	293.1	0.85%
Small cap growth	104	0.30%
Small cap value	180.6	0.53%
Micro cap	649.8	1.89%
Total Active	\$4,317.5	12.56%
<b>Total U.S. Equity</b>	<b>\$13,749.1</b>	<b>40.0%</b>

decrease of \$0.6 billion. The newly funded global equity allocation totaled \$3.7 billion at year end. Public equity assets were placed with 18 external managers and broadly diversified among the major countries and industrial sectors of the developed and emerging markets. The managers use active and passive strategies, and are expected to outperform their assigned benchmark, net of fees.

## U.S. EQUITIES

As of June 30, 2006, passively managed U.S. equity assets totaled \$9.4 billion and represented 27.4 percent of the System's total assets. Actively managed assets totaled \$4.3 billion and represented 12.6 percent of the System's total

assets. The U.S. equity allocation breakdown is as follows: U.S. equity returns are benchmarked against the Wilshire 5000 Free Float Index. For the fiscal year, the U.S. equity portfolio underperformed the benchmark by 90 basis points. The U.S. equity portfolio returned 9.0 percent for

International Equity	\$ Millions	% of Total Plan
Passively Managed		
Passively Managed		
MSCI AC World ex US	\$ 3,294.6	9.58%
Total Passive	3,294.6	9.58%
Actively Managed		
MSCI AC World ex US	847.2	2.47%
Small cap	354.5	1.03%
Total Active	1,201.9	3.50%
<b>Total International Equity</b>	<b>\$ 4,496.5</b>	<b>13.08%</b>

the fiscal year ended June 30, compared to a 9.9 percent return for the benchmark. For six and a half straight years, small capitalization stocks have outperformed their larger counterparts. Value stocks outpaced growth stocks, continuing a trend of the past several years.

## INTERNATIONAL EQUITIES

At the end of the fiscal year, \$4.5 billion, or 13.1 percent of the System's assets were invested in International Equities. The fund added two international small cap managers to the line-up during the course of the year to gain increased exposure to an attractive asset class. The international equity portfolios are managed externally by one passive manager, and three active managers.

International equity returns are benchmarked against the Morgan Stanley Capital International All Country World ex-U.S. Index. The international equity portfolio returned 28.2 percent in fiscal year 2006, outperforming the benchmark by 3 basis points. International equities were the top per-

Global Equity	\$ Millions	% of Total Plan
Actively Managed		
MSCI AC World	\$ 3,656.3	10.64%
<b>Total Global Equity</b>	<b>\$ 3,656.3</b>	<b>10.64%</b>

forming asset class for the fiscal year, led by strong gains in emerging countries including Russia, Brazil, China, Mexico, and developed countries including the United Kingdom, France and Japan. The addition of the two small cap international managers increased the System's exposure to a top performing asset class and aided performance meaningfully.

#### GLOBAL EQUITIES

The shift in asset allocation into Global Equities also benefited the System. Global equities totaled \$3.7 billion, or 10.6 percent of the System's total assets as of the fiscal year end. The Global Equity portfolio is managed by three active external managers.

Global Equity returns are benchmarked against the Morgan Stanley Capital International All Country World Index. The global equity portfolio returned 7.68 percent for the six months ending on June 30, outperforming the benchmark by 155 basis points. The global equity portfolio's out-performance was due, in part, to superior stock selection by the System's active managers.

#### PRIVATE EQUITY

The SRPS, with the assistance of the System's private equity consultant, continued to expand the System's private equity program in fiscal year 2006. In the fiscal year ending June 30, 2006, the SRPS made commitments to 11 funds totaling approximately \$198 million. This is in addition to commitments to nine funds totaling \$166 million in fiscal year 2005. As of June 30, 2006, the total market value of the private equity program was \$244 million.

For fiscal year 2007, we expect that the System's exposure to the private equity asset class will continue to increase toward the long-term targeted levels. The target allocation to this asset class is 2 percent with a range of 0-3 percent. At June 30, 2006, the actual allocation was 0.7 percent. Given the cash flow dynamics in private equity, it will take several more years for the target allocation to be reached.

#### FIXED INCOME

As of June 30, 2006 the SRPS had \$9.7 billion invested in the fixed income sector, representing approximately 28 percent of total assets. The objective of the fixed income portfolio is to outperform the Lehman Brothers U.S. Universal Index. Of the \$9.7 billion, \$4.5 billion (46 percent) is in strategies indexed to the Lehman Brothers U.S. Aggregate Index. The remaining \$5.2 billion is actively managed, by

four external managers, predominantly in core plus accounts, which seek to outperform their benchmarks through active management.

The SRPS fixed income portfolio returned -0.2 percent versus -0.3 percent for the Lehman Brothers U.S. Universal Index. Generally, the bond market environment was challenging, as the Federal Open Market Committee continued to tighten monetary policy and inflation trended upward. These factors placed downward pressure on bond prices, which, in turn, translated into significantly higher bond yields. Despite the relatively flat returns in the overall fixed income market, several sub-sectors performed relatively well, including emerging market debt (+8.1 percent) and high yield securities (+4.8 percent).

Although fiscal year 2006 was a difficult period for the bond market, fixed income securities typically provide more consistent, less volatile returns than equity markets. Given the lagging impact of monetary policy, it is widely anticipated that the Federal Open Market Committee is near or at the end of this tightening cycle. As such, the current and near-term market environments appear more favorable for fixed income returns. In addition, the System's active managers will continue to seek out undervalued bond sectors as well as individual securities to enhance returns.

#### REAL ESTATE

As of June 30, 2006, approximately 5.3 percent of System assets valued at \$1.8 billion were invested in a combination of real estate strategies: private market, direct equity; private market, indirect equity; and publicly traded. During fiscal year 2006, the Board of Trustees revised its Real Estate Investment Policy and Strategic Real Estate Investment Plan. As a result, the benchmark was modified from a 50 / 50 blend of the National Council of Real Estate Investment Fiduciaries Property Index ("NCREIF Property Index"), and the Wilshire Real Estate Securities Index ("WRESI") to a 70 / 30 weighted return of the NCREIF Property Index and the WRESI, respectively and net of fees. The objective is to achieve a total return that exceeds the benchmark return. The SRPS currently engages five external real estate managers toward meeting those objectives.

The SRPS real estate portfolio returned 23.8 percent versus 21.3 percent for the policy benchmark. The impressive returns in the real estate sector were attributed, in part, to healthy property market fundamentals, a compression of cap rates, and heavy capital flows. Demand remained very

strong, as the real estate sector provided investors with an opportunity to obtain greater diversification, as well as higher risk-adjusted returns, relative to other investment alternatives such as fixed income.

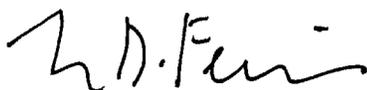
Based on the amount of committed but not yet invested capital, real estate returns appear supported in the near-term. Nonetheless, expectations for real estate returns must be tempered, as there are indications that transaction activity has slowed from its frenzied pace, appreciation gains have moderated, and higher long-term yields are placing upward pressure on cap rates.

#### REAL RETURN

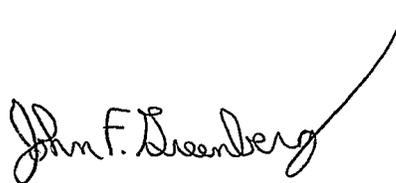
A real return mandate was funded during the year, with 2 percent of the System's assets placed in this strategy. Real return strategies, which generally invest in inflation protection securities, are largely utilized to protect investment returns against inflation, and provide diversification. These types of strategies are a good fit for portfolios like the System's, where benefits are inflation-adjusted.

The fiscal year ended June 30, 2006 was very positive, with strong investment returns and asset growth of \$2.3 billion. Stocks, bonds and real estate performed well, even though the economic environment was not always favorable. The diversification of the System's investment program was enhanced by the funding of the real return and global equity asset classes. We are proud of the System's recent strong investment performance, but cautious about returns going forward. The System has achieved returns of 10.4 percent, 9.5 percent and 16.2 percent over the past three years, but we do not anticipate that future returns will be as high. The investment program is well diversified and managed, and we expect it to generate good long-term returns.

Respectfully submitted,



Robert D. Feinstein  
Chief Operations Officer,  
Investment Division



John F. Greenberg, CFA  
Acting Chief Investment Strategist

INVESTMENT PORTFOLIOS BY MANAGER  
as of June 30, 2006  
(Expressed in Thousands)

	Fair Value	Investment Advisory Fee		Fair Value	Investment Advisory Fee
<b>Equity Managers</b>			<b>Fixed Income Managers</b>		
State Street Global Advisors	\$12,686,027	\$ 1,683	State Street Global Advisors	\$ 4,492,516	\$ 465
Templeton Investment Counsel, Inc.	1,545,559	2,190	Pacific Investment Management Company	2,433,669	4,061
Capital Guardian Trust Company	1,483,018	3,092	Western Asset Management	1,594,423	2,559
Wellington Management Co. LLP	926,600	2,832	Bridgewater Associates, Inc.	1,139,022	1,958
Dimensional Fund Advisors, Inc.	877,320	3,564	Payden & Rygel	672,406	932
Legg Mason Capital Management, Inc.	874,829	2,590	Internally Managed	4,783	N/A
Artisan Partners Limited Partnership	844,480	3,757	Other *	7	0
Acadian Asset Management	616,145	1,743		<u>\$10,336,826</u>	<u>\$ 9,975</u>
T. Rowe Price Associates, Inc.	602,106	1,383			
Payden & Rygel	430,154	99	<b>Real Estate Managers</b>		
Smith Breeden Associates	426,516	912	LaSalle Investment Management Securities, L.P.	\$ 975,377	\$ 1,862
Relational Investors, LLC	292,151	6,591	LaSalle Investment Management, Inc.	461,155	5,813
Private Equity Program	243,326	4,431	J.P. Morgan Investment Management, Inc.	331,448	2,454
GlobeFlex Capital, LP	123,846	376	Chesapeake Maryland Limited Partnership	22,339	225
Brown Investment Advisory & Trust Company	103,666	657	Lubert-Adler Management, Inc.	21,600	176
Internally Managed	29,086	N/A	Internally Managed	15,474	N/A
Other *	202	7,371	Prudential Investment/CIGNA	934	281
	<u>\$22,105,031</u>	<u>\$ 43,271</u>	Other *	0	250
				<u>\$ 1,828,327</u>	<u>\$ 11,061</u>

\* Consulting fees and investment managers no longer under contract as of 6/30/06.

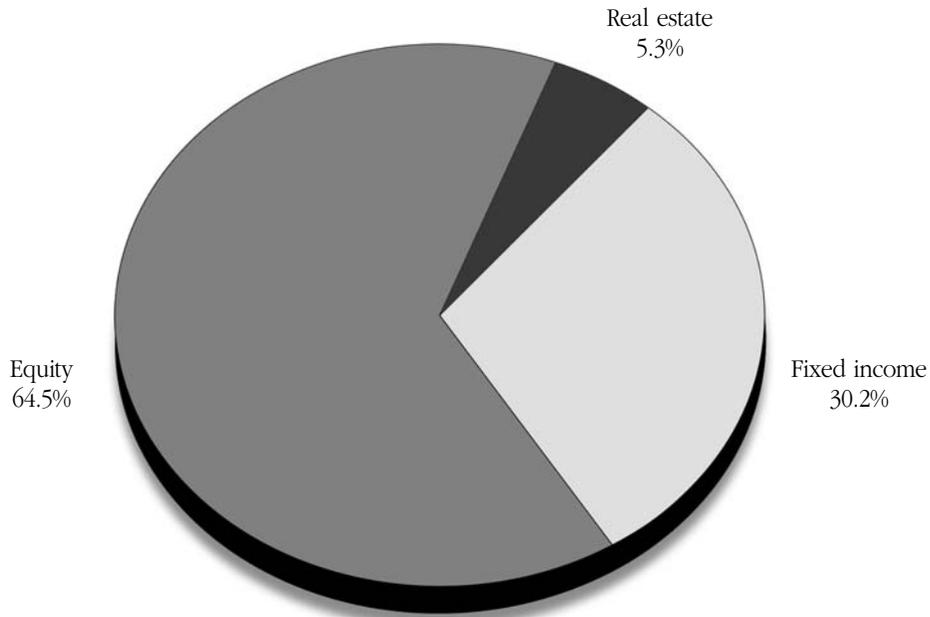
INVESTMENT PORTFOLIO SUMMARY  
as of June 30, 2006 and 2005  
(Expressed in Thousands)

	<u>2006</u>		<u>2005</u>	
	Fair Value	% of Fair Value	Fair Value	% of Fair Value
<b>Fixed Income</b>				
Domestic corporate obligations	\$ 6,411,213	18.6%	\$ 5,989,617	18.7%
Mortgages & mortgage related securities	1,800,338	5.3	1,746,849	5.5
U.S. Government obligations	1,666,613	4.9	1,761,411	5.5
International obligations	188,296	0.5	310,876	1.0
Domestic stocks	493	0.1	0	0.0
** Net cash & cash equivalents	<u>269,873</u>	<u>0.8</u>	<u>-334,296</u>	<u>-1.0</u>
* Total Fixed Income	<u><b>10,336,826</b></u>	<u><b>30.2</b></u>	<u><b>9,474,457</b></u>	<u><b>29.7</b></u>
<b>Equity</b>				
Domestic stocks	14,046,483	41.0	15,453,612	48.3
International stocks	7,047,192	20.6	4,982,880	15.6
Alternative investments	216,395	0.6	161,979	0.5
Fixed Income investments	656,373	1.9	0	0.0
** Net cash & cash equivalents	<u>138,588</u>	<u>0.4</u>	<u>268,503</u>	<u>0.8</u>
Total Equity	<u><b>22,105,031</b></u>	<u><b>64.5</b></u>	<u><b>20,866,974</b></u>	<u><b>65.2</b></u>
<b>Real Estate</b>				
Real Estate Investment Trusts	966,900	2.8	849,693	2.6
Pooled funds	332,393	1.0	304,379	1.0
Directly owned real estate	504,036	1.5	447,282	1.3
Alternative investments	43,941	0.1	80,527	0.3
** Net cash & cash equivalents	<u>-18,943</u>	<u>-0.1</u>	<u>-43,309</u>	<u>-0.1</u>
Total Real Estate	<u><b>1,828,327</b></u>	<u><b>5.3</b></u>	<u><b>1,638,572</b></u>	<u><b>5.1</b></u>
Total Portfolio	<u><b>\$34,270,184</b></u>	<u><b>100.0%</b></u>	<u><b>\$31,980,003</b></u>	<u><b>100.0%</b></u>

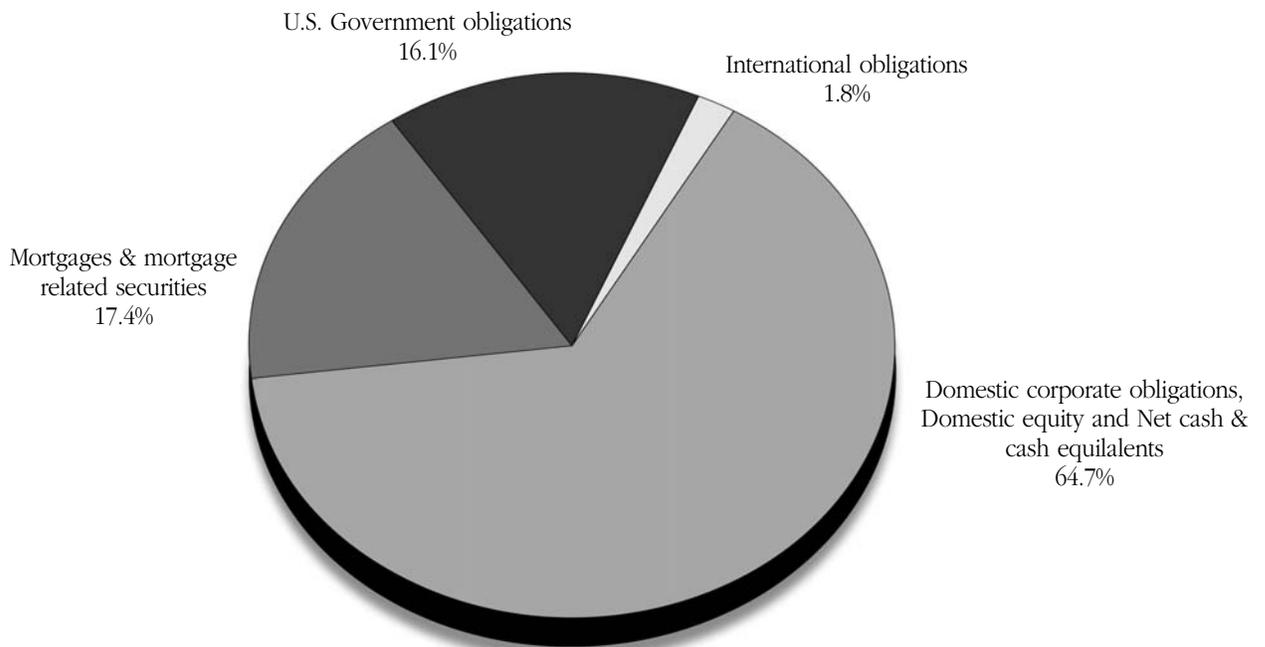
\* Security Lending collateral payable has been netted against the actual collateral. The amounts net to zero.

\*\* Includes investment receivables and payables.

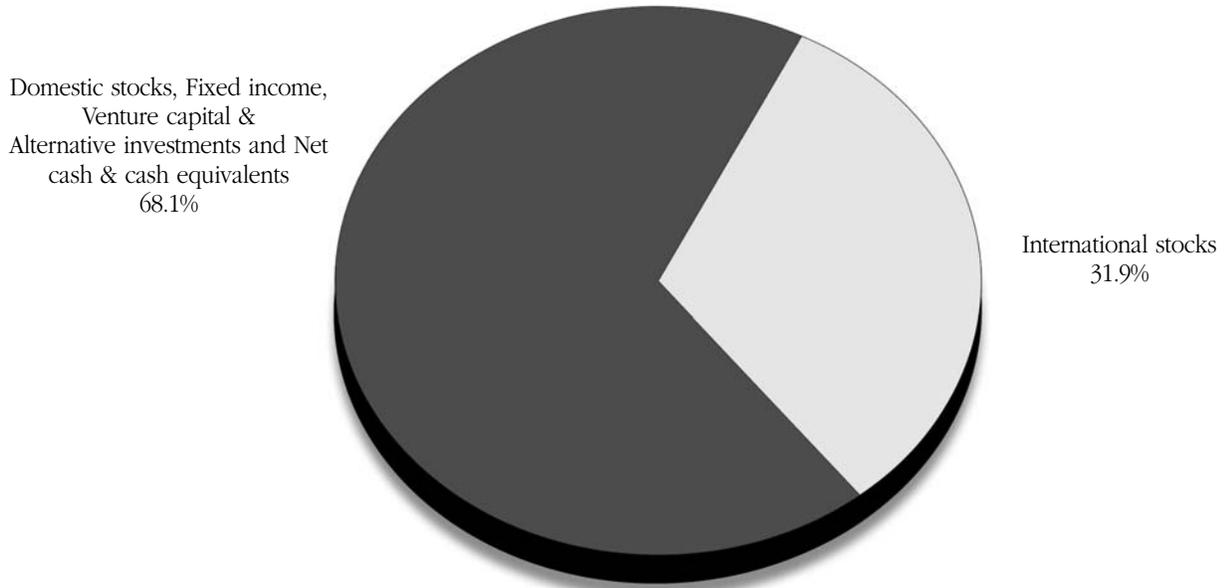
INVESTMENT PORTFOLIO ALLOCATION  
as of June 30, 2006



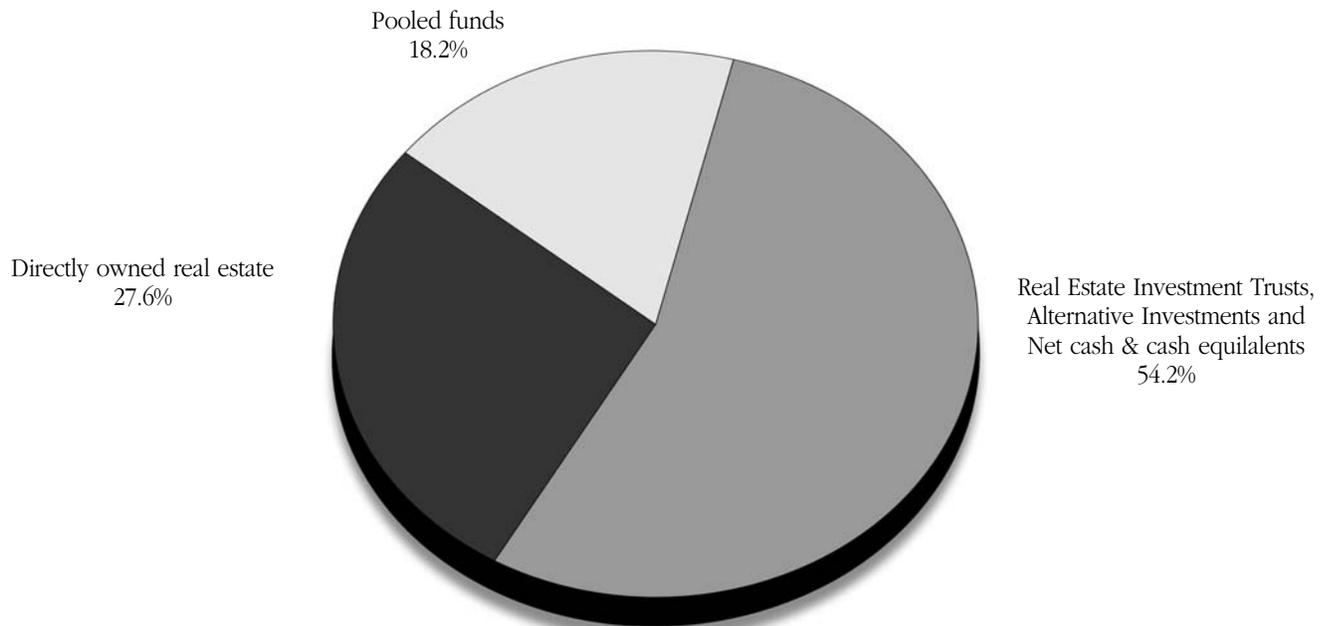
FIXED INCOME DISTRIBUTION BY TYPE  
as of June 30, 2006



