

**DEPARTMENT OF
THE TREASURY**

R. David Rousseau
State Treasurer

**DIVISION OF PENSIONS
AND BENEFITS**

Frederick J. Beaver
Director

**PUBLIC EMPLOYEES'
RETIREMENT SYSTEM
OF NEW JERSEY**

**BOARD OF TRUSTEES
as of June 30, 2008**

LEON FLANAGAN
Chairperson

FREDERICK J. BEAVER
State Treasurer's Representative

CHRISTINE VELIZ

JONATHAN BERG

EDWARD THOMSON, III

THOMAS BRUNO, JR.

JOHN LOWDEN

RONALD WINTHERS

SUZANNA BURIANI-DESANTIS

KELLIE KIEFER-PUSHKO
Deputy Attorney General

KATHLEEN COATES
Board Secretary

JACQUELYN BUSSANICH
Administrative Assistant

BUCK CONSULTANTS
Actuaries and Consultants

MEDICAL BOARD
David Jenkins, M.D.
William E. Ryan, M.D.



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

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

Dear Governor Corzine:

The Board of Trustees of the

PUBLIC EMPLOYEES' RETIREMENT SYSTEM

is pleased to present the Fiscal Year 2008 Annual Report in accordance with the provisions of N.J.S.A. 43:15A-21.

Respectfully submitted,


LEON FLANAGAN
Chairperson

**PUBLIC EMPLOYEES' RETIREMENT SYSTEM
BOARD OF TRUSTEES**



UNAVAILABLE
FOR PHOTO

LEON FLANAGAN
*Chairperson
State Representative*



FREDERICK J. BEAVER
*Treasurer's
Representative*



CHRISTINE VELIZ
State Representative



JONATHAN BERG
State Representative



**EDWARD
THOMSON, III**
*Gubernatorial
Appointee*



THOMAS BRUNO, JR.
State Representative



JOHN LOWDEN
State Representative



RONALD WINTHERS
State Representative



**SUZANNA
BURIANI-DESANTIS**
County Representative



KELLIE KIEFER-PUSHKO
Deputy Attorney General



KATHLEEN COATES
Board Secretary



JACQUELYN BUSSANICH
Administrative Assistant

SIGNIFICANT LEGISLATION

CHAPTER 250, P.L. 2007

Effective Date: January 4, 2008.

Description: This law prohibits the investment of New Jersey public employee retirement system funds in any foreign company that has an equity tie to the government of Iran, or its instrumentalities, and is engaged in business operations with entities in the defense sector or nuclear sector of Iran, or engaged in business operations with entities involved in the natural gas or petroleum sectors of Iran, or with that government. It does not apply to the activities of any foreign company providing humanitarian aid to the Iranian people through either a governmental or non-governmental organization.

This law requires the State Investment Council and the Director of the Division of Investment to divest any investments held in violation of the prohibition after consulting with an independent research firm that specializes in global security risk for portfolio determinations selected by the State Treasurer. Periodic progress reports by the division are required.

This act would be void if: 1) the Congress or the President of the United States declares that the government of Iran has ceased to acquire or develop weapons of mass destruction and to support international terrorism; or 2) the United States revokes all sanctions imposed against the government of Iran.

The law also provides that State Investment Council members, and State officers and employees involved therewith, would be indemnified and held harmless by the State of New Jersey from all liabilities and losses that these individuals may sustain or cause by reason of any decision to restrict or eliminate investments pursuant to this act.

CHAPTER 21, P.L. 2008

Effective Date: This act takes effect immediately (June 24, 2008).

Description:

This law provides early retirement incentive program to eligible State employees in the Executive Branch of State government and eligible Judiciary employees in the Judicial Branch of State government who apply to retire on or after March 1, 2008 but by July 15, 2008 and retire by August 1, 2008.

An eligible State employee or an eligible Judiciary employee who is at least 58 years of age and has at least 25 years of service credit under the Public Employees' Retirement System (PERS) or the Teachers' Pension and Annuity Fund (TPAF) will receive an additional three years of service credit. An employee who is at least 58 years of age and has at least 25 years of service credit and retires on a veteran's retirement under the PERS or the TPAF will receive an additional pension in the amount of 3/55 of the compensation upon which the retirement allowance is based.