**EQUITY DISTRIBUTION BY TYPE  
as of June 30, 2006**

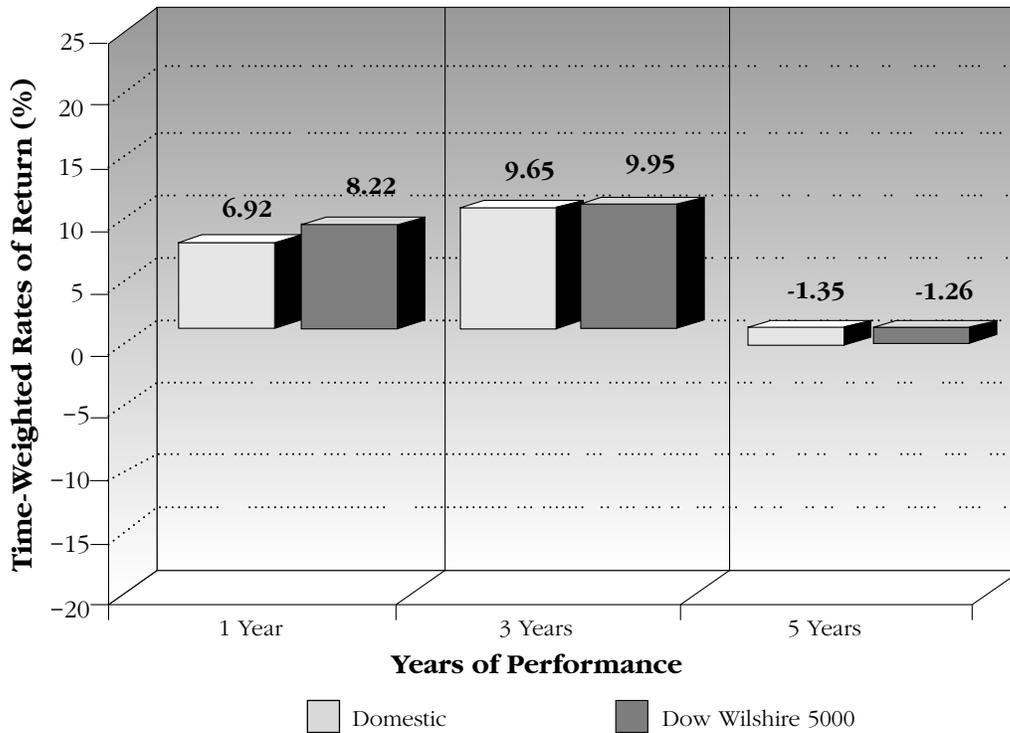


**REAL ESTATE DISTRIBUTION BY TYPE  
as of June 30, 2006**

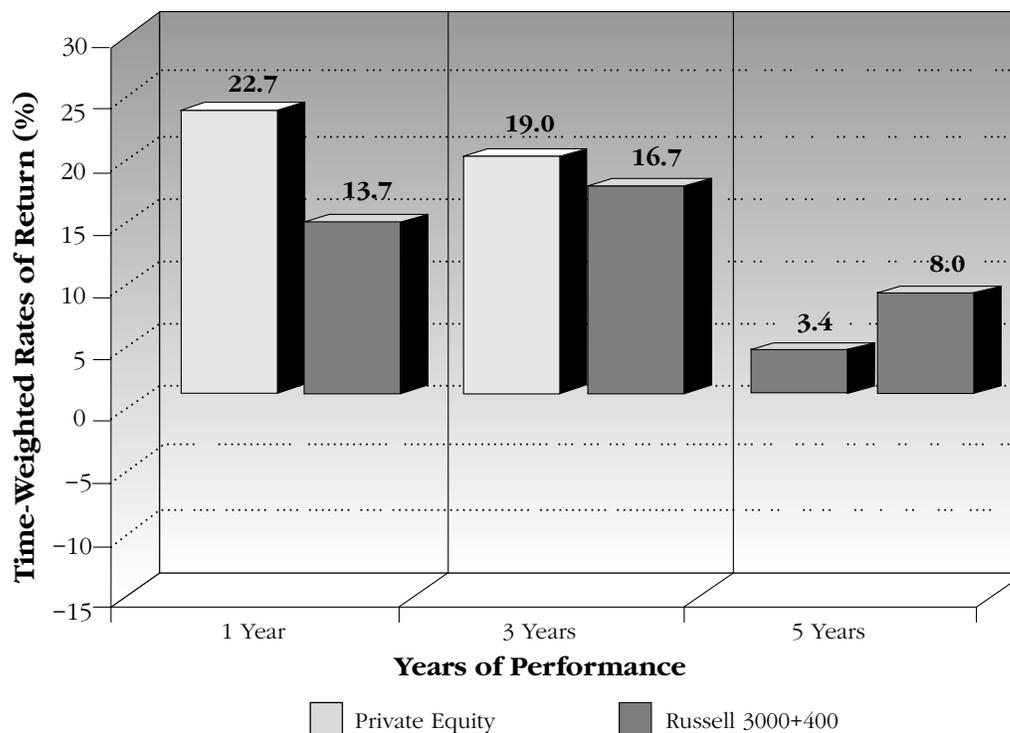


COMPARATIVE INVESTMENT RETURNS ENDING JUNE 30, 2006

DOMESTIC EQUITY

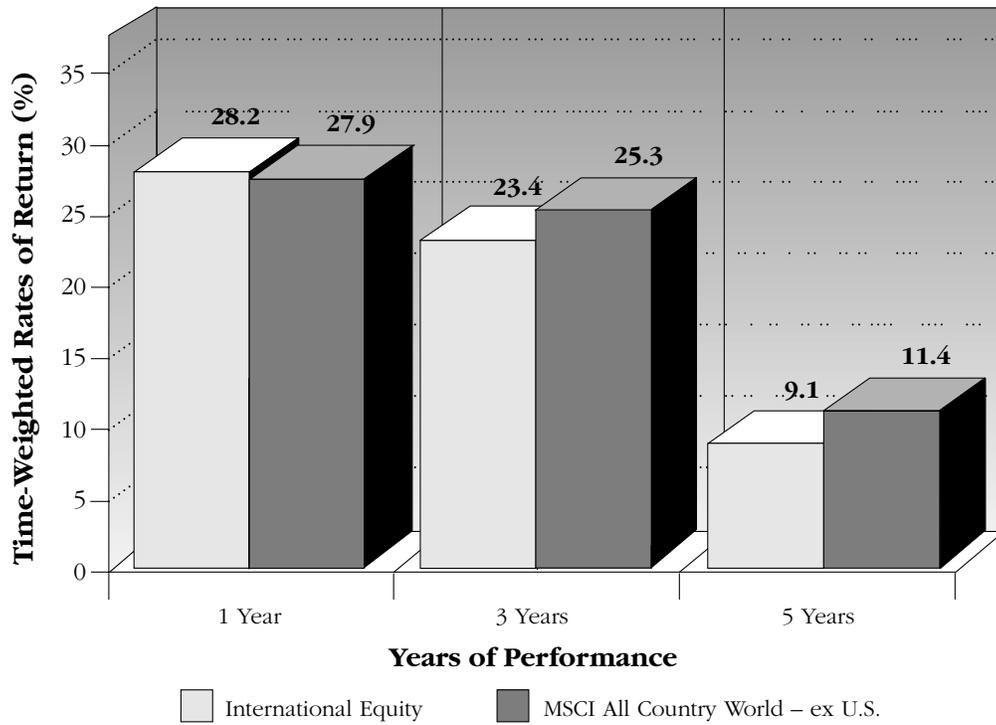


PRIVATE EQUITY

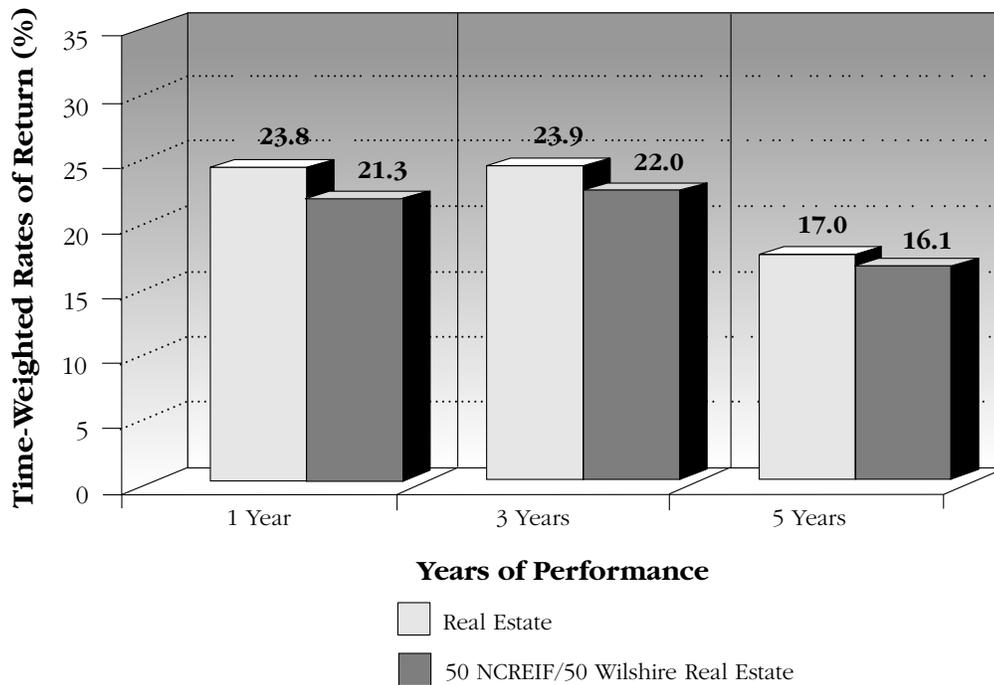


Comparative Investment Returns Ending June 30, 2006

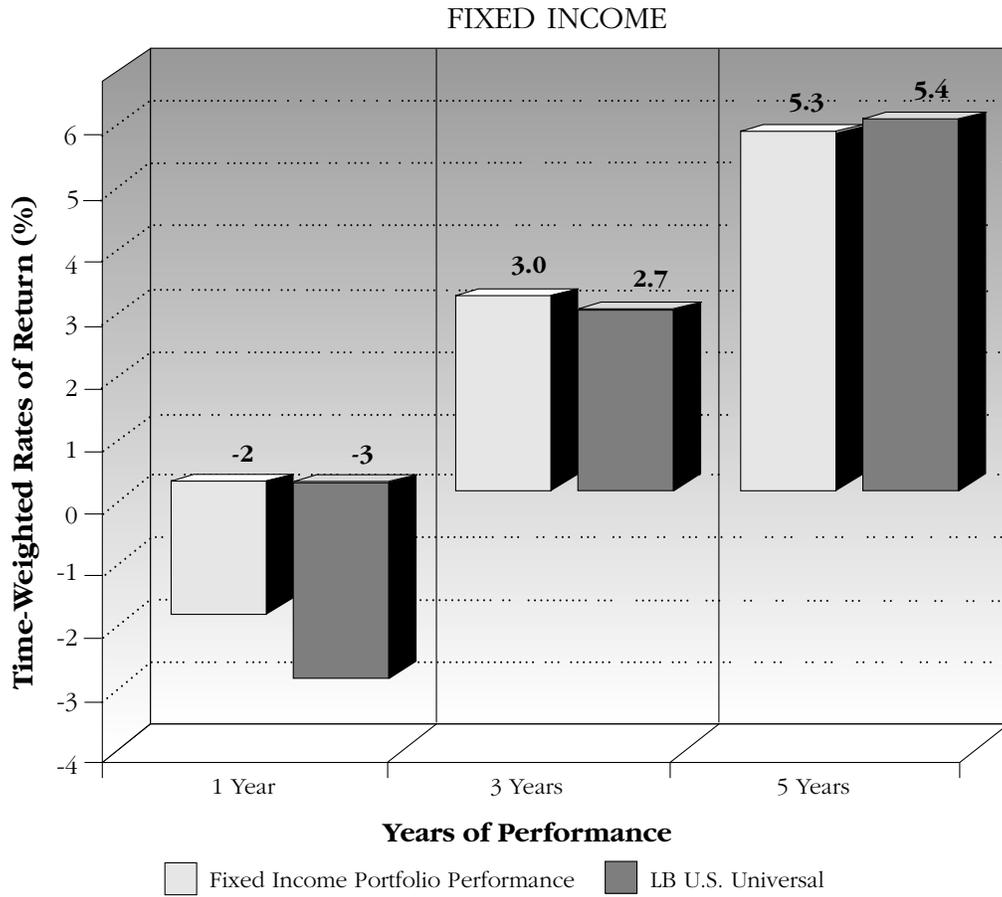
INTERNATIONAL EQUITY



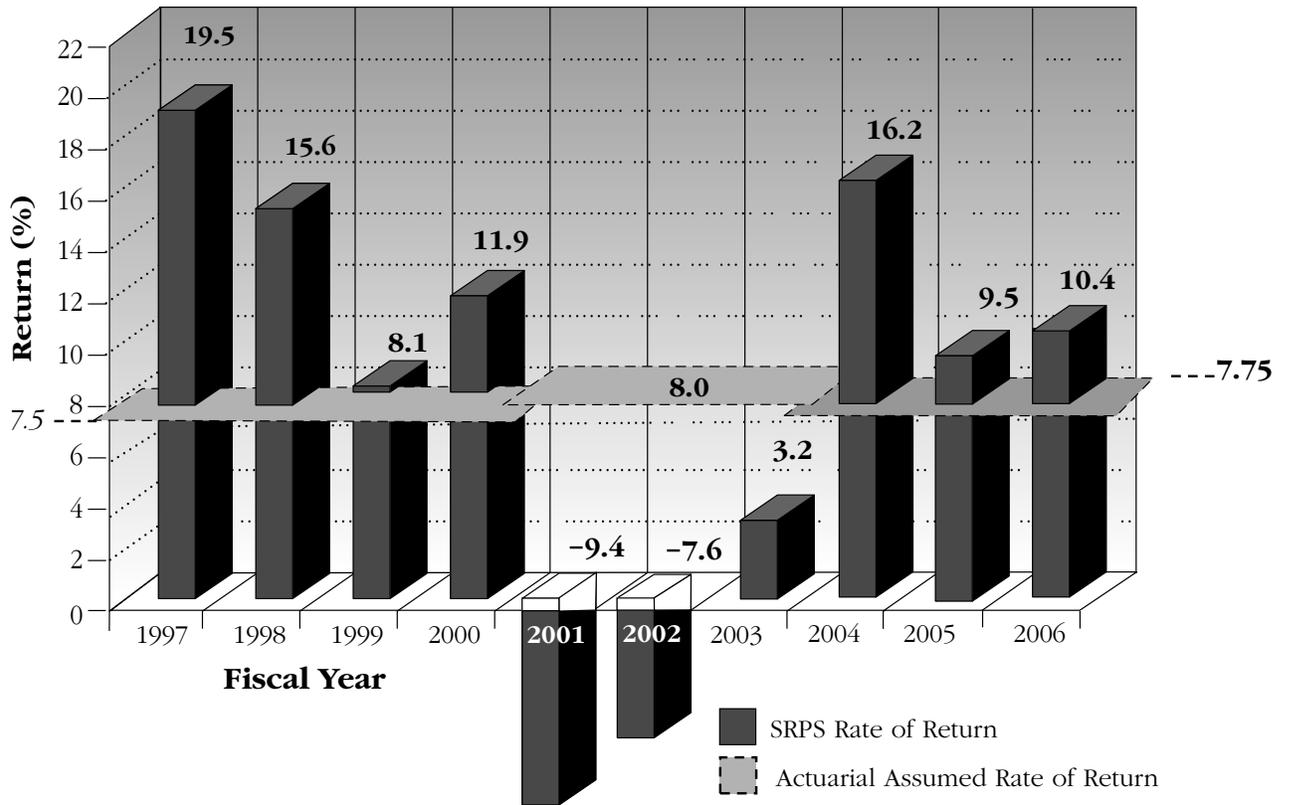
REAL ESTATE



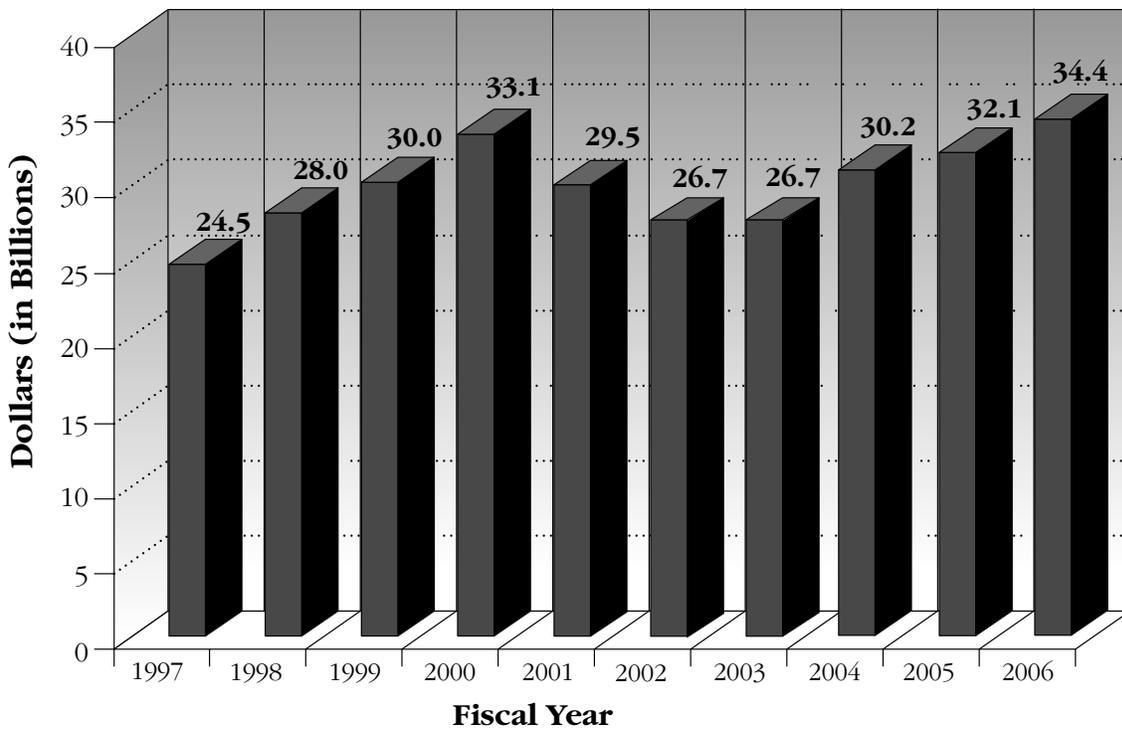
COMPARATIVE INVESTMENT RETURNS ENDING JUNE 30, 2006



TEN-YEAR HISTORY OF TIME-WEIGHTED ANNUAL RETURNS



TEN-YEAR GROWTH OF INVESTMENT PORTFOLIO



LARGEST 25 HOLDINGS  
as of June 30, 2006

<b>EQUITY INCOME SECURITIES:</b>	<b>No. of Shares</b>	<b>Fair Value</b>
Unitedhealth Group, Inc.	1,921,812	86,058,741
Tyco International Ltd.	3,074,223	84,541,133
Google, Inc.	184,428	77,336,193
Exxon Mobil Corporation	1,181,912	72,510,301
Cisco Systems, Inc.	3,542,775	69,190,396
Pfizer, Inc.	2,897,900	68,013,713
General Electric Company	2,055,894	67,762,266
Prudential Financial, Inc.	859,802	66,806,615
Astrazeneca PLC	1,084,160	64,854,451
J.P. Morgan Chase & Co.	1,490,700	62,609,400
Microsoft Corporation	2,601,165	60,607,145
Sprint Nextel Corporation	2,971,100	59,392,289
ING Group NV	1,391,012	54,656,905
Baxter International, Inc.	1,435,439	52,766,738
Medtronic, Inc.	1,105,658	51,877,473
Qwest Communications International, Inc.	6,402,544	51,796,581
Nestle SA	158,658	49,734,426
Time Warner, Inc.	2,848,930	49,286,489
AES Corporation	2,570,100	47,418,345
UBS AG	418,681	45,798,575
Amazon.Com, Inc.	1,165,300	45,073,804
National Semiconductor Corporation	1,856,073	44,267,341
Boeing Company	533,822	43,725,360
American International Group, Inc.	729,620	43,084,061
Countrywide Financial Corporation	1,131,158	43,074,497
TOTAL		<u>\$1,462,243,238</u>

<b>FIXED INCOME SECURITIES</b>	<b>Par</b>	<b>Fair Value</b>
Federal National Mortgage Assn., 0.01% due July 5, 2006	350,000,000	349,761,265
Federal National Mortgage Assn., TBA 5.0% due Dec. 1, 2099	270,840,000	253,171,915
Federal National Mortgage Assn., TBA 5.5% due Dec. 1, 2099	211,530,000	203,085,320
Federal National Mortgage Assn., TBA 6.0% due Dec. 1, 2099	120,590,000	118,658,679
Federal National Mortgage Assn., TBA 5.5% due Dec. 1, 2099	105,400,000	103,423,750
United States Treasury Notes, 1.875% due July 15, 2015	99,422,400	94,342,532
United States Treasury Notes, 1.875% due July 15, 2013	81,437,400	78,224,552
FNMA Pool 725946, 5.5% due Nov. 1, 2034	80,359,444	77,410,554
United States Treasury Notes, 4.5% due Nov. 15, 2010	75,000,000	73,260,000
Federal National Mortgage Assn., 0.01% due Aug. 1, 2006	72,900,000	72,577,534
United States Treasury Notes, 3.875% due Jan. 15, 2009	67,802,712	70,244,667
United States Treasury Bonds, 3.625% due April 15, 2028	57,292,080	67,980,634
United States Treasury Notes, 3.625% due Jan. 15, 2008	62,345,000	63,426,299
United States Treasury Bonds, 2.0% due Jan. 15, 2026	65,027,206	59,502,649
Countrywide Funding Repo, 5.15% due July 3, 2006	57,000,000	57,000,000
United States Treasury Notes, 4.25% due Jan. 15, 2010	53,161,008	56,479,419
United States Treasury Notes, 4.5% due Nov. 15, 2015	59,170,000	56,368,300
United States Treasury Notes, 3.0% due July 15, 2012	52,769,427	54,336,019
Federal National Mortgage Assn., TBA 6.5% due Dec. 1, 2099	53,940,000	54,218,125
Total Fina Elf Cap, 5.27% due July 3, 2006	52,800,000	52,784,541
United States Treasury Notes, 4.125% due Aug. 15, 2010	52,900,000	50,997,715
United States Treasury Bonds, 4.5% due Feb. 15, 2036	53,819,000	48,268,658
United States Treasury Notes, 2.0% due Jan. 15, 2016	50,138,036	47,892,691
Federal Home Loan Bank, 0.01% due July 3, 2006	47,300,000	47,280,640
United States Treasury Bonds, 2.375% due Jan. 15, 2025	44,350,220	43,158,061
TOTAL		<u>\$2,253,854,519</u>

*A complete list of portfolio holdings is available upon request.*

DOMESTIC AND INTERNATIONAL EQUITY COMMISSIONS TO BROKERS  
for the Fiscal Year Ended June 30, 2006  
(Expressed in Thousands)

Brokers *	Total Shares	Total Commission
Merrill Lynch & Co., Inc.	132,741	\$ 1,030
Lehman Brothers	86,524	668
UBS	21,120	645
Weeden & Co.	26,263	529
Goldman Sachs	24,175	491
State Street Brokerage	29,508	406
Credit Suisse First Boston	23,141	398
Morgan Stanley	32,289	378
Citigroup Global Markets	17,138	366
Bear Stearns	8,753	314
Pershing	22,551	304
JP Morgan Securities, Inc.	16,454	297
Deutsche Bank	36,059	294
Investment Technology Group	15,984	214
Banc of America	5,241	206
ADP Clearing & Outsourcing Services, Inc.	4,623	198
Stifel Nicolaus & Co., Inc.	3,047	149
Wachovia	2,937	140
Instinet	14,850	135
Nomura Securities International, Inc.	12,526	130
Warburg Dillon Reed	35,300	122
Prudential Equity Group	2,675	117
Thomas Weisel Partners	2,546	108
Credit Lyonnais Securities	10,246	102
ABN Amro	16,357	101
Other Broker Fees	114,678	2,181
Total Broker Commissions	<u>717,726</u>	<u>\$10,023</u>

\* Proceeds from the sale and disbursements for the purchase of securities are reported net of brokers' commissions. As such, brokers' commissions are not included as investment expenses on the Statements of Changes in Plan Net Assets. Other broker fees include 178 other brokers each receiving less than \$100,000 in total commissions.

For the fiscal year ended June 30, 2006, total domestic equity commissions averaged 1.81 cents per share, and total international equity commissions averaged 10.10 basis points per share.



This page intentionally left blank

### **EMPLOYEES' RETIREMENT & PENSION SYSTEMS**

**The Employees' Retirement System (established in 1941) and the Employees' Pension System (established in 1980) combined account for more than half of all State Retirement and Pension System members. Active membership in the combined employees' systems at the end of fiscal year 2006 exceeded 87,000 participants.**

**Membership includes all regular employees of the State of Maryland.**

**In addition, 144 local governmental units have voluntarily joined the system to provide survivor, disability, and retirement benefits for their employees. The governor, members of the General Assembly, and state correctional officers are also included as members of the combined employees' systems.**



THE SEGAL COMPANY  
2018 Powers Ferry Road, Suite 850 Atlanta, GA 30339-5003  
T 678.306.3100 F 678.306.3190 www.segalco.com

October 19, 2006

Board of Trustees  
State Retirement and Pension  
System of Maryland  
120 East Baltimore Street  
Baltimore, MD 21202

Dear Members of the Board:

At your request, we have conducted our annual actuarial valuation of the State Retirement and Pension System of Maryland as of June 30, 2006.

**Funding Objective**

The funding objective of the System is to establish contribution rates which, over time, will remain level as a percent of payroll. In order to achieve this, a contribution rate has generally been determined which will provide for current cost (i.e., normal cost expressed as a level percent of payroll) plus (or less) a level percent of payroll amortization of the pre-2001 unfunded liability (or surplus) to the year 2020, and of each subsequent layer of unfunded liability (or surplus) over a 25 year period from the year it first arises. Maryland law now contains provisions (i.e. a corridor approach) to prevent large fluctuations in the contribution rate. However, due to this corridor approach, the contribution rates for both the Employees' and Teachers' Combined Systems are lower than the actuarially determined rates.

**Assumptions**

The actuarial assumptions were recommended by the actuary and adopted by the Board of Trustees based on a review of the System's experience completed during Fiscal Year 2003.

The actuarial assumptions and methods used for this valuation meet the parameters set for disclosure by Governmental Accounting Standards Board Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*. These assumptions are presented in the financial section of the System's Comprehensive Annual Financial Report (CAFR).

The results and conclusions of this report are only valid for the July 1, 2006 plan year and should not be interpreted as applying in future years. Differences between our projections and actual amounts depend on the extent to which future experience conforms exactly to the assumptions used in this analysis. Actual amounts will differ from projected amounts to the extent that actual experience deviates from expected experience.

**Data Reliance**

In performing this analysis we relied on data and other information provided by Agency staff. We performed a limited review of the data for reasonableness and consistency and have not found material defects in the data. If there are material defects in the data, it is possible that they would be uncovered by a detailed, systematic review and comparison of the data to search for data values that are questionable or for relationships that are materially inconsistent. Such a review was beyond the scope of our assignment. If the underlying data or information is inaccurate, incomplete, or needs to be revised, the results of our analysis may likewise be inaccurate, incomplete, or may need to be revised.

**Supporting Schedules**

Certain information presented in the System's June 30, 2006 CAFR was derived from our June 30, 2006 actuarial valuation report. In this regard, we were responsible for producing all supporting schedules to be found in the Actuarial Section.

Additionally we were responsible for producing all data presented in the Schedule of Funding Progress, Schedule of Employer Contributions and Notes to the Required Supplementary Information shown in the Financial Section of the 2006 CAFR.

Information pertaining to valuations prior to June 30, 2006 was determined by the predecessor actuarial firm.

**Certification**

We the undersigned are consulting actuaries for Segal and are also members of the American Academy of Actuaries and meet their Qualification Standards to render the actuarial opinion contained herein. On the basis of the foregoing, we certify that, to the best of our knowledge this report is complete and accurate and has been prepared in accordance with Maryland's Annotated Code and generally recognized and accepted actuarial principles and practices which are consistent with the applicable Guides to Professional Conduct, Amplifying Opinions, and supporting Recommendations and Interpretations of the American Academy of Actuaries.

Sincerely,

Leon F. (Rocky) Joyner, Jr.  
FCA, ASA, MAAA, EA  
Vice President and Actuary

K. Eric Fredén  
FSA, MAAA, EA  
Vice President and Actuary

## BOARD SUMMARY

This report presents the results of the June 30, 2006 actuarial valuation of the State Retirement and Pension System of Maryland (SRPS). The primary purposes of performing the annual actuarial valuation are to:

- 1) **determine the contributions** to be paid by the State in Fiscal Year 2008;
- 2) **measure and disclose**, as of the valuation date, the financial condition of the fund;
- 3) **indicate trends** in the financial progress of the fund;
- 4) **provide specific information** and documentation required by the Government Accounting Standards Board (GASB).

In this section of the report, we will present a summary of the above information in the form of:

- the actuary's comments;
- the prior year's experience of the Fund's assets, liabilities, contributions, and membership;
- a series of graphs highlighting key trends experienced by the Fund; and
- a tabular summary, intended for quick reference purposes, of all the principal results from this year's valuation, compared to the prior year's.

### ACTUARY'S COMMENTS

- State contributions for the year beginning July 1, 2007 are estimated to total **\$950** million. This compares to the estimated amount of about **\$765** million in the last valuation. This change includes **\$121** million attributable to the enhanced benefits adopted in the 2006 Legislative session.
- The above amounts include the limitations on State contributions as a result of the corridor method. Without these limitations contributions in the year ended June 30, 2006 would have been **\$166** million higher than actually received. The expected limitation amounts for the years ending June 30, 2007 and June 30, 2008 are **\$199** and **\$162** million respectively.
- The effective amortization period for all State Systems combined is in excess of 50 years as of the June 30, 2006 valuation. These amortization periods do not comply with current generally accepted actuarial principles and practices. They also do not conform with current accounting guidelines. We note that the corridor method was reviewed and changes were proposed recently. We

recommend further review of this methodology with a possible change in conjunction with the next actuarial experience review.

- As noted in the recent actuarial audit the funding method used to value the plan, the Aggregate Entry Age Normal method, is no longer accepted by the Internal Revenue Service as a reasonable funding method. We note that while this IRS ruling is not binding for governmental pension plans, the Aggregate EAN method is rarely used and can mask plan experience. We recommend reviewing the continued appropriateness of using this method in conjunction with the next scheduled actuarial experience review.
- The net experience gain/(loss) for the State portion of the system was 0.07% of the June 30, 2005 actuarial accrued liability. For the individual plans, this percentage ranged from 0.07% for the Teacher's system to 3.35% for the Judge's System. These results indicate that in total the actuarial assumptions reasonably estimated emerging plan liabilities. These assumptions will be reviewed in detail with the next regular experience review.

The balance of this section summarizes System trends, and provides the principal details on this year's experience.

### PRIOR YEAR EXPERIENCE

#### Assets (State and Municipal)

Plan assets for this Fund are measured on both a market value and an actuarial or smoothed value basis. The actuarial smoothing method, essentially reflects only 20% of the difference between (a) the asset value if they had earned the assumed rate of 7.75%, and (b) the actual market value. In periods of high returns, this method significantly defers the amount of asset gains above the assumed return of 7.75%. Conversely, in periods of returns below the assumed, recognition of the losses is deferred. The primary advantage of this smoothing technique is contribution stability. The System does not feel the full impact of lower (or higher) costs when asset values fluctuate dramatically.

For the plan year ending June 30, 2006, the Fund earned **10.43%** on a market value basis and **6.70%** on a smoothed basis. While on a market basis, the Fund experienced an investment gain of **\$852** million, the actuarial or smoothed basis grew by less than 7.75% which produced a loss of **\$356** million. The specific changes between the prior year amounts and this year's are presented below.

Item (In Millions)	Market Value	Actuarial Value
June 30, 2005 Value	\$32,076	\$34,520
Change due to Municipal New Entrants/ Withdrawals	(10)	(10)
Employer Contributions	721	721
Member Contributions	215	215
Benefit Payments	(1,931)	(1,931)
Expected Investment Earnings (7.75%)	2,448	2,636
Expected Value June 30, 2006	\$33,519	\$36,151
Investment Gain (Loss)	852	(356)
June 30, 2006 Value	\$34,371	\$35,795

**Liabilities (State and Municipal)**

Three different measures of liabilities are calculated for this fund: a total value of future obligations (PVB), an actuarial liability (EAN), and an accrued benefit liability (PVAB). Only the actuarial liability is analyzed in terms of a gain or loss experience, which then is used to determine the System’s funding and accounting (GASB) disclosures. During the plan year ending in 2006, the actuarial liabilities experienced an overall loss of **\$239 million**, which is **0.55%** of the total actuarial liability being measured. The primary cause for liability experience being less favorable than anticipated this past year was annual salary increases being higher than anticipated.

LIABILITIES (In Millions)	Total Value (PVB)	Actuarial (EAN)	Accounting (PVAB)
June 30, 2005	\$47,066	\$39,133	\$32,947
June 30, 2006	\$53,956	\$43,243	\$36,627

**Unfunded Liabilities and Funding Ratios (State and Municipal)**

The difference between assets and liabilities is the unfunded liability. This is measured in two ways: unfunded *actuarial* liabilities, which compare the actuarial liabilities to the actuarial asset value, and unfunded *accrued* benefits, which compare the present value of benefits accrued as of the valuation date to the market value of assets. These amounts are shown for June 30, 2005 and June 30, 2006, as well as the corresponding funding ratios for each (assets divided by liabilities).

Item (In Millions)	Actuarial	PVAB
6/30/2005 Net Surplus (Unfunded)	(\$4,614)	(\$ 871)
Funding Ratio	88.2%	97.4%
6/30/2006 Net Surplus (Unfunded)	(\$7,448)	(\$2,256)
Funding Ratio	82.8%	93.8%

**Contributions (State Portion Only)**

In our report, we show the various contribution rates by system. In this summary, we present the overall State contribution rate, and compare it to the rate developed in the June 30, 2005 actuarial valuation. In summary, due to the net impact of enhanced benefits for the Teachers’ and Employees’ Systems, investment losses and liability gains, the overall State contribution requirement, payable in FY 2007 on the GASB disclosure basis, has increased by **1.43%** of payroll. It is important to note that this is not the contribution rate upon which the State will base its budget in either FY 2007 or FY 2008. This analysis compares the underlying cost calculations which will be used to disclose the State’s pension expense for GASB reporting purposes. The actual appropriations are calculated using the Corridor Funding Method for the two largest plans. This approach produced payroll-weighted averages of **9.18%** at June 30, 2006, increasing to **11.10%** as of June 30, 2006.

Rate as Percent of Covered Payroll – GASB Disclosure	
June 30, 2005 State Annual Required Contribution Rate	11.58%
Increase due to Assumption Changes	0.00%
Increase due to Plan Changes	1.42%
Increase due to Investment Loss	0.25%
Decrease due to Liability Gain	(0.24%)
June 30, 2006 State Annual Required Contribution Rate	13.01%

Rate as Percent of Covered Payroll – Budget (Corridor Method)	
June 30, 2005 State Appropriation Rate	9.18%
Increase due to Shift in Payroll for All Systems	0.00%
Increase due to Plan Changes	1.42%
Increase in Systems not within the Corridor	0.03%
Increase due to TCS falling out of Corridor	0.18%
Increase due to ECS remaining out of Corridor	0.29%
June 30, 2006 State Appropriation Rate	11.10%

**Membership (State and Municipal)**

There are four types of plan participants: current active workers, previous terminations who retain a right to a deferred vested benefit, previous terminations who are not vested but have member contributions in the System (inactives), and participants in pay status. In Appendix B, we present extensive details on membership statistics. Below, totals are compared for each participant group between June 30, 2005 and 2006.

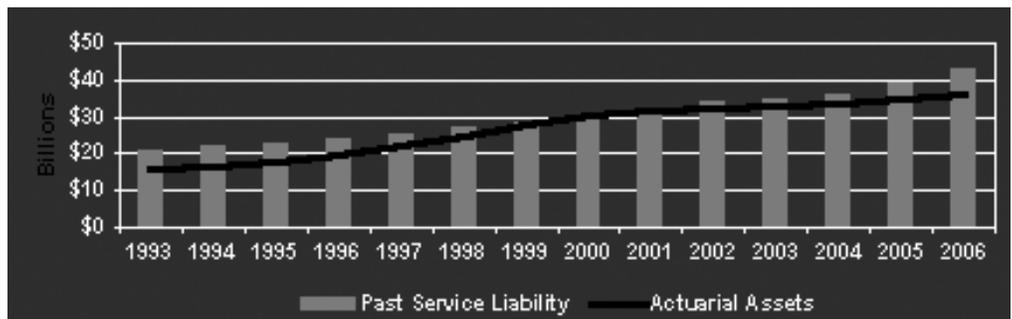
As shown below, there was an overall increase in participation during the year of **2.5%**.

	June 30, 2005	June 30, 2004	Change
Active Participants	191,273	185,861	1.2%
Terminated Vested Participants	49,310	36,523	2.0%
Participants In Pay Status	103,831	100,196	3.6%
<b>Total Participants</b>	<b>344,414</b>	<b>335,910</b>	<b>2.5%</b>

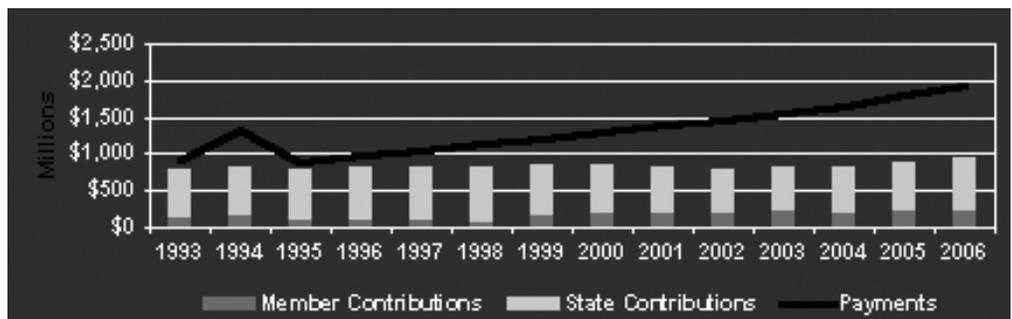
**Trends**

One of the best ways to measure or evaluate the financial condition of a pension plan is to examine the historical trends that are evolving. Presented below are three charts which show trend information from 1993 through the end of 2006, on the System's assets and liabilities, annual cash flows in and out of the fund, and the State contribution rate. Our comments on each follow.

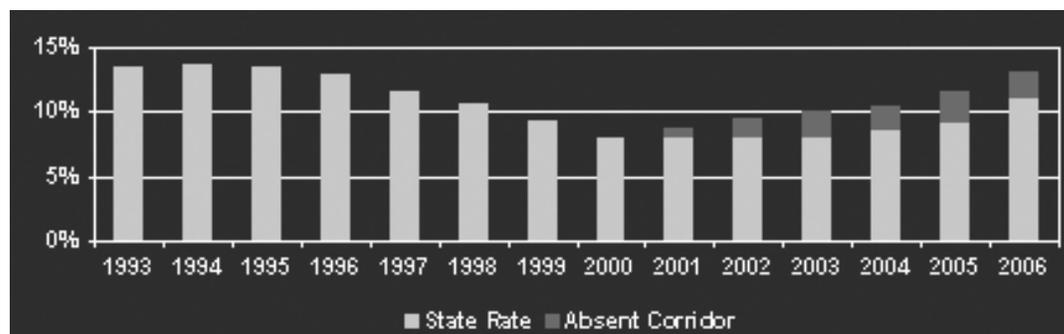
**Chart A:**  
Assets/Liabilities



**Chart B:**  
Cash Flows



**Chart C:**  
State Contribution Rate



## Comments

Chart A places into perspective the aforementioned investment and liability performance losses of this past year. The ratio of actuarial assets to liabilities (i.e., funding ratio) has grown since the early 1980's. The unfavorable investment experience from 2000 through 2003 has eroded the funded ratio from its peak in 2000.

Chart B presents an emerging trend that will have investment implications. It is a trend being faced by many state-wide retirement systems, with the aging of our baby boomer generations. Payments to retirees are on the increase, while cash into the fund, from employer and employee contributions, is stable or declining. The ECS contribution rate started increasing in FY 2006 and the TCS contribution rate began increasing in FY 2007 under the corridor method.

Finally, Chart C, looks only at the State contribution rate which is used each year to determine the upcoming fiscal year State appropriation. It shows the impact of the past decade's sustained investment gains, a continuous lowering of the rate until 2000. Plan amendments are not subject to the corridor method. Effective with the 2001 valuation, the State appropriations are performed under a corridor funding method for the two largest plans. The appropriation remained essentially level for a few years before increasing with the 2004 valuation. In the absence of favorable investment and/or demographic experience, the contribution rates can be expected to increase to the level indicated if the corridor method had not been adopted. Without the corridor method, the State contribution in FY 2008 would be 1.91% of payroll higher than the amount to be budgeted under the corridor method. This is 15% less than the actuarial rate. Note that the full effect of the benefit enhancements first reflected for FY 2008 are included in the cost rate.

---

## ACTUARIAL METHODS AND ASSUMPTIONS

### Funding Method

The System uses the entry age normal cost method with projection to determine the actuarial accrued liability on which future employer contribution rates will be based. Under this funding method, a total contribution rate is determined which consists of two elements, the normal cost rate and the unfunded actuarial liability rate (see note 4).

The unfunded actuarial accrued liability (UAAL) is being amortized, as a level percentage of payroll, in distinct pieces. The UAAL which existed as of the June 30, 2000 actuarial valuation is being amortized over the remaining 14-year period to June 30, 2020. Each new layer of UAAL arising subsequent to the year ended June 30, 2000 is being amortized in separate annual layers over a 25-year period. Each separate amortized layer has a closed amortization period. The equivalent single amortization period is 30 years.

### Asset Valuation Method

Assets are valued for funding purposes using a five-year moving average. Under this method, the year end actuarial asset value equals 1/5 of the current fiscal year end fair value, as reported in the financial statements, plus 4/5 of the "expected market value." For purposes of this calculation, the "expected market value" is the preceding fiscal year's actuarial asset

value, adjusted for the current fiscal year's cash flows with interest accumulated at the actuarial assumed rate of return on investments.

### Actuarial Assumptions

The assumptions used for the actuarial valuation were recommended by the System's independent actuary, based upon periodic analyses of the System's experience, and adopted by the Board of Trustees. Differences between assumed and actuarial experience (i.e., actuarial gains and losses) are part of the unfunded actuarial liability. The following significant assumptions were used in the actuarial valuation as of June 30, 2006:

- a rate of return on investments of 7.75% compounded annually (adopted June 30, 2003);
- projected salary increases of 4% compounded annually, attributable to inflation (adopted June 30, 2003);
- additional projected salary increases ranging from 0.00% to 11.96% per year attributable to seniority and merit (adopted June 30, 2003);
- post-retirement benefit increases ranging from 3% to 4% per year depending on the system (adopted June 30, 2003);
- rates of mortality, termination of service, disablement and retirement based on actual experience during the period from 1981 through 2002 (adopted June 30, 2003); and
- an increase in the aggregate active member payroll of 4% annually (adopted June 30, 2003).

ACCOUNTING STATEMENT INFORMATION  
THE TOTAL SYSTEMS OF THE STATE OF MARYLAND  
(STATE AND MUNICIPAL)

	2006	2005
<b>A. FASB #35 basis</b>		
1. Present value of benefits accrued to date:		
a. Members currently receiving payments	\$21,050,092,563	\$19,997,772,896
b. Former vested members	1,036,360,357	977,556,545
c. Active members	<u>14,540,067,073</u>	<u>11,971,373,761</u>
2. Total present value of accrued benefits (1 (a) + 1 (b) + 1 (c))	36,626,519,993	32,946,703,202
3. Assets at market value	<u>34,370,818,638</u>	<u>32,075,918,515</u>
4. Unfunded value of accrued benefits (2-3)	<u>\$2,255,701,355</u>	<u>\$ 870,784,687</u>
5. Ratio of assets to value of benefits (3/2)	93.84%	97.36%
<b>B. GASB #25 basis</b>		
1. Actuarial accrued liabilities for retirees and beneficiaries currently receiving benefits and terminated employees not yet receiving benefits	\$22,086,452,920	\$20,975,329,441
2. Actuarial accrued liabilities for current employees	<u>21,157,039,537</u>	<u>18,158,120,326</u>
3. Total actuarial accrued liability (1+2)	43,243,492,457	39,133,449,767
4. Net actuarial assets available for benefits	<u>35,795,025,134</u>	<u>34,519,500,395</u>
5. Unfunded actuarial accrued liability (3-4)	<u>\$ 7,448,467,323</u>	<u>\$ 4,613,949,372</u>

SUMMARY OF UNFUNDED ACTUARIAL  
(STATE AND

Valuation Date June 30,	Actuarial Liabilities For			Total Liabilities	Actuarial Value of Assets
	Active Member Contributions	Retirees, Term Vested and Inactives	Active Members Employer Fin. Portion		
1997	\$1,502,991,713	\$12,714,514,210	\$11,165,702,737	\$25,383,208,660	\$21,920,695,723
1998	1,505,629,954	12,866,065,299	13,045,239,668	27,416,934,921	24,850,355,227
1999	1,580,530,209	13,583,779,499	13,311,070,338	28,475,380,046	27,646,578,997
2000	1,662,397,147	14,636,664,952	13,980,804,631	30,279,866,730	30,649,380,445
2001	1,752,989,299	15,939,733,140	14,777,219,354	32,469,941,793	31,914,778,425
2002	1,858,783,727	16,783,959,580	15,488,540,705	34,131,284,012	32,323,263,153
2003	1,973,371,055	17,573,117,822	15,428,111,989	34,974,600,866	32,631,464,884
2004	2,064,065,193	19,041,901,524	15,219,737,348	36,325,704,065	33,484,656,570
2005	2,148,065,879	20,975,329,441	16,010,054,447	39,133,449,767	34,519,500,395
2006	2,217,897,868	22,086,452,920	18,939,141,669	43,243,492,457	35,795,025,134

SUMMARY OF RETIREES AND BENEFICIARIES ADDED TO AND REMOVED FROM ROLLS  
(STATE AND MUNICIPAL)

Fiscal Year Ended	Added to Rols		Removed from Rols		Rolls-End of Year		% Increase in Annual Allowances	Average Annual Allowance
	Number	Annual Allowance	Number	Annual Allowances	Number	Annual Allowances		
1997	7,157	\$119,374,380	2,731	\$33,641,211	71,488	\$ 987,588,667	9.51%	\$13,815
1998	5,217	90,497,436	2,366	30,768,198	74,339	1,047,317,905	6.05	14,088
1999	5,514	93,034,053	2,375	30,628,858	77,478	1,109,723,100	5.96	14,323
2000	5,758	115,003,079	2,463	31,450,868	80,773	1,211,400,269	7.41	14,998
2001	6,071	145,073,765	2,659	34,172,397	84,185	1,322,301,637	9.15	15,708
2002	5,925	107,545,768	2,743	36,803,883	87,367	1,393,043,522	5.35	15,945
2003	6,216	123,497,444	2,780	38,449,020	90,803	1,478,091,946	6.11	16,278
2004	6,822	152,664,871	2,745	38,223,588	94,880	1,592,533,229	7.74	16,785
2005	8,179	179,497,068	2,863	41,696,122	100,196	1,730,334,175	8.65	17,269
2006	6,822	164,369,688	3,247	34,799,179	103,831	1,859,904,684	7.49	17,913

LIABILITIES / SOLVENCY TEST  
MUNICIPAL)

Ratio of Assets to Actuarial Liabilities			Funded Ratio (Assets/Liab. Coverage)	Unfunded Actuarial Accrued Liability (UAAL)	Covered Payroll	UAAL as % of Covered Payroll
Active Member Contributions	Retirees Term Vested and Inactives	Active Members Employer Fin. Portion				
100%	100%	68.99%	86.36%	\$3,462,512,937	\$5,657,384,942	61%
100	100	80.33	90.64	2,566,579,694	5,900,456,000	43
100	100	93.77	97.09	828,801,049	6,312,417,000	13
100	100	102.64	101.22	(369,513,715)	6,725,870,000	(5)
100	100	96.24	98.29	555,163,368	7,255,036,000	8
100	100	88.33	94.70	1,808,020,859	7,867,794,200	23
100	100	84.81	93.30	2,343,135,982	8,134,419,291	29
100	100	81.33	92.18	2,841,047,495	8,069,480,852	35
100	100	71.18	88.21	4,613,949,372	8,603,760,761	54
100	100	60.67	82.78	7,448,467,323	9,287,575,596	80

STATEMENT OF CHANGES IN TOTAL ACTUARIAL  
PRESENT VALUE OF ALL ACCRUED BENEFITS  
(STATE AND MUNICIPAL)  
(Expressed in Millions)

	<b>Accumulated Benefit Obligation (FASB 35)</b>
Actuarial present value of accrued benefits at June 30, 2005	\$ <u>32,947</u>
Increase (decrease) during year attributable to:	
Passage of Time	2,480
Benefits Paid – FY 2006	(1,931)
Benefits Accrued, Other Gains/Losses	2,022
Plan Amendment & Changes in Actuarial Assumptions	<u>1,109</u>
Net Increase	<u>3,680</u>
Actuarial present value of accrued benefits at June 30, 2006	\$ <u><u>36,627</u></u>

REPORT OF THE ACTUARY ON THE VALUATION OF THE  
STATE RETIREMENT AND PENSION SYSTEM OF MARYLAND  
(STATE AND MUNICIPAL)  
**as of June 30, 2006**  
*Summary of Principal Results*

	June 30, 2006	June 30, 2005	% Change
<b>1. Participant Data</b>			
Number of:			
Active Members	191,273	188,050	1.7 %
Retired Members and Beneficiaries	103,831	100,196	3.6
Vested Former Members	<u>49,310</u>	<u>37,248</u>	32.4
Total Participants	<u>344,414</u>	<u>325,494</u>	5.8
Covered Annual Salaries of Active Members	\$ 9,089,950,701	\$ 8,603,760,761	5.7
Annual Retirement Allowances for for Retired Members and Beneficiaries	\$ 1,859,904,684	\$ 1,730,334,175	7.5
<b>2. Assets and Liabilities</b>			
Total Actuarial Liability	\$ 43,243,492,457	\$ 39,133,449,767	10.5
Assets for Valuation Purposes	<u>35,795,025,134</u>	<u>34,519,500,395</u>	3.7
Unfunded Actuarial Liability (Surplus)	<u>\$ 7,448,467,323</u>	<u>\$ 4,613,949,372</u>	61.4
FASB Accrued Liability	\$ 36,626,519,993	\$ 32,946,703,202	11.2
Market Value of Assets	<u>34,370,818,638</u>	<u>32,075,918,515</u>	7.2
Unfunded FASB Accrued Liability (Surplus)	<u>\$ 2,255,701,355</u>	<u>\$ 870,784,687</u>	159.0

\* Does not include members of State Police and LEOPS who have elected the DROP.

REPORT OF THE ACTUARY ON THE TWENTY-SIXTH ANNUAL VALUATION OF THE  
TEACHERS' COMBINED SYSTEM OF THE STATE OF MARYLAND  
as of June 30, 2006

*Summary of Principal Results*

	June 30, 2006	June 30, 2005	% Change
<b>1. Participant Data</b>			
Number of:			
Active Members	100,318	97,790	2.6 %
Retired Members and Beneficiaries	50,279	48,091	4.5
Vested Former Members	<u>21,053</u>	<u>20,143</u>	4.5
Total Participants	<u>171,650</u>	<u>166,024</u>	3.4
Covered Annual Salaries of Active Members	\$ 5,161,482,879	\$ 4,867,396,045	6.0
Annual Retirement Allowances for for Retired Members and Beneficiaries	\$ 1,126,950,408	\$ 1,049,319,738	7.4
<b>2. Assets and Liabilities</b>			
Total Actuarial Liability	\$ 25,617,483,931	\$ 23,305,198,400	9.9
Assets for Valuation Purposes	<u>21,575,451,378</u>	<u>20,801,529,328</u>	3.7
Unfunded Actuarial Liability (Surplus)	<u>\$ 4,042,032,553</u>	<u>\$ 2,503,669,072</u>	61.4
FASB Accrued Liability	\$ 21,559,930,484	\$ 19,703,988,613	9.4
Market Value of Assets	<u>20,741,517,825</u>	<u>19,357,871,605</u>	7.1
Unfunded FASB Accrued Liability (Surplus)	<u>\$ 818,412,659</u>	<u>\$ 346,117,008</u>	136.5

REPORT OF THE ACTUARY ON THE TWENTY-SIXTH ANNUAL VALUATION OF THE  
EMPLOYEES' COMBINED SYSTEM OF THE STATE OF MARYLAND  
(STATE AND MUNICIPAL)  
**as of June 30, 2006**  
*Summary of Principal Results*

	June 30, 2006	June 30, 2005	% Change
<b>1. Participant Data</b>			
Number of:			
Active Members	87,100	86,656	0.5 %
Retired Members and Beneficiaries	50,487	49,158	2.7
Vested Former Members	<u>28,063</u>	<u>27,349</u>	2.6
Total Participants	<u>165,650</u>	<u>163,163</u>	1.5
Covered Annual Salaries of Active Members	\$ 3,707,419,470	\$ 3,537,601,880	4.8
Annual Retirement Allowances for for Retired Members and Beneficiaries	\$ 615,281,664	\$ 574,110,012	7.2
<b>2. Assets and Liabilities</b>			
Total Actuarial Liability	\$ 15,291,090,847	\$ 13,671,755,822	11.8
Assets for Valuation Purposes	<u>12,287,941,567</u>	<u>11,855,672,591</u>	3.6
Unfunded Actuarial Liability (Surplus)	<u>\$ 3,003,149,280</u>	<u>\$ 1,816,083,231</u>	65.4
FASB Accrued Liability	\$ 12,808,953,126	\$ 11,225,188,692	14.1
Market Value of Assets	<u>11,821,365,766</u>	<u>11,037,018,138</u>	7.1
Unfunded FASB Accrued Liability (Surplus)	<u>\$ 987,587,360</u>	<u>\$ 188,170,554</u>	424.8

REPORT OF THE ACTUARY ON THE FIFTY-SIXTH ANNUAL VALUATION OF THE  
STATE POLICE RETIREMENT SYSTEM OF THE STATE OF MARYLAND  
as of June 30, 2006

*Summary of Principal Results*

	June 30, 2006	June 30, 2005	% Change
<b>1. Participant Data</b>			
Number of:			
Active Members	1,441	1,439	0.1 %
Retired Members and Beneficiaries	1,937	1,909	1.5
Vested Former Members	<u>58</u>	<u>47</u>	23.4
Total Participants	<u>3,436</u>	<u>3,395</u>	1.2
Covered Annual Salaries of Active Members	\$ 79,049,617	\$ 76,463,416	3.4
Annual Retirement Allowances for for Retired Members and Beneficiaries	\$ 75,249,756	\$ 68,733,154	9.5
<b>2. Assets and Liabilities</b>			
Total Actuarial Liability	\$ 1,325,874,916	\$ 1,284,949,704	3.2
Assets for Valuation Purposes	<u>1,301,876,790</u>	<u>1,289,345,033</u>	1.0
Unfunded Actuarial Liability (Surplus)	\$ <u>23,998,126</u>	\$ <u>(4,395,329)</u>	(646.0)
FASB Accrued Liability	\$ 1,286,976,803	\$ 1,209,385,668	6.4
Market Value of Assets	<u>1,210,073,370</u>	<u>1,154,310,866</u>	4.8
Unfunded FASB Accrued Liability (Surplus)	\$ <u>76,903,433</u>	\$ <u>55,074,802</u>	39.6

REPORT OF THE ACTUARY ON THE TWENTY-SIXTH ANNUAL VALUATION OF THE  
PENSION PLAN OF JUDGES AND THEIR SURVIVING SPOUSES  
as of June 30, 2006

*Summary of Principal Results*

	June 30, 2006	June 30, 2005	% Change
<b>1. Participant Data</b>			
Number of:			
Active Members	296	282	5.0 %
Retired Members and Beneficiaries	330	316	4.4
Vested Former Members	<u>14</u>	<u>15</u>	(6.7)
Total Participants	<u>640</u>	<u>613</u>	4.4
Covered Annual Salaries of Active Members	\$ 35,524,704	\$ 33,074,430	7.4
Annual Retirement Allowances for for Retired Members and Beneficiaries	\$ 20,135,364	\$ 18,471,726	9.0
<b>2. Assets and Liabilities</b>			
Total Actuarial Liability	\$ 352,537,011	\$ 328,032,741	7.5
Assets for Valuation Purposes	<u>273,678,641</u>	<u>260,124,866</u>	5.2
Unfunded Actuarial Liability (Surplus)	\$ <u>78,858,370</u>	\$ <u>67,907,875</u>	16.1
FASB Accrued Liability	\$ 340,463,117	\$ 314,096,676	8.4
Market Value of Assets	<u>261,060,907</u>	<u>240,135,182</u>	8.7
Unfunded FASB Accrued Liability (Surplus)	\$ <u>79,402,210</u>	\$ <u>73,961,494</u>	7.4

REPORT OF THE ACTUARY ON THE FIFTEENTH ANNUAL VALUATION OF THE  
LAW ENFORCEMENT OFFICERS' PENSION SYSTEM OF THE STATE OF MARYLAND  
(STATE AND MUNICIPAL)

**as of June 30, 2006**  
*Summary of Principal Results*

	June 30, 2006	June 30, 2005	% Change
<b>1. Participant Data</b>			
Number of:			
Active Members	2,063	1,826	13.0 %
Retired Members and Beneficiaries	782	708	10.5
Vested Former Members	<u>115</u>	<u>104</u>	10.6
Total Participants	<u>2,960</u>	<u>2,638</u>	12.2
Covered Annual Salaries of Active Members	\$ 104,515,314	\$ 87,219,783	19.8
Annual Retirement Allowances for for Retired Members and Beneficiaries	\$ 22,008,960	\$ 19,493,836	12.9
<b>2. Assets and Liabilities</b>			
Total Actuarial Liability	\$ 649,825,724	\$ 537,735,690	20.8
Assets for Valuation Purposes	<u>352,415,577</u>	<u>310,087,428</u>	13.7
Unfunded Actuarial Liability (Surplus)	\$ <u>297,410,147</u>	\$ <u>227,648,262</u>	30.6
FASB Accrued Liability	\$ 623,901,419	\$ 488,403,785	27.7
Market Value of Assets	<u>333,024,309</u>	<u>283,944,060</u>	17.3
Unfunded FASB Accrued Liability (Surplus)	\$ <u>290,877,110</u>	\$ <u>204,459,725</u>	42.3

\* Does not include members who elected DROP.

REPORT OF THE ACTUARY ON THE FOURTEENTH ANNUAL VALUATION OF THE  
LOCAL FIRE AND POLICE SYSTEM OF THE STATE OF MARYLAND  
as of June 30, 2006

*Summary of Principal Results*

	June 30, 2006	June 30, 2005	% Change
<b>1. Participant Data</b>			
Number of:			
Active Members	55	57	(3.5) %
Retired Members and Beneficiaries	16	14	14.3
Vested Former Members	<u>7</u>	<u>6</u>	16.7
Total Participants	<u><u>78</u></u>	<u><u>77</u></u>	1.3
Covered Annual Salaries of Active Members	\$ 1,958,717	\$ 2,005,207	(2.3)
Annual Retirement Allowances for for Retired Members and Beneficiaries	\$ 278,532	\$ 205,709	35.4
<b>2. Assets and Liabilities</b>			
Total Actuarial Liability	\$ 6,680,028	\$ 5,777,410	15.6
Assets for Valuation Purposes	<u>3,661,181</u>	<u>2,741,149</u>	33.6
Unfunded Actuarial Liability (Surplus)	\$ <u>3,018,847</u>	\$ <u>3,036,261</u>	(0.6)
FASB Accrued Liability	\$ 6,295,044	\$ 5,639,768	11.6
Market Value of Assets	<u>3,776,461</u>	<u>2,638,664</u>	43.1
Unfunded FASB Accrued Liability (Surplus)	\$ <u><u>2,518,583</u></u>	\$ <u><u>3,001,104</u></u>	(16.1)

## SCHEDULE OF ACTIVE MEMBERSHIP VALUATION DATA BY PLAN

**Teachers' Retirement**

<b>Valuation Date As of June 30,</b>	<b>Number</b>	<b>Annual Payroll</b>	<b>Annual Average Pay</b>	<b>% Increase Avg. Pay</b>
1997	15,619	\$799,096,847	\$51,162	2.18%
1998	14,346	760,092,729	52,983	3.56
1999	13,043	719,046,552	55,129	4.05
2000	11,634	671,990,806	57,761	4.77
2001	10,396	638,864,807	61,453	6.39
2002	9,270	604,172,528	65,175	6.06
2003	8,199	555,522,563	67,755	3.96
2004	7,197	502,487,678	69,819	3.05
2005	6,255	464,693,323	74,291	6.41
2006	5,449	413,849,937	75,950	2.23

**Teachers' Pension**

<b>Valuation Date As of June 30,</b>	<b>Number</b>	<b>Annual Payroll</b>	<b>Annual Average Pay</b>	<b>% Increase Avg. Pay</b>
1997	66,978	\$2,352,121,326	\$35,118	0.88%
1998	71,435	2,559,167,548	35,825	2.01
1999	75,578	2,831,567,375	37,465	4.58
2000	79,297	3,057,854,648	38,562	2.93
2001	82,901	3,355,335,942	40,474	4.96
2002	87,086	3,718,881,395	42,704	5.51
2003	89,099	3,966,679,839	44,520	4.25
2004	88,765	4,113,119,415	46,337	4.08
2005	91,535	4,590,698,122	50,152	8.23
2006	94,869	4,855,335,579	51,179	2.04

**Employees' Retirement**

(State and Municipal)

<b>Valuation Date As of June 30,</b>	<b>Number</b>	<b>Annual Payroll</b>	<b>Annual Average Pay</b>	<b>% Increase Avg. Pay</b>
1997	13,469	\$445,726,994	\$33,093	0.13%
1998	13,149	439,012,253	33,388	0.89
1999	12,657	436,772,178	34,508	3.35
2000	12,213	444,062,220	36,360	5.37
2001	11,962	457,899,607	38,280	5.28
2002	11,722	470,462,717	40,135	4.85
2003	11,347	462,088,968	40,723	1.47
2004	10,489	438,455,277	41,801	2.65
2005	9,869	423,715,070	42,934	2.71
2006	10,121	467,808,791	46,222	7.66

## SCHEDULE OF ACTIVE MEMBERSHIP VALUATION DATA BY PLAN

*(continued)***Employees' Pension**

(State and Municipal)

<b>Valuation Date As of June 30,</b>	<b>Number</b>	<b>Annual Payroll</b>	<b>Annual Average Pay</b>	<b>% Increase Avg. Pay</b>
1997	68,195	\$1,953,776,617	\$28,650	1.39%
1998	68,893	2,009,173,639	29,164	1.79
1999	70,426	2,176,887,154	30,910	5.99
2000	73,212	2,385,187,733	32,579	5.40
2001	76,024	2,626,959,051	34,554	6.06
2002	78,584	2,886,208,074	36,728	6.29
2003	77,939	2,961,965,306	38,004	3.47
2004	75,955	2,964,093,317	39,024	2.68
2005	76,787	3,187,380,273	41,509	6.37
2006	76,979	3,325,316,541	43,198	4.07

**Judges' Retirement**

<b>Valuation Date As of June 30,</b>	<b>Number</b>	<b>Annual Payroll</b>	<b>Annual Average Pay</b>	<b>% Increase Avg. Pay</b>
1997	268	\$25,007,240	\$93,311	3.00%
1998	273	25,552,537	93,599	0.31
1999	283	29,576,854	104,512	11.66
2000	283	30,146,837	106,526	1.93
2001	281	30,554,439	108,735	2.07
2002	281	31,824,096	113,253	4.16
2003	287	33,168,859	115,571	2.05
2004	283	33,149,832	117,137	1.36
2005	282	33,897,984	120,206	2.62
2006	296	35,939,104	121,416	1.01

**State Police Retirement**

<b>Valuation Date As of June 30,</b>	<b>Number</b>	<b>Annual Payroll</b>	<b>Annual Average Pay</b>	<b>% Increase Avg. Pay</b>
1997	1,588	\$62,936,492	\$39,633	0.61%
1998	1,635	70,663,067	43,219	9.05
1999	1,647	75,601,750	45,903	6.21
2000	1,636	79,388,246	48,526	5.71
2001	1,578	79,382,508	50,306	3.67
2002	1,589	81,141,520	52,323	4.01
2003	1,542	80,838,519	52,424	0.19
2004	1,445	77,531,613	53,655	2.35
2005	1,439	77,610,367	53,934	0.52
2006	1,441	80,648,855	55,967	3.77

SCHEDULE OF ACTIVE MEMBERSHIP VALUATION DATA BY PLAN  
(continued)

**Law Enforcement Officers' Pension**

<b>Valuation Date As of June 30,</b>	<b>Number</b>	<b>Annual Payroll</b>	<b>Annual Average Pay</b>	<b>% Increase Avg. Pay</b>
1997	317	\$12,904,416	\$40,708	2.77%
1998	755	30,511,663	40,413	(0.72)
1999	862	36,435,243	42,268	4.59
2000	1,130	50,301,859	44,515	5.32
2001	1,318	60,438,291	45,856	3.01
2002	1,410	65,915,519	46,748	1.95
2003	1,481	69,469,540	46,907	0.34
2004	1,675	78,628,672	46,942	0.07
2005	1,826	88,925,957	48,700	3.75
2006	2,063	106,668,684	51,706	6.17

**Local Fire and Police**

<b>Valuation Date As of June 30,</b>	<b>Number</b>	<b>Annual Payroll</b>	<b>Annual Average Pay</b>	<b>% Increase Avg. Pay</b>
1997	168	\$5,815,010	\$34,613	3.92%
1998	177	6,287,842	35,525	2.63
1999	178	6,529,920	36,685	3.27
2000	184	6,937,750	37,705	2.78
2001	140	5,600,965	40,007	6.11
2002	181	7,188,351	39,715	(0.73)
2003	127	4,685,697	36,895	(7.10)
2004	52	1,782,520	34,279	(7.09)
2005	57	2,085,416	36,586	6.73
2006	55	2,008,605	36,520	(0.18)



This page intentionally left blank

## **JUDGES' RETIREMENT SYSTEM**

The Judges' Retirement System was established by the General Assembly in 1969. Future survivor, disability and retirement benefits will be provided to its current active membership of 296 participants. The Judicial System of Maryland is responsible for issuing findings of fact and conclusions of law in both criminal and civil matters. Membership includes judges of the District Court, Circuit Court, Court of Appeals and the Court of Special Appeals, as well as State Workers' Compensation Commissioners.

SCHEDULE OF RETIRED MEMBERS BY TYPE

as of June 30, 2006

Amount of Monthly Benefit	Number of Retirees	Type of Retirement						
		1	2	3	4	5	6	7
\$ 1- 300	14,702	11,059	1,356	1,029	25	29	851	354
301- 600	14,705	8,882	2,256	1,128	99	73	1,871	396
601- 900	12,270	7,413	1,709	905	101	107	1,777	259
901- 1,200	10,784	6,803	1,413	702	117	272	1,335	142
1,201 - 1,500	9,296	5,916	1,262	574	87	379	987	91
1,501 - 1,800	8,004	5,242	1,249	364	78	379	634	58
1,801 - 2,100	7,328	5,104	1,014	290	87	326	482	24
2,101 - 2,400	6,316	4,495	879	212	86	306	324	14
2,401 - 2,700	5,606	4,330	616	166	52	200	233	11
2,701 - 3,000	4,776	4,038	329	116	37	143	104	8
Over 3000	10,044	8,520	481	297	70	544	119	13
	<u>103,831</u>	<u>71,801</u>	<u>12,564</u>	<u>5,783</u>	<u>839</u>	<u>2,758</u>	<u>8,715</u>	<u>1,371</u>

**Type of Retirement:**

- 1 – Normal retirement for age and service
- 2 – Early retirement
- 3 – Survivor payment – normal or early retirement
- 4 – Survivor payment – death in service
- 5 – Accidental disability retirement
- 6 – Ordinary disability retirement
- 7 – Survivor payment – disability retirement

SCHEDULE OF BENEFIT EXPENSE BY TYPE

(Expressed In Thousands)

Fiscal Year	Age & Service Benefits		Death In Service	Disability Benefits			Death After Retirement	Total
	Retirees	Survivors	Pre-Retirement	Retirees		Post-Retirement		
			Benefits	Accidental	Ordinary	Survivors	Benefits	
1997	\$ 823,755	\$ 48,178	\$ 6,352	\$ 26,419	\$ 51,660	\$ 5,445	\$ 11,294	\$ 973,103
1998	887,541	51,908	6,756	28,465	55,661	5,866	11,577	1,047,774
1999	942,736	55,997	6,335	33,788	59,219	6,451	10,560	1,115,086
2000	974,585	62,158	7,372	25,801	96,168	14,073	10,797	1,190,954
2001	1,039,129	66,756	7,561	29,230	103,575	15,599	10,954	1,272,804
2002	1,116,884	72,211	7,908	32,642	113,107	16,836	12,738	1,372,326
2003	1,197,037	78,064	7,443	36,113	122,967	18,355	14,278	1,474,257
2004	1,275,254	82,862	8,515	39,777	131,115	19,798	13,301	1,570,622
2005	1,377,977	88,895	8,369	43,933	142,872	21,318	14,033	1,697,397
2006	1,479,107	101,395	8,655	48,351	152,800	24,036	15,124	1,829,468

OF RETIREMENT AND OPTION SELECTED

<b>#Option Selected</b>							
<b>Max.</b>	<b>Opt. 1</b>	<b>Opt. 2</b>	<b>Opt. 3</b>	<b>Opt. 4</b>	<b>Opt. 5</b>	<b>Opt. 6</b>	<b>Opt. 7</b>
6,181	3,458	1,891	1,183	1,103	436	439	11
5,183	3,060	1,826	1,827	1,723	352	722	14
4,071	2,122	1,531	1,703	1,877	279	673	14
3,250	1,726	1,653	1,525	1,666	306	652	6
2,523	1,476	1,554	1,391	1,461	319	565	7
2,123	1,251	1,403	1,183	1,246	275	517	6
2,134	1,069	1,196	1,077	1,196	200	450	6
2,070	789	998	896	1,077	164	316	6
1,709	674	932	820	953	169	342	7
1,592	596	583	704	945	85	266	5
3,966	920	1,223	1,602	1,734	143	425	30
<u>34,802</u>	<u>17,140</u>	<u>14,791</u>	<u>13,911</u>	<u>14,980</u>	<u>2,727</u>	<u>5,367</u>	<u>114</u>

**Option Selected:**

- Max. – At member’s death, all payments cease. Surviving beneficiary(ies) will receive pro-rated payment for the number of days in the final month.
- Opt. 1 – Guarantees return of the present value of the retirement benefit less the total payments already paid to the member.
- Opt. 2 – Guarantees the same payment to the designated beneficiaries for their lifetime.
- Opt. 3 – Guarantees one half the member’s payment to the designated beneficiaries for their lifetime.
- Opt. 4 – Guarantees return of the member’s accumulated contributions and interest less the member’s accumulated reserves already paid.
- Opt. 5 – Guarantees the same payment to the designated beneficiaries for their lifetime, unless the beneficiaries predecease the respective members. Allowance then increases to the maximum.
- Opt. 6 – Guarantees one half the member’s payment to the designated beneficiaries for their lifetime, unless the beneficiaries predecease the respective members. Allowance then increases to the maximum.
- Opt. 7 – Special option calculation performed by actuary.

SUMMARY OF MEMBERSHIP

	Total	Teachers' Retirement	Teachers' Pension	*Employees' Retirement
<b>From July 7/1/01 to 6/30/02</b>				
Active Members	190,123	9,270	87,086	11,722
Average Final Annual Salary	\$41,383	\$65,175	\$42,704	\$40,135
Retired Members	87,367	29,989	11,931	24,904
Average Monthly Retirement Allowance	\$1,329	\$1,959	\$1,066	\$1,107
Vested Former Members	44,355	1,643	16,397	1,331
<b>From July 7/1/02 to 6/30/03</b>				
Active Members	190,021	8,199	89,099	11,347
Average Final Annual Salary	\$42,808	\$67,755	\$44,520	\$40,723
Retired Members	90,803	30,305	13,370	24,662
Average Monthly Retirement Allowance	\$1,357	\$2,013	\$1,094	\$1,144
Vested Former Members	45,573	1,577	17,284	17,284
<b>From July 7/1/03 to 6/30/04</b>				
Active Members	185,861	7,197	88,765	10,489
Average Final Annual Salary	44,169	69,819	46,337	41,801
Retired Members	94,880	30,598	15,093	24,559
Average Monthly Retirement Allowance	\$1,399	\$2,089	\$1,142	\$1,195
Vested Former Members	46,911	1,478	18,327	1,311
<b>From July 7/1/04 to 6/30/05</b>				
Active Members	188,050	6,255	91,535	9,869
Average Final Annual Salary	\$47,163	\$74,291	\$50,152	\$42,934
Retired Members	100,196	30,921	17,170	24,633
Average Monthly Retirement Allowance	\$1,439	\$2,172	\$1,181	\$1,252
Vested Former Members	47,664	1,351	18,792	1,291
<b>From July 7/1/05 to 6/30/06</b>				
Active Members	191,273	5,449	94,869	10,121
Average Final Annual Salary	\$48,557	\$75,950	\$51,179	\$46,222
Retired Members	103,831	31,138	19,141	24,271
Average Monthly Retirement Allowance	\$1,493	\$2,253	\$1,241	\$1,311
Vested Former Members	49,310	1,229	19,824	1,258

\* Includes members of the Maryland General Assembly and correctional officers.

DATA BY PLAN

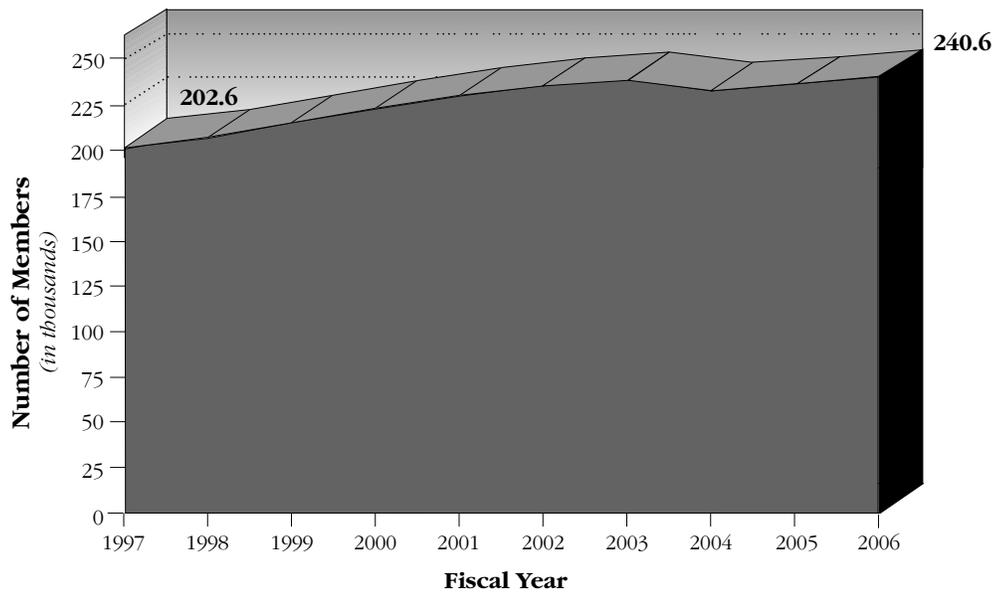
<b>Employees' Pension</b>	<b>Judges' Retirement</b>	<b>State Police Retirement</b>	<b>Law Enforcement Officers' Pension</b>	<b>Local Fire and Police</b>
78,584	281	1,589	1,410	181
\$36,728	\$113,253	\$52,323	\$46,749	\$39,715
18,205	311	1,598	403	26
\$575	\$4,615	\$2,695	\$2,002	\$1,612
24,845	10	27	66	36
77,939	287	1,542	1,481	127
\$38,004	\$115,571	\$52,424	\$46,907	\$36,895
19,929	306	1,695	503	33
\$607	\$4,676	\$2,787	\$2,067	\$1,577
25,212	13	41	62	35
75,955	283	1,445	1,675	52
39,024	117,137	53,655	46,942	34,279
21,913	309	1,790	581	37
\$650	\$4,730	\$2,902	\$2,174	\$1,564
25,626	14	44	81	30
76,787	282	1,439	1,826	57
\$41,509	\$120,206	\$53,934	\$48,700	\$36,586
24,525	316	1,909	708	14
\$693	\$4,871	\$3,000	\$2,295	\$1,225
26,058	15	47	104	6
76,979	296	1,441	2,063	55
\$43,198	\$121,416	\$55,967	\$51,706	\$36,520
26,216	330	1,937	782	16
\$742	\$5,085	\$3,237	\$2,345	\$1,451
26,805	14	58	115	7

TEN-YEAR HISTORY OF MEMBERSHIP BY PLAN

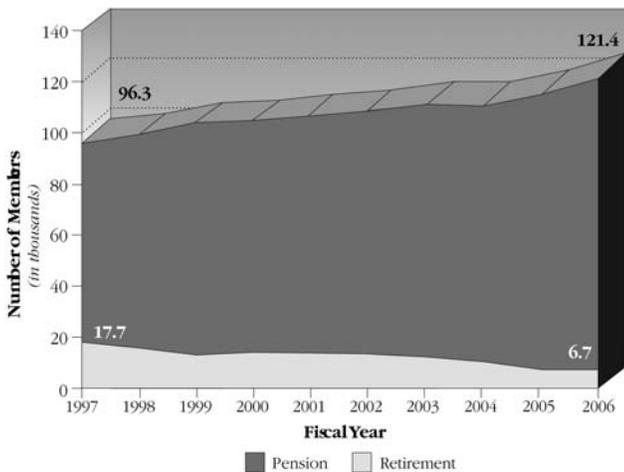
Fiscal Year	Total	Teachers'		Employees'		Judges'	State Police	Law Enforcement Officers'	Local Fire and Police
		Retirement	Pension	Retirement*	Pension	Retirement	Retirement	Pension	
1997	202,568	17,681	78,659	14,912	88,918	282	1,610	328	178
1998	208,139	16,311	83,877	14,521	90,515	289	1,659	776	191
1999	214,339	14,949	88,882	14,034	93,414	296	1,676	892	196
2000	222,100	13,491	94,154	13,614	97,517	296	1,658	1,166	204
2001	227,799	12,126	98,508	13,312	100,420	294	1,602	1,367	170
2002	234,478	10,913	103,483	13,053	103,429	291	1,616	1,476	217
2003	235,594	9,776	106,383	12,696	103,151	300	1,583	1,543	162
2004	232,772	8,675	107,092	11,800	101,581	297	1,498	1,756	82
2005	235,714	7,606	110,327	11,160	102,845	297	1,486	1,930	63
2006	240,583	6,678	114,693	11,398	103,784	310	1,499	2,178	62

Note: Includes vested former members. \*Includes members of the Maryland General Assembly and correctional officers.

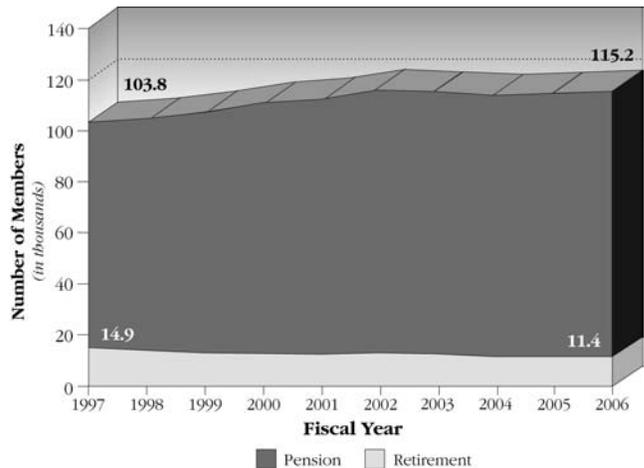
TOTAL SYSTEM MEMBERSHIP



MEMBERSHIP IN TEACHERS' PLANS



MEMBERSHIP IN EMPLOYEES' PLANS

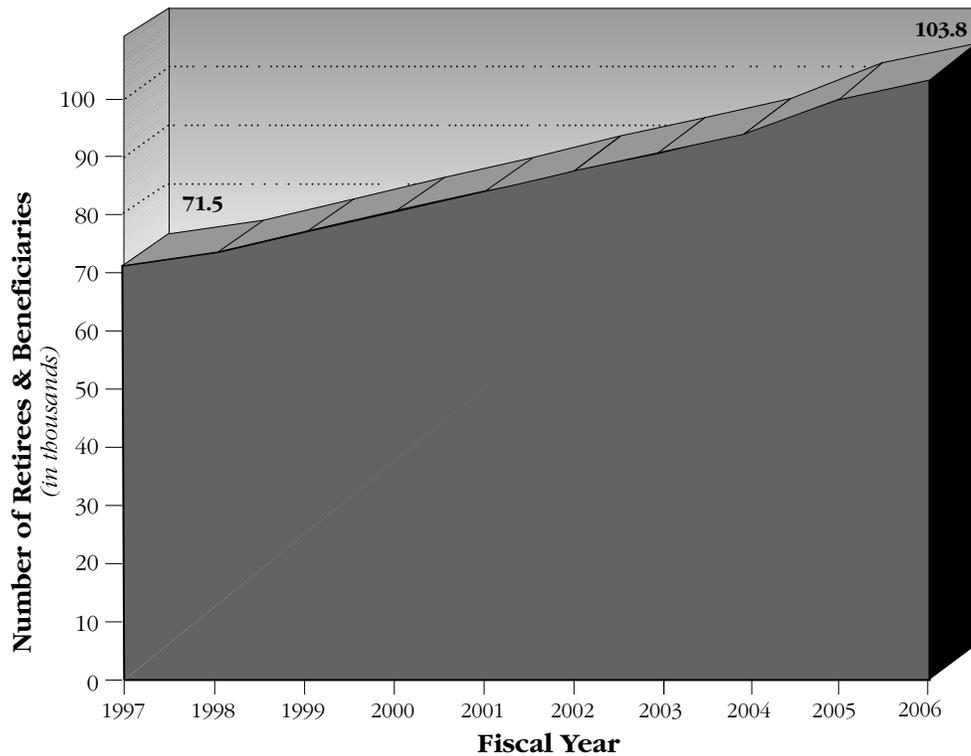


TEN-YEAR HISTORY OF RETIREES AND BENEFICIARIES BY PLAN

Fiscal Year	Total	Teachers' Retirement	Teachers' Pension	Employees' Retirement*	Employees' Pension	Judges' Retirement	State Police Retirement	Law	Local Fire
								Enforcement Officers' Pension	and Police
1997	71,488	27,330	5,481	25,882	11,221	273	1,175	117	9
1998	74,339	27,841	6,499	25,827	12,513	275	1,234	139	11
1999	77,478	28,383	7,674	25,730	13,937	284	1,286	170	14
2000	80,773	29,061	9,084	25,489	15,241	285	1,388	206	19
2001	84,185	29,599	10,527	25,212	16,702	297	1,518	309	21
2002	87,367	29,989	11,931	24,904	18,205	311	1,598	403	26
2003	90,803	30,305	13,370	24,662	19,929	306	1,695	503	33
2004	94,880	30,598	15,093	24,559	21,913	309	1,790	581	37
2005	100,196	30,921	17,170	24,633	24,525	316	1,909	708	14
2006	103,831	31,138	19,144	24,271	26,216	330	1,937	782	16

\* Includes members of the Maryland General Assembly and correctional officers.

TOTAL SYSTEM RETIREES AND BENEFICIARIES



**TEN-YEAR HISTORY OF CHANGES IN FUND BALANCE**  
for the Years Ended June 30,  
(Expressed in Millions)

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Fund balance, beginning of year	\$20,755.7	\$24,542.8	\$28,061.2	\$29,985.6	\$33,110.7	\$29,564.7	\$26,668.5	\$26,727.8	\$30,166.7	\$32,073.7
Contributions	824.7	814.4	855.7	864.9	907.4	779.0	814.5	836.2	879.5	936
Net investment income	3,985.3	3,782.2	2,225.4	3,487.7	(3,138.8)	(2,265.3)	756.7	4,202.6	2,766.4	3,225.6
Benefit and expense payments	(1,022.9)	(1,078.2)	(1,156.7)	(1,227.5)	(1,314.6)	(1,409.9)	(1,511.9)	(1,599.9)	(1,738.9)	(1,864.5)
Fund balance, end of year	<u>\$24,542.8</u>	<u>\$28,061.2</u>	<u>\$29,985.6</u>	<u>\$33,110.7</u>	<u>\$29,564.7</u>	<u>\$26,668.5</u>	<u>\$26,727.8</u>	<u>\$30,166.7</u>	<u>\$32,073.7</u>	<u>\$34,370.8</u>

**TEN-YEAR HISTORY OF EMPLOYER CONTRIBUTION RATES BY PLAN**

Fiscal Year	State						Participating Governmental Units				
	Combined State Contribution Rate	Teachers' Combined Rate	Employees' Combined Rate	Judges' Retirement	State Police Retirement	Law Enforcement Officers' Pension	Combined Participating Governmental Unit Contribution Rate	Local Fire and Police	Law Enforcement Officers' Pension	Employees' Retirement	Employees' Pension
1997	13.50%	16.09%	8.54%	52.56%	17.65%	35.15%	7.92%	16.19%	N/A	10.91%	7.46%
1998	12.90	15.48	8.21	52.49	13.08	26.27	7.04	16.29	N/A	11.96	6.96
1999	11.67	13.99	7.13	52.12	10.91	25.60	6.02	16.42	N/A	10.91	5.91
2000	10.70	12.54	7.15	48.18	1.26	22.96	3.83	14.99	N/A	8.70	3.70
2001	9.31	10.95	5.71	46.75	8.44	23.38	2.95	15.00	N/A	7.81	2.81
2002	7.98	9.35	4.73	42.66	5.83	32.41	1.94	14.85	31.83%	6.75	1.75
2003	8.01	9.35	4.73	43.92	5.78	36.10	1.95	14.78	29.59	6.95	1.95
2004	8.06	9.35	4.73	43.74	7.58	35.13	2.87	14.31	30.21	7.59	2.59
2005	7.97	9.35	4.73	36.72	–	37.73	5.28	20.44	32.10	9.87	4.87
2006	8.46	9.35	5.76	41.12	8.22	38.47	5.36	20.44	32.67	9.80	4.80

TEN-YEAR HISTORY OF REVENUES BY SOURCE AND EXPENSES BY TYPE  
(Expressed in Thousands)

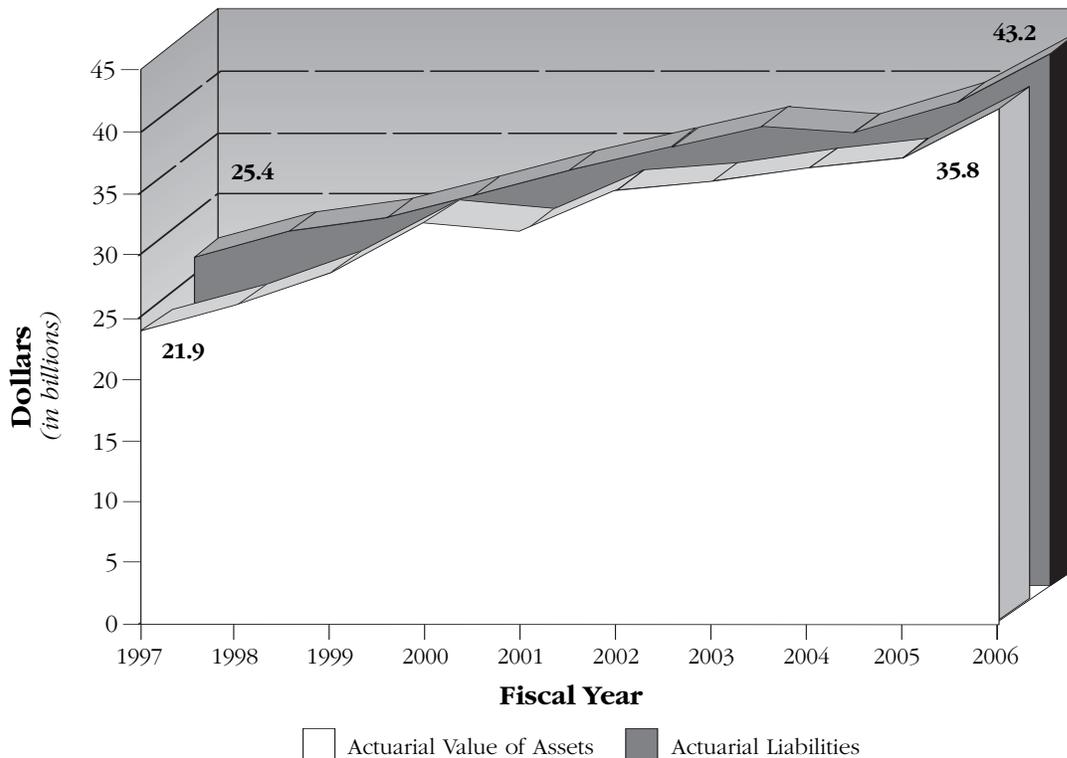
<b>REVENUES</b>						
<b>Fiscal Year</b>	<b>Members' Contributions</b>	<b>Employers' and Other Contributions</b>	<b>Annual Covered Payroll</b>	<b>Employers' and Other Contributions as a Percent of Covered Payroll</b>	<b>Net Investment Income</b>	<b>Total Revenues</b>
1997	\$ 84,444	\$740,258	\$5,657,385	13.08%	\$ 3,985,260	\$ 4,809,962
1998	78,609	735,788	5,900,456	12.47	3,782,237	4,596,634
1999	162,342	693,353	6,312,417	10.98	2,225,398	3,081,093
2000	182,507	682,422	6,725,870	10.15	3,487,722	4,352,651
2001	189,769	717,576	7,255,036	8.74	(3,138,763)	(2,231,418)
2002	199,304	579,718	7,867,794	7.39	(2,265,315)	(1,486,293)
2003	207,584	606,900	8,134,419	7.46	756,747	1,571,231
2004	204,158	632,052	8,069,481	7.83	4,202,632	5,038,842
2005	208,997	670,554	8,603,761	7.79	2,766,389	3,645,940
2006	215,077	720,876	9,287,576	7.76	3,225,649	4,161,602

<b>EXPENSES</b>				
<b>Fiscal Year</b>	<b>Benefits</b>	<b>Administrative Expenses</b>	<b>Refunds</b>	<b>Total</b>
1997	\$ 973,103	\$ 9,717	\$ 40,060	\$1,022,880
1998	1,047,774	10,441	20,007	1,078,222
1999	1,115,086	24,742	16,898	1,156,726
2000	1,190,954	19,751	16,805	1,227,510
2001	1,272,804	24,823	16,977	1,314,604
2002	1,372,325	20,064	17,476	1,409,865
2003	1,474,257	21,352	16,310	1,511,919
2004	1,570,622	17,376	11,942	1,599,940
2005	1,697,397	22,386	19,162	1,738,945
2006	1,829,468	18,579	16,455	1,864,502

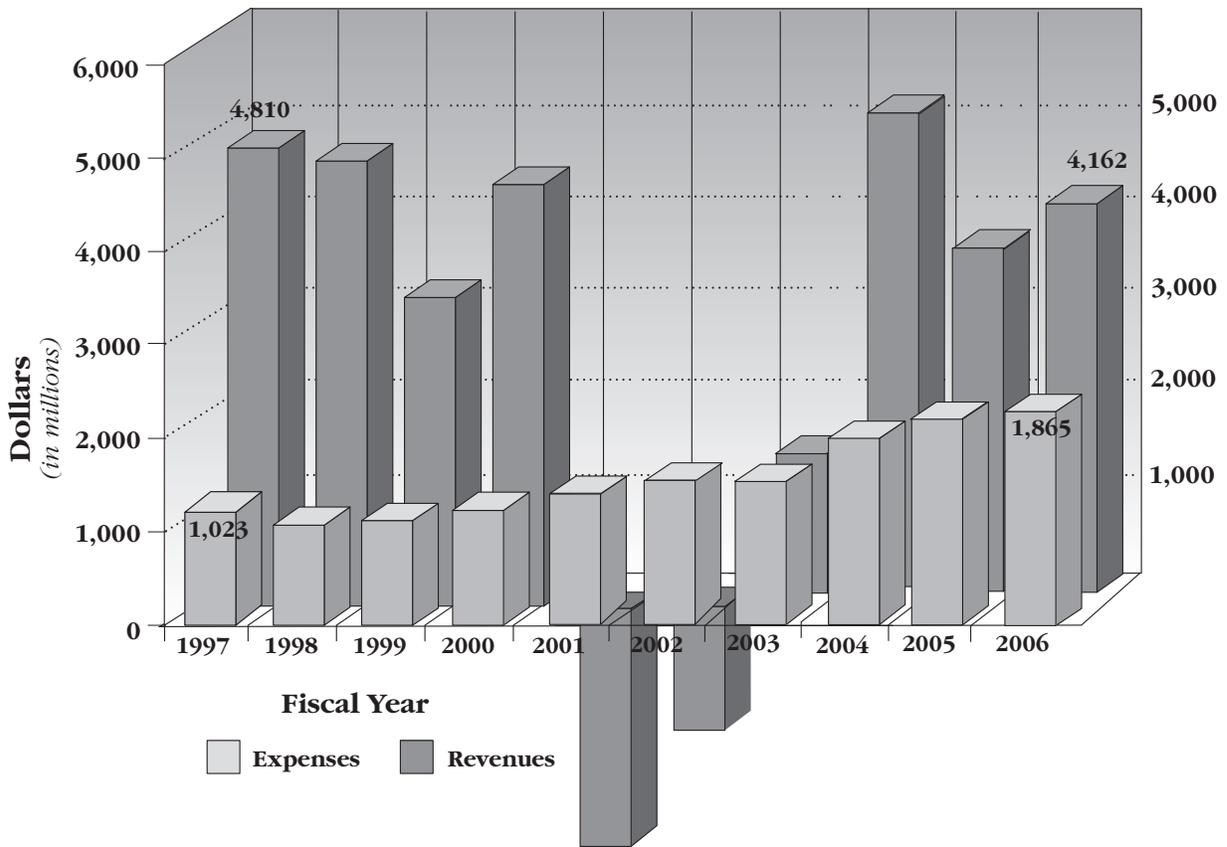
**EMPLOYER CONTRIBUTIONS RECEIVED**  
(Expressed in Thousands)

	<b>Teachers' Retirement and Pension System</b>	<b>Employees' Retirement and Pension System</b>	<b>Judges' Retirement System</b>	<b>State Police Retirement System</b>	<b>Local Fire and Police System</b>	<b>Law Enforcement Officers' Pension System</b>	<b>Totals</b>	
							<b>2006</b>	<b>2005</b>
<b>EMPLOYER CONTRIBUTIONS:</b>								
Normal (A)	\$ 364,051	\$ 287,517	\$ 9,887	\$ 6,681	\$ 221	\$ 20,052	\$ 688,408	\$ 667,403
Unfunded Actuarial Liability	78,010	(69,654)	4,555	0	231	15,166	28,399	(1,357)
<b>Total Employer Contributions</b>	<b>\$ 442,061</b>	<b>\$ 217,863</b>	<b>\$ 14,442</b>	<b>\$ 6,681</b>	<b>\$ 542</b>	<b>\$ 35,216</b>	<b>\$ 716,806</b>	<b>\$ 666,046</b>
<b>CONTRIBUTION RATES AS A PERCENTAGE OF PAYROLL:</b>								
<b>State:</b>								
Normal	7.70%	7.50%	28.15%	25.05%	—	21.25%	8.02%	8.02%
Unfunded Actuarial Liability	1.65%	- 1.74%	12.97%	- 16.83%	—	17.22%	0.44%	-0.05%
<b>Total State</b>	<b>9.35%</b>	<b>5.76%</b>	<b>41.12%</b>	<b>0.00%</b>	<b>0.00%</b>	<b>38.47%</b>	<b>8.46%</b>	<b>7.97%</b>
<b>Participating Governmental Units:</b>								
Normal	—	6.55%	—	—	11.25%	20.90%	6.83%	6.76%
Unfunded Actuarial Liability	—	- 1.75%	—	—	16.36%	11.77%	- 1.47%	- 1.48%
<b>Total Municipal</b>	<b>0.00%</b>	<b>4.80%</b>	<b>0.00%</b>	<b>0.00%</b>	<b>27.61%</b>	<b>32.67%</b>	<b>5.36%</b>	<b>5.28%</b>

**TEN-YEAR HISTORY OF FUNDING PROGRESS**



TEN-YEAR HISTORY OF REVENUES VS. EXPENSES



PRINCIPAL PARTICIPATING EMPLOYERS  
CURRENT YEAR AND NINE YEARS AGO

	2006			1997		
	Covered Employees	Rank	Percentage of Total System	Covered Employees	Rank	Percentage of Total System
<b>Participating Government</b>						
State of Maryland	297,091	1	86%	240,238	1	88%
All other (Participating Municipalities)	47,323	2	14%	33,818	2	12%
Total System	344,414			274,056		

**Governmental Units Participating in the Systems**

as of June 30, 2006

Allegany Community College	Garrett County Board of Education	Prince Georges County Crossing Guards
Allegany County Board of Education	Garrett County Community Action Committee	Prince Georges County Government
Allegany County Commission	Garrett County Office for Children, Youth and Family	Prince Georges County Memorial Library
Allegany County Housing Authority	Greenbelt, City of	Princess Anne, Town of
Allegany County Library	Hagerstown, City of	Queen Anne's County Board of Education
Allegany County Transit Authority	Hagerstown Junior College	Queen Anne's County Commission
Annapolis, City of	Hancock, Town of	Queenstown, Town of
Anne Arundel County Board of Education	Harford Community College	Regional Educational Service Agency of Appalachian Maryland
Anne Arundel County Community College	Harford County Board of Education	Ridgely, Town of
Anne Arundel County Economic Opportunity Commission	Harford County Government	Rockhall, Town of
Berlin, Town of	Harford County Library	St. Mary's County Board of Education
Brunswick, Town of	Housing Authority of Cambridge	St. Mary's County Commission
Calvert County Board of Education	Howard Community College	Salisbury, City of
Cambridge, City of	Howard County Board of Education	Shore up!
Caroline County Board of Education	Howard County Community Action Committee	Snow Hill, Town of
Carroll County Board of Education	Hurlock, Town of	Somerset County Board of Education
Carroll County Public Library	Hyattsville, City of	Somerset County Commission
Carroll Soil Conservation District	Kent County Board of Education	Somerset County Sanitary District, Inc.
Catoctin & Frederick Soil Conservation District	Kent County Commissioners	Southern Maryland Tri-County Community Action Committee
Cecil County Board of Education	LaPlata, Town of	St. Mary's County Metropolitan Commission
Cecil County Commission	Manchester, Town of	St. Michaels, Commissioners of
Cecil County Library	Maryland Health & Higher Education Facilities Authority	Takoma Park, City of
Charles County Community College	Middletown, Town of	Talbot County Board of Education
Chesapeake Bay Commission	Montgomery College	Talbot County Council
Chestertown, Town of	Mount Airy, Town of	Taneytown, Town of
Cheverly, Town of	Mount Rainier, City of	Thurmont, Town of
Cresaptown Civic Improvement Association	New Carrollton, City of	Tri-County Council of Western Maryland
Crisfield, City of	North Beach, Town of	Tri-County for the Lower Eastern Shore
Crisfield Housing Authority	Northeast Maryland Waste Disposal Authority	Upper Marlboro, Town of
Cumberland, City of	Oakland, Town of	Walkersville, Town of
Cumberland, City of – Police Department	Oxford, Town of	Washington County Board of Education
Denton, Town of	Pocomoke City	Washington County Board of License Commission
District Heights, City of	Preston, Town of	Washington County Library
Dorchester County Board of Education	Prince Georges Community College	Westminister, City of
Dorchester County Commission	Prince Georges County Board of Education	Worcester County Board of Education
Dorchester County Roads Board		Worcester County Commission
Eastern Shore Regional Library		Worcester County Liquor Board
Frederick County Board of Education		Wor-Wic Tech Community College
Fruitland, City of		

**Withdrawn Governmental Units**

Allegany County Government	Howard County Economic Development Authority	St. Mary's Nursing Home
Anne Arundel County Government	Howard County Government	University of Maryland Medical System
Baltimore Metropolitan Council	Interstate Commission on the Potomac River Basin	Washington County Commission
Bethesda Fire Department	Lexington Market Authority	Washington County License Commissioners
Calvert County Commission	Maryland Environmental Services	Washington County Roads Board
Caroline County Roads Board	Maryland National Capital Park & Planning Commission	Washington County Sanitary District
Carroll County Government	Montgomery County Board of Education	Washington Suburban Sanitary Commission
Chevy Chase Fire Department	Montgomery County Government	Wicomico County Department of Recreation and Parks
Elkton, Town of	Montgomery County Public Library	Wicomico County Roads Board
Frederick County Government	Rockville, City of	
Garrett County Commission		
Garrett County Roads Board		
Harford County Liquor Board		

### **LAW ENFORCEMENT OFFICERS' PENSION SYSTEM**

**The Law Enforcement Officers' Pension System was established by the General Assembly in 1990. This system was designed specifically for law enforcement officers employed by the Department of Natural Resources (DNR). In recent years this system has been expanded to include other Maryland State and local government law enforcement officer groups.**

## TEACHERS' RETIREMENT SYSTEM

## A COMPOSITE PICTURE

	2006	2005
<b>Total Membership</b>		
Active Vested	5,445	6,254
Active Non-vested	4	1
Vested Former Members	1,229	1,351
Retired Members	31,138	30,921
<b>Active Members</b>		
Number	5,449	6,255
Average Age	57.4	56.8
Average Years of Service	32.0	29.9
Average Annual Salary	\$75,950	\$74,291
<b>Retirees &amp; Beneficiaries</b>		
Number	31,138	30,921
Average Age	73.1	72.8
Average Monthly Benefit	\$ 2,253	\$ 2,172

**THE TEACHERS' RETIREMENT SYSTEM (TRS)** was established on August 1, 1927 and is administered in accordance with the State Personnel and Pensions Article of the Annotated Code of Maryland. Prior to January 1, 1980, membership in the TRS was a condition of employment for State and local teachers and certain board of education, public library and community college employees, unless those who were eligible elected to participate in an optional retirement program. Effective July 1, 1971 Baltimore City teachers and retired teachers were included in the TRS.

Effective January 1, 1980, the TRS was effectively closed to new membership when the Teachers' Pension System (TPS) was established. Individuals who were members of the TRS on December 31, 1979, continue their TRS membership unless, and until, they elected to transfer to the TPS prior to January 1, 2005.

### Member Contributions

All member contributions to the TRS are based on a specified percentage of annual earnable compensation. Members who elected in 1984 to receive unlimited future cost-of-living adjustments (COLA) contribute 7% if enrolled after June 30, 1973. Members enrolled before July 1, 1973 contribute the lesser of 7% or 2% more than the rate of contribution in effect on the date of their enrollment. This option is referred to as Selection A (Unlimited COLA).

Members who elected in 1984 to receive limited future COLA's contribute 5% if enrolled after June 30, 1973. Members enrolled before July 1, 1973 contribute the lesser of 5% or the rate of contribution in effect on the date of their enrollment. This option is referred to as Selection B (Limited COLA).

All other TRS members contribute 2%. This option is referred to as Selection C (Combination Formula), that provides a two-part benefit calculation upon retirement.

Members who are in Selection A, B, or C will remain in these until their retirement. As of January 1, 2005, they were no longer permitted to change selections.

### Service Retirement Allowances

**Eligibility** — TRS members are eligible for full service retirement allowances upon attaining age 60 or upon accumulating 30 years of eligibility service regardless of age.

**Allowances** — Full service retirement allowances equal 1/55 (1.8%) of the highest three years' average final salary (AFS) multiplied by the number of years and months of accumulated creditable service. Allowances for members who fail to make all required contributions are reduced by the actuarial equivalent of the total unpaid contributions plus interest to date of retirement. Service is accrued based on a full normal school year (ten months).

### Early Retirement Allowances

**Eligibility** — TRS members are eligible for early service retirement allowances upon accumulating at least 25 years of eligibility service prior to attaining age 60.

**Allowances** — Early service retirement allowances equal the amount payable for a full service retirement reduced by 0.5% for each month by which the retirement date precedes the earlier of the date on which the member reaches age 60, or the date on which the member would have completed 30 years of service. The maximum reduction for a TRS member is 30 percent. The maximum reduction for a TRS member who elected Selection C is 42% on the second part of the benefit calculation.

### Ordinary Disability Retirement Allowances

**Eligibility** — TRS members are eligible for ordinary disability retirement allowances upon completing five years of eligibility service and receiving certification from the Medical Board that they are permanently incapable of performing their necessary job functions.

**Allowances** — Ordinary disability retirement allowances generally equal 1/55 (1.8%) of the highest three years' AFS multiplied by the number of years of accumulated creditable service. However, the ordinary disability benefits can be no greater than 1.8% of AFS for each year of creditable service the members would have received had they continued to work until age 60.

### **Accidental Disability Retirement Allowances**

**Eligibility** — TRS members are eligible for accidental disability benefits if the Medical Board certifies that, in the course of job performance and as the direct result of an accidental injury, they became totally and permanently disabled.

**Allowances** — Accidental disability allowances equal the sum of an annuity determined as the actuarial value of the members' accumulated contributions, plus 2/3 (66.7%) of AFS. Allowances may not exceed the members' AFS.

### **Death Benefits**

**Eligibility** — To be eligible for death benefits, TRS members must have either accumulated at least one year of eligibility service prior to the date of death or died in the line of duty.

**Benefits** — The benefit provided upon death for TRS members equals the members' annual earnable compensation at the time of death plus accumulated contributions. Under certain circumstances, surviving spouses who were named as sole primary beneficiaries may elect to receive either the aforementioned lump sum payment, or a monthly allowance calculated under Option 2 (100% survivor option).

### **Vested Retirement Allowances**

**Eligibility** — TRS members are eligible for vested retirement allowances after separation from service and upon reaching normal retirement age, provided that at least five years of eligibility service was accumulated prior to separation.

**Allowances** — Vested allowances equal the normal service retirement allowances computed on the basis of the members' accumulated creditable service and AFS at the point of separation.

If members do not withdraw their contributions, and die before attaining age 60, their accumulated contributions are returned to the designated beneficiary.

### **Cost-of-Living Adjustments**

Retirement allowances are adjusted each year based on the Consumer Price Index. Cost-of-living adjustments (COLAs) are effective July 1st of each year and are applied to all allowances payable for the year. However, the method by which the annual COLAs are computed depends upon elections made by members who were active on July 1, 1984 (or within 90 days of returning to service, for members who were inactive on July 1, 1984). Each option is explained in the following column.

**Selection A (Unlimited COLA)** — TRS members who elected Selection A, agreed to contribute no more than 7% of earnable compensation in return for unlimited annual COLAs after retirement.

**Selection B (Limited COLA)** — TRS members who elected Selection B, agreed to contribute no more than 5% of earnable com-

penensation in return for COLAs that are limited to 5% annually after retirement.

**Selection C (Combination Formula)** — TRS members who elected Selection C, agreed to contribute no more than 2% of earnable compensation in return for COLAs that, similar to the retirement benefit, are divided into two parts.

**Part 1:** For creditable service accumulated before electing Selection C, an allowance is calculated using the formula for determining a full service TRS retirement allowance. The COLAs are unlimited unless the member elected Selection B prior to electing Selection C, in which case COLAs are limited to 5%.

**Part 2:** For creditable service accumulated after electing Selection C, an allowance is calculated using the formula for determining a full service TPS pension allowance. The COLAs are limited to 3%.

### **Optional Forms of Payment**

**Option 1:** Payment guarantees a cash reserve equal to the excess of the present value of the retirement allowance at the date of retirement minus the total amount of payments (less COLAs) made to the date of death.

**Option 2:** 100% joint and survivor annuity.

**Option 3:** 50% joint and survivor annuity.

**Option 4:** Payment guarantees a minimum return of the members' accumulated contributions.

**Option 5:** 100% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

**Option 6:** 50% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

Except for a spouse or disabled child, the beneficiary designated under Option 2 or 5 cannot be more than 10 years younger than the retiree (IRS Regulation).

### **Workers' Compensation Benefits Reduction**

Disability retirement allowances are generally reduced by workers' compensation benefits paid after retirement if, and to the extent that, such benefits are for the same injury and the same period of time for which the retirement benefits are payable. The workers' compensation benefit reduction cannot reduce any retirement allowance to less than the amount necessary to cover the retiree's monthly health insurance premiums.

### **Pension Changes**

Effective July 1, 2006, the employee contribution for selection C, Part 2 increases to 3%.

## TEACHERS' PENSION SYSTEM

## A COMPOSITE PICTURE

	2006	2005
<b>Total Membership</b>		
Active Vested	63,968	59,944
Active Non-vested	30,901	31,591
Vested Former Members	19,824	18,792
Retired Members	19,141	17,170
<b>Active Members</b>		
Number	94,869	91,535
Average Age	43.4	43.7
Average Years of Service	11.0	10.6
Average Annual Salary	\$51,179	\$50,152
<b>Retirees &amp; Beneficiaries</b>		
Number	19,141	17,170
Average Age	65.6	65.7
Average Monthly Benefit	\$ 1,241	\$ 1,181

**THE TEACHERS' PENSION SYSTEM (TPS)** was established on January 1, 1980 and is administered in accordance with the State Personnel and Pensions Article of the Annotated Code of Maryland. Membership in the TPS was a condition of employment for all State and local teachers and certain board of education, public library and community college employees hired after December 31, 1979, (unless those who are eligible elect to participate in an optional retirement program) until July 1, 1998. As of July 1, 1998, all TPS members, except for those who transfer from the TRS after April 1, 1998, became members of the Teachers' Contributory Pension System (TCPS).

### Member Contributions

All TPS members are required to contribute 5% of earnable compensation in excess of the social security taxable wage base. Members of the TCPS are required to contribute 2% of earnable compensation.

### Service Pension Allowances

**Eligibility** — TPS and TCPS members are eligible for full service pension allowances upon accumulating 30 years of eligibility service regardless of age. Absent 30 years of eligibility service, members must meet one of the following conditions to be eligible for full service pension allowances:

- age 62, & five years of eligibility service
- age 63, & four years of eligibility service
- age 64, & three years of eligibility service
- age 65 or older, & two years of eligibility service

**Allowances** — For TPS members, full service pension allowances equal 0.8% of the highest three consecutive years' AFS up to the Social Security Integration Level (SSIL), plus 1.5% of AFS in excess of the SSIL, multiplied by the number of years of accumulated creditable service.

For the purpose of computing pension allowances, the SSIL is the average of the social security wage bases for the 35 years immediately prior to the year of retirement.

For TCPS members, full service pension allowances equals 1.2% of AFS for service accrued prior to July 1, 1998, (or if greater the TPS benefit noted above on service prior to July 1, 1998), plus 1.4% of AFS for service accrued on and after July 1, 1998.

### Early Service Pension Allowances

**Eligibility** — TPS and TCPS members are eligible for early service pension allowances upon attaining age 55 with at least 15 years of eligibility service.

**Allowances** — Early service pension allowances for both the TPS and TCPS equal the amount payable for a full service pension reduced by 0.5% for each month by which the retirement date precedes the date on which the members reach age 62. The maximum reduction is 42 percent.

### Ordinary Disability Pension Allowances

**Eligibility** — TPS and TCPS members are eligible for ordinary disability pension allowances upon completing five years of eligibility service and receiving certification from the Medical Board that they are permanently incapable of performing their necessary job functions.

**Allowances** — For TPS and TCPS members, ordinary disability pension allowances equal the full service pension allowances if the members are at least age 62 on the date of retirement. Otherwise, the allowances equal the full service pension allowances computed as though the members had continued to accrue service credits until age 62 without any change in the rate of earnable compensation.

### Accidental Disability Pension Allowances

**Eligibility** — TPS and TCPS members are eligible for accidental disability pension allowances if the Medical Board certifies that, in the course of their job performance and as the direct result of an accidental injury, they became totally and permanently disabled.

**Allowances** — For TPS and TCPS members, accidental disability pension allowances equal the sum of an annuity determined as the actuarial value of the members' accumulated contributions, and 2/3 (66.7%) of AFS. Allowances may not exceed the members' AFS.

### **Death Benefits**

**Eligibility** — To be eligible for death benefits, TPS and TCPS members must have either accumulated at least one year of eligibility service prior to the date of death or died in the line of duty.

**Benefits** — The benefit provided upon death of TPS or TCPS members equals the members' annual earnable compensation on the date of death plus accumulated contributions. Under certain circumstances, surviving spouses who were named as sole primary beneficiaries may elect to receive either the aforementioned lump sum payment, or a monthly allowance calculated under Option 2 (100% survivor option).

If at the time of death, the members had:

- accrued at least 25 years of eligibility service, or
- attained age 55 with at least 15 years of eligibility service, or
- attained age 62, then

the survivor's allowance is determined as if the members had been eligible to retire, and had in fact retired.

### **Vested Pension Allowances**

**Eligibility** — TPS and TCPS members are eligible for vested pension allowances after separation from service and upon reaching age 62, provided that at least five years of eligibility service was accumulated prior to separation. TPS and TCPS members may be eligible for reduced vested pension allowances upon attaining age 55 with at least 15 years of eligibility service. Vested allowances are reduced by 0.5% for each month by which the allowance commencement date precedes the date on which the members attain age 62.

**Allowances** — For the TPS and TCPS, vested allowances equal the normal service pension allowances computed on the basis of the members' accumulated creditable service and AFS at the point of separation.

TPS members who elect to withdraw their accumulated contributions remain eligible to receive the employer-provided share of the vested benefit. If members do not withdraw their contributions, and die before attaining age 62, their accumulated contributions are returned to the designated beneficiary.

### **Cost-of-Living Adjustments**

Retirement allowances for TPS and TCPS members are adjusted each year based on the Consumer Price Index. COLAs are effective July 1st of each year and, beginning July 1998, are compounded annually for TCPS and TPS members. The Systems limit the increase a retiree may receive to a maximum of 3%.

### **Optional Forms of Payment**

**Option 1:** Payment guarantees a cash reserve equal to the excess of the present value of the pension allowance at the date of retirement minus the total amount of payments (less COLAs) made to the date of death.

**Option 2:** 100% joint and survivor annuity.

**Option 3:** 50% joint and survivor annuity.

**Option 4:** Payment guarantees a minimum return of the members' accumulated contributions.

**Option 5:** 100% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

**Option 6:** 50% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

Except for a spouse or disabled child, the beneficiary designated under Option 2 or 5 cannot be more than 10 years younger than the retiree (IRS regulation).

### **Workers' Compensation Benefits Reduction**

Disability retirement allowances are generally reduced by workers' compensation benefits paid after retirement if, and to the extent that, such benefits are for the same injury and the same period of time for which the retirement benefits were paid. The workers' compensation benefit reduction cannot reduce any retirement allowance to less than the amount necessary to cover the retiree's monthly health insurance premiums.

### **Pension Changes**

Effective July 1, 2006 there is an Alternate Contributory Pension Selection (ACPS) which applies to all TPS members except for those who transferred from the TRS after April 1, 1998. Under the ACPS, service accrued July 1, 1998 is 1.8% (increased from 1.4%) per year of service.

## EMPLOYEES' RETIREMENT SYSTEM

## A COMPOSITE PICTURE

	2006	2005
<b>Total Membership</b>		
Active Vested	10,120	7,539
Active Non-vested	1	2,330
Vested Former Members	1,258	1,291
Retired Members	24,271	24,633
<b>Active Members</b>		
Number	10,121	9,869
Average Age	449	45.1
Average Years of Service	16.2	16.2
Average Annual Salary	\$46,222	\$42,934
<b>Retirees &amp; Beneficiaries</b>		
Number	24,271	24,633
Average Age	73.3	73.3
Average Monthly Benefit	\$ 1,311	\$ 1,252

**THE EMPLOYEES' RETIREMENT SYSTEM (ERS)** was established on October 1, 1941 and is administered in accordance with the State Personnel and Pensions Article of the Annotated Code of Maryland. Prior to January 1, 1980, membership in the ERS was a condition of employment for all State employees (other than those eligible for participation in another system) and employees of participating governmental units. For certain elected and appointed officials, participation in ERS was optional.

Effective January 1, 1980, the ERS was effectively closed to new membership when the Employees' Pension System (EPS) was established. Individuals who were members of the ERS on December 31, 1979, continue their ERS membership unless, and until, they elect to transfer to the EPS, prior to January 1, 2005..

### Member Contributions

All member contributions to the ERS are based on a specified percentage of annual earnable compensation. Members who elected in 1984 to receive unlimited future COLAs contribute 7% if enrolled after June 30, 1973. Members enrolled before July 1, 1973 contribute the lesser of 7% or 2% more than the rate of contribution in effect on their date of enrollment. This option is referred to as Selection A (Unlimited COLA).

Members who elected in 1984 to receive limited future COLAs contribute 5% if enrolled after June 30, 1973. Members enrolled before July 1, 1973 contribute the lesser of 5% or the rate of contribution in effect on the date of their enrollment. This option is referred to as Selection B (Limited COLA).

Members who are State employees as well as members whose

employer elected to participate in the Employees' Contributory Pension System (ECPS) contribute 2% of earnable compensation under an option that provides a two-part benefit calculation upon retirement. This option is referred to as Selection C (Combination Formula). All other ERS members whose employer elected not to participate in the ECPS contribute 5% of the portion of annual earnable compensation in excess of the social security wage base under Selection C.

Members who are in Selection A, B, or C will remain in these until their retirement. As of January 1, 2005, they were no longer permitted to change selections.

### Service Retirement Allowances

**Eligibility** — ERS members are eligible for full service retirement allowances upon attaining age 60 or upon accumulating 30 years of eligibility service regardless of age.

**Allowances** — Full service retirement allowances equal 1/55 (1.8%) of the highest three years' AFS multiplied by the number of years and months of accumulated creditable service. Allowances for members who fail to make all required contributions are reduced by the actuarial equivalent of the total unpaid contributions plus interest to date of retirement.

### Early Retirement Allowances

**Eligibility** — ERS members are eligible for early service retirement allowances upon accumulating at least 25 years of eligibility service prior to attaining age 60.

**Allowances** — Early service retirement allowances equal the amount payable for a full service retirement reduced by 0.5% for each month by which the retirement date precedes the earlier of the date on which the member reaches age 60, or the date on which the member would have completed 30 years of service. The maximum reduction for an ERS member is 30 percent. The maximum reduction for an ERS member who elected Selection C is 42% on the second part of the benefit calculation.

### Ordinary Disability Retirement Allowances

**Eligibility** — ERS members are eligible for ordinary disability retirement allowances upon completing five years of eligibility service and receiving certification from the Medical Board that they are permanently incapable of performing their necessary job functions.

**Allowances** — Ordinary disability retirement allowances generally equal 1/55 (1.8%) of the highest three years' AFS multiplied by the number of years of accumulated creditable service. However, the ordinary disability benefits can be no greater than 1.8% of AFS for each year of creditable service the members would have received had they continued to work until age 60.

### **Accidental Disability Retirement Allowances**

**Eligibility** — ERS members are eligible for accidental disability benefits if the Medical Board certifies that, in the course of job performance and as the direct result of an accidental injury, they became totally and permanently disabled.

**Allowances** — Accidental disability allowances equal the sum of an annuity determined as the actuarial value of the members' accumulated contributions, plus 2/3 (66.7%) of AFS. Allowances may not exceed the members' AFS.

### **Death Benefits**

**Eligibility** — To be eligible for death benefits, ERS members must have either accumulated at least one year of eligibility service prior to the date of death or died in the line of duty.

**Benefits** — The benefit provided upon death for ERS members equals the members' annual earnable compensation at the time of death plus accumulated contributions. Under certain circumstances, surviving spouses who were named sole primary beneficiaries may elect to receive either the aforementioned lump sum payment, or a monthly allowance calculated under Option 2 (100% survivor option).

### **Vested Retirement Allowances**

**Eligibility** — ERS members are eligible for vested retirement allowances after separation from service and upon reaching normal retirement age, provided that at least five years of eligibility service was accumulated prior to separation.

**Allowances** — Vested allowances equal the normal service retirement allowances computed on the basis of the members' accumulated creditable service and AFS at the point of separation.

If members do not withdraw their contributions, and die before attaining age 60, their accumulated contributions are returned to the designated beneficiary.

### **Cost-of-Living Adjustments**

Retirement allowances are adjusted each year based on the Consumer Price Index. COLAs are effective July 1st of each year and are applied to all allowances payable for the year. However, the method by which the annual COLAs are computed depends upon elections made by members who were active on July 1, 1984 (or within 90 days of returning to service for members who were inactive on July 1, 1984). Each option is explained below.

**Selection A (Unlimited COLA)** — ERS members who elected Selection A, agreed to contribute no more than 7% of earnable compensation in return for unlimited annual COLAs after retirement.

**Selection B (Limited COLA)** — ERS members who elected Selection B, agreed to contribute no more than 5% of earnable compensation in return for COLAs that are limited to 5% annually after retirement.

**Selection C (Combination Formula)** — ERS members who elected Selection C, agreed to contribute 2% of earnable compensation (or 5% of earnable compensation in excess of the social security wage base if the employer did not elect to participate in the ECPS) in return for COLAs that, similar to the retirement benefit, are divided into two parts:

**Part 1:** For creditable service accumulated before electing Selection C, an allowance is calculated using the formula for determining a full service ERS retirement allowance. The COLAs are unlimited unless the members elected Selection B prior to electing Selection C, in which case COLAs are limited to 5%.

**Part 2:** For creditable service accumulated after electing Selection C, an allowance is calculated using the formula for determining a full service EPS pension allowance. Generally, the COLAs are limited to 3%; however, if the employers do not participate in the ECPS, the COLA's are limited to 3% of the initial allowance.

### **Optional Forms of Payment**

**Option 1:** Payment guarantees a cash reserve equal to the excess of the present value of the retirement allowance at the date of retirement minus the total amount of payments (less COLA's) made to the date of death.

**Option 2:** 100% joint and survivor annuity.

**Option 3:** 50% joint and survivor annuity.

**Option 4:** Payment guarantees a minimum return of the members' accumulated contributions.

**Option 5:** 100% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

**Option 6:** 50% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

Except for a spouse or disabled child, the beneficiary designated under Option 2 or 5 cannot be more than 10 years younger than the retiree (IRS regulation).

### **Workers' Compensation Benefits Reduction**

Disability retirement allowances, except for employees of participating governmental units, are generally reduced by workers' compensation benefits paid after retirement if, and to the extent that, such benefits are for the same injury and the same period of time for which the retirement benefits are payable. The workers' compensation benefit reduction cannot reduce any retirement allowance to less than the amount necessary to cover the retiree's monthly health insurance premiums.

### **Miscellaneous Provisions for Members of the Maryland General Assembly**

Upon attaining age 60 with at least eight years of eligibility service, members of the Maryland General Assembly are eligible for a

service retirement allowance. The allowance is equal to 3% of the current salary for an active legislator multiplied by the number of years of accumulated creditable service (to a maximum of 22 years, 3 months). The maximum benefit payable is two-thirds of the current legislative salary.

Reduced benefits are payable upon attaining age 50 with at least eight years of eligibility service. Early service retirement allowances equal the amount payable for a full service retirement reduced by 0.5% for each month by which the retirement date precedes the date on which the member reaches age 60.

Legislators contribute 5% of annual earnable compensation during the first 22 years and 3 months of service, after which no employee contributions are required. If legislators are separated from service before accumulating eight years of eligibility service, they may elect to continue to contribute an amount equal to the combined member and employer contributions until the date the members would have completed eight years of eligibility service. By doing so, such legislators would be eligible for a retirement allowance equal to 24% of the current salary for an active legislator, payable at age 60 (or a reduced benefit upon attaining age 50).

Legislators who have a minimum 8 years of service and who are certified as disabled may resign their positions and receive a normal service retirement allowance. Upon the death of a legislator, the surviving spouse receives 50% of the amount to which the legislator would have been entitled. However, the surviving spouse of a legislator who dies in office with fewer than eight years of eligibility service will receive a lump sum death benefit

equal to the sum of the legislator's annual earnable compensation at the time of death, plus accumulated contributions.

Legislators' retirement allowances are adjusted based on changes in the salaries of current members of the General Assembly.

### **Miscellaneous Provisions for State Correctional Officers**

State correctional officers, within certain grades, become members of the Correctional Officers' Retirement System (CORS) as a condition of employment. Correctional officers are eligible for normal service retirement allowances upon accumulating 20 years of eligibility service. Members are eligible to receive vested retirement allowance payments upon attaining age 55. For administrative convenience, the CORS is accounted for as a component of the ERS.

### **Pension Changes**

ERS effective July 1, 2006:

The employee contribution Selection C, Part 2 increases to 3% if the employer elects to participate in the Alternate Contributory Pension Selection.

CORS effective, July 1, 2006:

1. Dietary, maintenance and supply correctional officers became eligible for CORS membership.
2. Local governments are eligible to participate in CORS for detention center officers.

## EMPLOYEES' PENSION SYSTEM

### A COMPOSITE PICTURE

	2006	2005
<b>Total Membership</b>		
Active Vested	56,828	52,663
Active Non-vested	20,151	24,124
Vested Former Members	26,805	26,058
Retired Members	26,216	24,525
<b>Active Members</b>		
Number	76,979	76,787
Average Age	47.2	46.8
Average Years of Service	12.3	11.8
Average Annual Salary	\$43,198	\$41,509
<b>Retirees &amp; Beneficiaries</b>		
Number	26,216	24,525
Average Age	66.5	66.2
Average Monthly Benefit	\$ 743	\$ 693

**THE EMPLOYEES' PENSION SYSTEM (EPS)** was established on January 1, 1980 and is administered in accordance with the State Personnel and Pensions Article of the Annotated Code of Maryland. Membership in the EPS was a condition of employment for all State employees (other than those eligible for participation in another system) until July 1, 1998, and continues to be a condition of employment for employees of participating governmental units that have not elected to participate in the Employees' Contributory Pension System (ECPS). As of July 1, 1998, EPS members who were State employees, except for those who transfer from the ERS after April 1, 1998, became members of the ECPS. As of July 1, 1999, EPS members who were employees of governmental units were eligible to participate in the ECPS retroactive to July 1, 1998, provided the participating governmental unit elected participation in the ECPS.

### **Member Contributions**

All EPS members are required to contribute 5% of earnable compensation in excess of the social security wage base. Members of the ECPS are required to contribute 2% of earnable compensation.

### **Service Pension Allowances**

**Eligibility** — EPS and ECPS members are eligible for full service pension allowances upon accumulating 30 years of eligibility service regardless of age. Absent 30 years of eligibility service, members must meet one of the following conditions to be eligible for full service pension allowances:

- age 62, & five years of eligibility service
- age 63, & four years of eligibility service
- age 64, & three years of eligibility service
- age 65 or older, & two years of eligibility service

**Allowances** — For EPS members, full service pension allowances equal 0.8% of the highest three consecutive years' AFS up to the SSIL, plus 1.5% of AFS in excess of the SSIL, multiplied by the number of years of accumulated creditable service. For the purpose of computing pension allowances, the SSIL is the average of the social security wage bases for the 35 years immediately prior to the year of retirement.

For ECPS members, full service retirement allowances equal 1.2% of AFS for service accrued prior to July 1, 1998, (or if greater, the EPS benefit noted above on service prior to July 1, 1998), plus 1.4% of AFS for service accrued on and after July 1, 1998. Allowances for members who fail to make all required contributions are reduced by the actuarial equivalent of the total unpaid contributions plus interest to date of retirement.

### **Early Service Pension Allowances**

**Eligibility** — EPS and ECPS members are eligible for early service pension allowances upon attaining age 55 with at least 15 years of eligibility service.

**Allowances** — Early service pension allowances for both the EPS and ECPS equal the amount payable for a full service pension reduced by 0.5% for each month by which the retirement date precedes the date on which the member reaches age 62. The maximum reduction is 42 percent.

### **Ordinary Disability Pension Allowances**

**Eligibility** — EPS and ECPS members are eligible for ordinary disability pension allowances upon completing five years of eligibility service and receiving certification from the Medical Board that they are permanently incapable of performing their necessary job functions.

**Allowances** — For EPS and ECPS members, ordinary disability pension allowances equal the full service pension allowances if the members are at least age 62 on the date of retirement. Otherwise, the allowances equal the full service pension allowances computed as though the members had continued to accrue service credits until age 62 without any change in the rate of earnable compensation.

### **Accidental Disability Pension Allowances**

**Eligibility** — EPS and ECPS members are eligible for accidental disability pension allowances if the Medical Board certifies that, in the course of their job performance and as the direct result of an accidental injury, they became totally and permanently disabled.

**Allowances** — For EPS and ECPS members, accidental disability pension allowances equal the sum of an annuity determined as the actuarial value of the members' accumulated contributions, and 2/3 (66.7%) of AFS. Allowances may not exceed the members' AFS.

### **Death Benefits**

**Eligibility** — To be eligible for death benefits, EPS and ECPS members must have either accumulated at least one year of eligibility service prior to the date of death or died in the line of duty.

**Benefits** — The benefit provided upon death of EPS and ECPS members equals the members' annual earnable compensation on the date of death plus accumulated contributions. Under certain circumstances, surviving spouses who were named sole primary beneficiaries may elect to receive either the aforementioned lump sum payment, or a monthly allowance calculated as payment under Option 2 (100% survivor option).

If at the time of death, the members had:

- accrued at least 25 years of eligibility service, or
- attained age 55 with at least 15 years of eligibility service, or
- attained age 62, then

the survivor's allowance is determined as if the members had been eligible to retire.

### **Vested Pension Allowances**

**Eligibility** — EPS and ECPS members are eligible for vested pension allowances after separation from service and upon reaching age 62, provided that at least five years of eligibility service was accumulated prior to separation. EPS and ECPS members may be eligible for reduced vested pension allowances upon attaining age 55 with at least 15 years of eligibility service. Vested allowances are reduced by 0.5% for each month by which the allowance commencement date precedes the date on which the members attain age 62.

**Allowances** — For the EPS and ECPS, vested allowances equal the normal service pension allowances computed on the basis of the members' accumulated creditable service and AFS at the point of separation.

EPS members who elect to withdraw their accumulated contributions, remain eligible to receive the employer-provided share of the vested benefit. If members do not withdraw their contributions, and die before attaining age 62, their accumulated contributions are returned to the designated beneficiary.

**Cost-of-Living Adjustments**

Retirement allowances for EPS and ECPS members are adjusted each year based on the Consumer Price Index. COLAs are effective July 1st of each year and beginning July 1998, are compounded annually for ECPS members and EPS members, who are State employees, participating governmental unit employees, and for those who transferred from the ERS after April 1, 1998. The Systems limit the increase a retiree may receive to a maximum of 3%. COLAs for all other EPS members remain limited to 3% of the initial allowance annually.

**Optional Forms of Payment**

**Option 1:** Payment guarantees a cash reserve equal to the excess of the present value of the pension allowance at the date of retirement minus the total amount of payments (less COLAs) made to the date of death.

**Option 2:** 100% joint and survivor annuity.

**Option 3:** 50% joint and survivor annuity.

**Option 4:** Payment guarantees a minimum return of the members' accumulated contributions.

**Option 5:** 100% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

**Option 6:** 50% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

Except for a spouse or disabled child, the beneficiary designated under Option 2 or 5 cannot be more than 10 years younger than the retiree (IRS regulation).

**Workers' Compensation Benefits Reduction**

Disability retirement allowances, except for retirees of a participating governmental unit, are generally reduced by workers' compensation benefits paid after retirement if, and to the extent that, such benefits are for the same injury and the same period of time for which the retirement benefits were paid.

The workers' compensation benefit reduction cannot reduce any retirement allowance to less than the amount necessary to cover the retiree's monthly health insurance premiums.

**Pension Changes**

Effective July 1, 2006, there is an Alternate Contributory Pension Selection (ACPS) which applies to all state employees and employees of participating governmental units whose employer elects participation in the ACPS by June 30, 2007. Under the ACPS, service accrued after July 1, 1998 is 1.8% (increase from 1.4%) per year of service.

JUDGES' RETIREMENT SYSTEM

**A COMPOSITE PICTURE**

	2006	2005
<b>Total Membership</b>		
Active Vested	296	282
Active Non-vested	—	—
Vested Former Members	14	15
Retired Members	330	316
<b>Active Members</b>		
Number	296	282
Average Age	56.4	56.6
Average Years of Service	9.4	9.9
Average Annual Salary	\$121,416	\$120,206
<b>Retirees &amp; Beneficiaries</b>		
Number	330	316
Average Age	77.7	77.6
Average Monthly Benefit	\$ 5,085	\$ 4,871

**THE JUDGES' RETIREMENT SYSTEM (JRS)** was established on June 30, 1969 and is administered in accordance with the State Personnel and Pensions Article of the Annotated Code of Maryland. Membership is a condition of employment for all District Court, Circuit Court, Court of Appeals and Court of Special Appeals judges. Full-time masters in chancery and masters in juvenile causes appointed prior to June 30, 1989 and Workers' Compensation Commission judges are also members of the JRS.

**Member Contributions**

All members contribute 6% of annual earnable compensation during the first 16 years of service. After accruing 16 years of credit, no member contributions are required.

**Service Retirement Allowances**

**Eligibility** — JRS members are eligible for full service retirement allowances upon attaining age 60 or upon retirement by order of the Court of Appeals, with at least 16 years of eligibility service. All JRS members must retire at age 70.

**Allowances** — Full service retirement allowances equal  $\frac{2}{3}$  (66.7%) of the current salary for an active judge holding a comparable position. If members retire with less than 16 years of eligibility service, the annual retirement allowance is prorated accordingly.

### **Early Retirement Allowances**

**Eligibility** — JRS members are not eligible for early service retirement allowances.

### **Disability Retirement Allowances**

**Eligibility** — JRS members are eligible for disability retirement allowances upon receiving certification from the Medical Board that they are permanently incapable of performing their necessary job functions.

**Allowances** — The disability retirement allowances for JRS members generally equal the full service retirement allowance based on the members' actual length of service. However, for members completing at least three years of eligibility service, the disability benefit will be no less than  $\frac{1}{3}$  (33.3%) of the members' annual earnable compensation at the time of retirement.

### **Death Benefits**

**Eligibility** — All JRS members, and former members, are eligible for death benefits regardless of age or length of service.

**Benefits** — The benefit provided upon death for JRS members, former members or retirees equals 50% of a service retirement allowance payable to the surviving spouse.

Special provisions apply in circumstances where deceased JRS members, former members or retirees have no surviving spouses, but are survived by a minor child (under age 18). In the event that deceased JRS members or former members are not survived by spouses or minor children, then all accumulated contributions are refunded to the estate.

### **Vested Retirement Allowances**

**Eligibility** — JRS members are immediately vested. Members leaving the bench before attaining age 60 are eligible to receive their service retirement allowances commencing upon attaining age 60.

**Allowances** — Vested allowances equal the normal service retirement allowances computed on the basis of the members' accumulated creditable service and the salaries of active judges holding comparable positions.

JRS members may elect to withdraw their accumulated contributions within six months of separation in lieu of receiving vested retirement allowances.

### **Optional Forms of Payment**

Generally, JRS retirement allowances are paid as a 50% joint and survivor annuity to the retirees' surviving spouse, or if there is no spouse, to any child under age 18. If the retirees have neither a living spouse nor children under 18 at retirement, retirees may select any one of the following six payment options.

**Option 1:** Payment guarantees a cash reserve equal to the excess of the present value of the retirement allowance at the date of retirement minus the total amount of payments made to the date of death.

**Option 2:** 100% joint and survivor annuity.

**Option 3:** 50% joint and survivor annuity.

**Option 4:** Payment guarantees a minimum return of the members' accumulated contributions.

**Option 5:** 100% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

**Option 6:** 50% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

Once retired, neither the option nor designated beneficiary(ies) may be changed. Except for a spouse or disabled child, the beneficiary designated under Option 2 or 5 cannot be more than 10 years younger than the retiree (IRS regulation).

## STATE POLICE RETIREMENT SYSTEM

## A COMPOSITE PICTURE

	2006	2005
<b>Total Membership</b>		
Active Vested	1,109	1,095
Active Non-vested	332	344
Vested Former Members	58	47
Retired Members	1,937	1,909
<b>Active Members</b>		
Number	1,441	1,439
Average Age	35.3	35.3
Average Years of Service	11.4	10.9
Average Annual Salary	\$55,967	\$53,934
<b>Retirees &amp; Beneficiaries</b>		
Number	1,937	1,909
Average Age	59.0	58.8
Average Monthly Benefit	\$ 3,237	\$ 3,000

**THE STATE POLICE RETIREMENT SYSTEM (SPRS)** was established on July 1, 1949 and is administered in accordance with the State Personnel and Pensions Article of the Annotated Code of Maryland. Membership is a condition of employment for all uniformed officers of the Maryland State Police. The Superintendent of the Maryland State Police may elect membership in either the SPRS or the EPS.

### Member Contributions

All SPRS members contribute 8% of annual earnable compensation during employment.

### Service Retirement Allowances

**Eligibility** — SPRS members are eligible for full service retirement allowances upon attaining age 50 or upon accumulating 22 years of eligibility service regardless of age. Except for the Superintendent, all SPRS members must retire at age 60.

**Allowances** — Full service retirement allowances equal 2.55% of AFS up to a maximum 71.4% of AFS (28 years). Allowances for members who fail to make all required contributions are reduced by the actuarial equivalent of the total unpaid contributions plus interest to date of retirement.

### Early Retirement Allowances

**Eligibility** — SPRS members are not eligible for early service retirement allowances.

### Ordinary Disability Retirement Allowances

**Eligibility** — SPRS members are eligible for ordinary disability retirement allowances upon completing five years of eligibility service and receiving certification from the Medical Board that they are permanently incapable of performing their necessary job functions.

**Allowances** — Ordinary disability retirement allowances generally equal 2.55% of the AFS multiplied by the number of years of creditable service up to a maximum of 28 years. The minimum ordinary disability retirement allowance is 35% of AFS.

### Special Disability Retirement Allowances

**Eligibility** — SPRS members are eligible for special disability benefits if the Medical Board certifies that they became totally and permanently incapacitated for duty arising out of or in the actual performance of duty.

**Allowances** — Special disability allowances equal the sum of an annuity determined as the actuarial value of the members' accumulated contributions, and 2/3 (66.7%) of AFS. Allowances may not exceed the members' AFS.

### Ordinary Death Benefits

**Eligibility** — To be eligible for ordinary death benefits, SPRS members must have accumulated at least one but less than two years of eligibility service prior to the date of death.

**Benefits** — The ordinary death benefit equals the members' annual earnable compensation at time of death plus accumulated contributions.

### Special Death Benefits

#### **Members in Service**

**Eligibility** — To be eligible for special death benefits, SPRS members in service must have accumulated at least two years of eligibility service prior to the date of death or died in the line of duty.

**Benefits** — The special benefit provided upon the death of SPRS members in service equals 50% of the members' annual earnable compensation at time of death paid as an annuity plus return of accumulated contributions. In cases where the deceased members are not survived by a spouse, the decedents' children or dependent parents, if any, will continue to receive an annuity equal to 50% of the members' annual earnable compensation until the youngest child reaches age 18, or for the life of each dependent parent. The special death benefit for troopers killed in the line of duty is 2/3 (66.7%) of AFS.

### **Survivor Benefit**

**Eligibility** — To be eligible for survivor benefits, SPRS retirees must have retired on either a service retirement allowance or a disability allowance.

**Benefits** — The survivor benefit provided upon the death of an SPRS retiree equals 50% of the retirees' retirement allowance, paid as an annuity. In cases where the deceased members are not survived by a spouse, the decedents' children, if any, will continue to receive 50% of the retirees' allowance until the youngest child reaches age 18.

In addition to the survivor benefits explained above, the survivors of both deceased members in service and deceased retirees may be eligible for certain additional benefits based upon Title II of the federal Social Security Act.

### **Vested Retirement Allowances**

**Eligibility** — SPRS members are eligible for vested retirement allowances after separation from service and upon reaching age 50, provided that at least five years of eligibility service was accumulated prior to separation.

**Allowances** — Vested allowances equal the normal service retirement allowances computed on the basis of the members' accumulated creditable service and AFS at the point of separation.

SPRS members may elect to withdraw their accumulated contributions within two years of separation in lieu of receiving vested retirement allowances. If members do not withdraw their contributions, and die before attaining age 50, their accumulated contributions are returned to the designated beneficiary.

### **Cost-of-Living Adjustments**

Retirement allowances are adjusted each year based on the Consumer Price Index. COLAs are effective July 1st of each year and are applied to all allowances payable for the year.

### **Optional Forms of Payment**

Generally, SPRS retirement allowances are paid as a 50% joint and survivor annuity to the retirees' spouse, or if there is no spouse, to any child under age 18. If the retirees have neither a living spouse nor children under 18 at retirement, the retirees may select any one of the following six payment options.

**Option 1:** Payment guarantees a cash reserve equal to the present value of the retirement allowance at the date of retirement minus the total amount of payments (less COLAs) made to the date of death.

**Option 2:** 100% joint and survivor annuity.

**Option 3:** 50% joint and survivor annuity.

**Option 4:** Payment guarantees a minimum return of the members' accumulated contributions.

**Option 5:** 100% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

**Option 6:** 50% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

Except for a spouse or disabled child, the beneficiary designated under Option 2 or 5 cannot be more than 10 years younger than the retiree (IRS regulation).

### **Workers' Compensation Benefits Reduction**

Disability retirement allowances are generally reduced by workers' compensation benefits paid after retirement if, and to the extent that, such benefits are for the same injury and the same period of time for which the retirement benefits are payable. The workers' compensation benefit reduction cannot reduce any retirement allowance to less than the amount necessary to cover the retiree's monthly health insurance premiums.

### **Deferred Retirement Option Program**

SPRS members are eligible to participate in a Deferred Retirement Option Program (DROP). To participate, the SPRS member must have at least 22 years of creditable service, but less than 28 years, and be under age 60. The maximum period of participation is 4 years. During the DROP period, the SPRS member is deemed retired and the retirement allowance is placed in an account earning 6% interest. At the end of the DROP period, the lump sum held in the DROP account is paid to the SPRS retiree. The SPRS member must end employment and fully retire at the end of the DROP period.

## LAW ENFORCEMENT OFFICERS' PENSION SYSTEM

## A COMPOSITE PICTURE

	2006	2005
<b>Total Membership</b>		
Active Vested	1,546	1,282
Active Non-vested	517	544
Vested Former Members	115	104
Retired Members	782	708
<b>Active Members</b>		
Number	2,063	1,826
Average Age	39.8	39.5
Average Years of Service	11.2	10.7
Average Annual Salary	\$51,706	\$48,700
<b>Retirees &amp; Beneficiaries</b>		
Number	782	708
Average Age	56.8	56.7
Average Monthly Benefit	\$ 2,345	\$ 2,294

**THE LAW ENFORCEMENT OFFICERS PENSION SYSTEM (LEOPS)**

was established on July 2, 1990 and is administered in accordance with the State Personnel and Pensions Article of the Annotated Code of Maryland. Membership in the LEOPS is a condition of employment for all uniformed law enforcement officers of the Maryland State Department of Natural Resources; the Maryland Investigative Services Unit; the Maryland Transportation Authority Police Force; the Baltimore City Sheriff's Department; the State Fire Marshall's Office; the University System of Maryland Police Force; Morgan University Police Force; the BWI Airport Fire and Rescue Department; the Department of General Services Police Force; the Department of Health and Mental Hygiene; the Motor Vehicle Administration; and the Department of Labor, Licensing, and Regulation; the State Department of Elections; Field Enforcement Bureau; Firefighters for Martin's Airport Aviators employed by the Department of State Police. In addition, membership includes law enforcement officers, firefighters, and paramedics employed by a governmental unit that elects to participate in LEOPS.

The LEOPS consists of two separate components — a retirement plan (closed to new members January 1, 2005) and a pension plan. Retirement plan provisions are applicable to those officers who, on the date they elected to participate in the LEOPS, were members of ERS (closed as of January 1, 2005). Pension plan provisions are applicable to all other LEOPS members.

**Member Contributions**

All member contributions to the LEOPS are based on the members' annual earnable compensation. Members subject to retire-

ment plan provisions that elected to receive unlimited future COLAs contribute 7%. This option is referred to as Selection A (Unlimited COLA).

Members subject to retirement plan provisions that elected to receive limited future COLAs contribute 5%. This option is referred to as Selection B (Limited COLA).

Members subject to pension plan provisions contribute 4% of annual earnable compensation during employment.

**Service Retirement Allowances**

**Eligibility** — LEOPS members are eligible for full service retirement allowances upon attaining age 50 or upon accumulating 25 years of eligibility service regardless of age.

**Allowances** — For members subject to the retirement plan provisions, full service retirement allowances equal 2.3% of AFS for the first 30 years of creditable service, plus 1.0% of AFS for each additional year.

For members subject to the pension system provisions, full service pension allowances equal 2.0% of AFS up to a maximum benefit of 60% of AFS (30 years of credit).

Allowances for members who fail to make all required contributions are reduced by the actuarial equivalent of the total unpaid contributions plus interest to the date of retirement.

**Early Retirement Allowances**

**Eligibility** — LEOPS members are not eligible for early service retirement allowances.

**Ordinary Disability Retirement Allowances**

**Eligibility** — LEOPS members are eligible for ordinary disability retirement allowances upon completing five years of eligibility service and receiving Medical Board certification as to their permanent incapacity to perform their necessary job functions.

**Allowances** — Ordinary disability retirement allowances for LEOPS members subject to retirement plan provisions equal the greater of the normal service retirement allowance or 25% of AFS.

Ordinary disability retirement allowances for LEOPS members subject to pension plan provisions equal the full service pension allowance if the member is at least age 50 on the date of retirement. Otherwise, the allowances equal full service pension allowances computed as though the member had continued to work until age 50 without any change in the rate of earnable compensation.

### **Accidental Disability Retirement Allowances**

**Eligibility** — LEOPS members are eligible for accidental disability benefits if the Medical Board certifies that they became totally and permanently incapacitated for duty arising out of or in the actual performance of duty.

**Allowances** — Accidental disability allowances equal the sum of an annuity determined as the actuarial value of the members' accumulated contributions, and 2/3 (66.7%) of AFS. Allowances may not exceed the members' AFS.

### **Ordinary Death Benefits**

**Eligibility** — To be eligible for ordinary death benefits, LEOPS members must have accumulated at least one but less than two years of eligibility service prior to the date of death.

**Benefits** — The ordinary death benefit equals the members' annual earnable compensation at the time of death plus accumulated contributions.

### **Special Death Benefits**

#### **Members in Service**

**Eligibility** — To be eligible for special death benefits, LEOPS members in service must have accumulated at least two years of eligibility service prior to the date of death or died in the line of duty.

**Benefits** — The special death benefit provided upon death for LEOPS members in service equals 50% of the applicable ordinary disability allowance. In cases where the deceased members are not survived by a spouse, the decedents' children, if any, will continue to receive the special death benefit until the youngest child reaches age 18. The special death benefit for officers killed in the line of duty is 2/3 (66.7%) of AFS.

#### **Survivor Benefits**

**Eligibility** — To be eligible for survivor benefits, LEOPS retiree must have retired on either a service retirement allowance or a disability allowance.

**Benefits** — The survivor benefit provided upon death for LEOPS retiree equals 50% of the retiree' retirement allowance, paid as an annuity. In cases where the deceased members are not survived by a spouse, the decedents' children, if any, will continue to receive 50% of the retiree' allowance until the youngest child reaches age 18.

### **Vested Pension Allowances**

**Eligibility** — LEOPS members are eligible for vested pension allowances after separation from service and upon attaining age

50, provided that they accumulated at least five years of eligibility service prior to separation.

**Allowances** — Vested allowances equal the normal service retirement or pension allowances computed on the basis of the members' accumulated creditable service and AFS at the date of separation.

### **Cost-of-Living Adjustments**

Retirement allowances are adjusted each year based on the Consumer Price Index. COLAs are effective July 1st of each year and are applied to all allowances payable for the year. For LEOPS members subject to retirement plan provisions, annual COLAs are determined under the various methods applicable to ERS members. Each method is explained below:

**Selection A (Unlimited COLA)** — LEOPS members who elected Selection A (while enrolled in the ERS), agreed to contribute 7% of earnable compensation in return for unlimited annual COLAs after retirement.

**Selection B (Limited COLA)** — LEOPS members who elected Selection B (while enrolled in the ERS), agreed to contribute no more than 5% of earnable compensation in return for COLAs which are limited to 5% annually after retirement.

For all other LEOPS members, annual COLA's are limited to 3% of the annual allowance.

### **Optional Forms of Payment**

Generally, LEOPS retirement allowances are paid as a 50% joint and survivor annuity to the retiree' spouse, or if there is no spouse, to any child under age 18. If the retiree have neither a living spouse nor children under 18 at retirement, the retiree may select any one of the following six payment options.

**Option 1:** Payment guarantees a cash reserve equal to the excess of the present value of the retirement allowance at the date of retirement minus the total amount of payments (less COLAs) made to the date of death.

**Option 2:** 100% joint and survivor annuity.

**Option 3:** 50% joint and survivor annuity.

**Option 4:** Payment guarantees a minimum return of the members' accumulated contributions.

**Option 5:** 100% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

**Option 6:** 50% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

Except for a spouse or disabled child, the beneficiary designated under Option 2 or 5 cannot be more than 10 years younger than the retiree (IRS regulation).

**Workers' Compensation Benefits Reduction**

Disability retirement allowances are generally reduced by workers' compensation benefits paid after retirement if, and to the extent that, such benefits are for the same injury and the same period of time for which the retirement benefits are payable. The workers' compensation benefit reduction cannot reduce any retirement allowance to less than the amount necessary to cover the retiree's monthly health insurance premiums.

**Deferred Retirement Option Program**

LEOPS members are eligible to participate in a Deferred Retirement Option Program (DROP). To participate, the LEOPS member must have at least 25 years of creditable service, but less than 30 years. The maximum period of participation is 5 years. During the DROP period, the LEOPS member is deemed retired and the retirement allowance is placed in an account earning 6% interest. At the end of the DROP period, the lump sum held in the DROP account is paid to the LEOPS retiree. The LEOPS member must end employment and fully retire at the end of the DROP period.

**LOCAL FIRE AND POLICE SYSTEM**

<b>A COMPOSITE PICTURE</b>		
	<b>2006</b>	<b>2005</b>
<b>Total Membership</b>		
Active Vested	36	32
Active Non-vested	19	25
Vested Former Members	7	6
Retired Members	16	14
<b>Active Members</b>		
Number	55	57
Average Age	37.2	37.0
Average Years of Service	11.0	10.4
Average Annual Salary	\$36,520	\$36,586
<b>Retirees &amp; Beneficiaries</b>		
Number	16	14
Average Age	58.4	57.9
Average Monthly Benefit	\$ 1,451	\$ 1,224

**Service Retirement Allowances**

**Eligibility** — All LFPS members are eligible for full service retirement or pension allowances upon accumulating 25 years of eligibility service, regardless of age. Also, regardless of the length of service, LFPS retirement plan members are eligible for full service retirement allowances upon attaining age 60; and LFPS pension plan members are eligible for full service pension allowances upon attaining age 62.

**Allowances** — For members subject to retirement plan provisions, full service retirement allowances equal 1/50 (2.0%) of AFS for the first 30 years of creditable service, plus 1/100 (1.0%) of AFS for each additional year.

For members subject to pension plan provisions, full service pension allowances equal 1.0% of AFS up to the SSIL, plus 1.5% of AFS in excess of the SSIL, multiplied by the number of years of accumulated creditable service. LFPS pension plan members whose employers do not contribute to social security receive 1.5% of their entire AFS as a pension allowance.

Allowances for members who fail to make all required contributions are reduced by the actuarial equivalent of the total unpaid contributions plus interest to the date of retirement.

**Early Retirement Allowances**

**Eligibility** — LFPS members are not eligible for early service retirement allowances.

**Ordinary Disability Retirement Allowances**

**Eligibility** — LFPS members are eligible for ordinary disability retirement allowances upon completing five years of eligibility service with Medical Board certification as to their permanent incapacity to perform their necessary job functions.

**THE LOCAL FIRE AND POLICE SYSTEM (LFPS)** was established on July 1, 1989 and is administered in accordance with the State Personnel and Pensions Article of the Annotated Code of Maryland. Effective January 1, 2005, membership in the LFPS was closed to new employers. Current employers continue to participate and membership remains mandatory for their law enforcement officers and fire fighters.

**Member Contributions**

Members subject to pension plan provisions contribute 5% of earnable compensation in excess of the social security wage base.

**Allowances** — Ordinary disability retirement allowances for LFPS members equal the full service pension allowance if the member is at least age 62 on the date of retirement. Otherwise, the allowances equal full service pension allowances computed as though the member had continued to work until age 62 without any change in the rate of earnable compensation.

### **Accidental Disability Retirement Allowances**

**Eligibility** — LFPS members are eligible for accidental disability benefits if the Medical Board certifies that, in the course of job performance and as the direct result of an accidental injury, they became totally and permanently disabled.

**Allowances** — Accidental disability allowances equal the sum of an annuity determined as the actuarial value of the members' accumulated contributions, and 2/3 (66.7%) of AFS. Allowances may not exceed the members' AFS.

### **Ordinary Death Benefits**

**Eligibility** — To be eligible for death benefits, LFPS members must have accumulated at least one year of eligibility service prior to the date of death or died in the line of duty.

**Benefits** — The benefit provided upon death for LFPS members equals the members' annual earnable compensation at the time of death plus accumulated contributions. Under certain circumstances, surviving spouses who were named sole primary beneficiaries may elect to receive either the aforementioned lump sum payment or a monthly allowance calculated under Option 2 (100% survivor option).

### **Vested Pension Allowances**

**Eligibility** — LFPS members are eligible for vested pension allowances after separation from service and upon attaining age 62, provided that they accumulated at least five years of eligibility service prior to separation. LFPS members subject to pension plan provisions may be eligible for reduced vested pension allowances upon attaining age 55 with at least 15 years of eligibility service. Vested allowances are reduced by 0.5% for each month by which the allowance commencement date precedes the date on which the members attain age 62.

**Allowances** — Vested allowances equal the normal service retirement or pension allowances computed on the basis of the members' accumulated creditable service and AFS at the date of separation.

LFPS pension plan members, who elect to withdraw their accumulated contributions, if any, remain eligible to receive the employer-provided vested benefit.

### **Cost-of-Living Adjustments**

Retirement and pension allowances are adjusted each year based on the Consumer Price Index. COLA's are effective July 1st of each year and are applied to all allowances payable for the year. For all LFPS members who are not former members of the ERS, annual COLAs are limited to 3% of the initial allowance annually.

### **Optional Forms of Payment**

**Option 1:** Payment guarantees a cash reserve equal to the present value of the retirement allowance at the date of retirement minus the total amount of payments (less COLAs) made to the date of death.

**Option 2:** 100% joint and survivor annuity.

**Option 3:** 50% joint and survivor annuity.

**Option 4:** Payment guarantees a minimum return of the members' accumulated contributions.

**Option 5:** 100% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

**Option 6:** 50% joint and survivor annuity with adjustment to maximum benefit if beneficiary predeceases retiree.

Except for a spouse or disabled child, the beneficiary designated under Option 2 or 5 cannot be more than 10 years younger than the retiree (IRS regulation).

### **Workers' Compensation Benefits Reduction**

Disability retirement allowances are generally reduced by workers' compensation benefits paid after retirement if, and to the extent that, such benefits are for the same injury and the same period of time for which the retirement benefits are payable. The workers' compensation benefit reduction cannot reduce any retirement allowance to less than the amount necessary to cover the retiree's monthly health insurance premiums.



This page intentionally left blank