For an eligible State employee, but not an eligible Judiciary employee, who is at least 60 years of age and has at least 20, but less than 25, years of service credit under the PERS or the TPAF, the retirement system will pay the premium or periodic charges for health care benefits provided to the retired State employee and the employee's dependents, but not including survivors, under the State Health Benefits Program, in the same manner provided for State payment of premiums or periodic charges for a retired State employee with 25 or more years of service credit under current law and in the same manner provided for State payment of premiums or periodic charges for a qualified retiree from the TPAF under current law.

An eligible State employee, but not an eligible Judiciary employee, who is at least 60 years of age and has at least 10, but less than 20, years of service credit under the PERS or the TPAF will receive an additional pension of \$500 a month for 24 months following the date of retirement.

To receive these benefits, an eligible State employee or an eligible Judiciary employee must submit an application for retirement on or after March 1, 2008 but by July 15, 2008 and retire no later than August 1, 2008. An application submitted by an eligible State employee or an eligible Judiciary employee for retirement within the time period set to receive the benefits provided will be irrevocable seven days after submission.

Service credit in the Public Employees' Retirement System or the Teachers' Pension and Annuity Fund established through a purchase completed after the effective date of this law will not be considered in determining an employee's eligibility, except that those employees who have previously authorized payroll deductions for a purchase of service credit or those employees who have received a quo-

tation for a purchase of service credit from the Division of Pensions and Benefits within the 90 days prior to the effective date of this act may effectuate the purchase to qualify for eligibility under this act so long as that entire purchase is paid in full by July 15, 2008 or the date of the expiration of the purchase quotation, whichever date is earliest.

An "eligible State employee" means a full-time employee of the Executive Branch of State government eligible to participate in the New Jersey State Health Benefits Program of the State of New Jersey, but not including an employee of the Department of Human Services, Department of Military and Veterans' Affairs, Department of Corrections, Juvenile Justice Commission in but not of the Department of Law and Public Safety, Office of the Public Defender in but not of the Department of the Treasury, and Department of Children and Families.

The term does not include an employee of Rutgers, The State University; the New Jersey Institute of Technology; the University of Medicine and Dentistry of New Jersey; or a State college or university.

The term does not include an employee of a public authority, board, commission, corporation, or other agency or instrumentality of the State allocated in, but not of, a principal department of State government pursuant to Article V, Section IV, paragraph 1 of the New Jersey Constitution, authorized to participate in the Public Employees' Retirement System under section 73 of P.L.1954, c.84 (C.43:15A-73) or P.L.1990, c.25 (C.43:15A-73.2 et seq.), or an employee of a public agency or organization as defined in section 71 of P.L.1954, c.84 (C.43:15A-71), or a person participating in the Public Employees' Retirement System under the provisions of P.L.1972, c.167 (C.43:15A-135 et seq.), P.L.2001, c. 259 (C.43:15A-142 et seq.), P.L.2001, c.366 (C.43:15A-155 et seq.) or P.L.1953, c.202 (C.32:23-1 et seq.).

"Eligible Judiciary employee" means a full-time employee of the Judicial branch of State Government eligible to participate in the New Jersey State Health Benefits Program of the State of New Jersey. The term does not include a Justice of the Supreme Court, or a Judge of the Superior Court, or a Judge of a Municipal Court or an employee of a Municipal Court.

An eligible State employee who retires and receives a benefit will not be eligible for appointment to, or employment in, any position or capacity in the Executive Branch of State government, other than employment on an hourly basis for emergency management purposes, for a period of three years following the effective date of retirement. An eligible State employee who retires and receives a benefit will be barred from being awarded any contract for professional services by the Executive Branch of State government, or from performing professional services for the State as part of a contract awarded to a third party by the Executive Branch of State government, for a period of three years following the effective date of retirement.

An eligible Judiciary employee who retires and receives a benefit pursuant to this section will not be eligible for appointment to, or employment in, any position or capacity in the Judicial Branch of State Government for a period of three years following the effective date of retirement. An eligible Judiciary employee who retires and receives a benefit will be barred from being awarded any contract for professional services by the Judicial Branch of State Government, or from performing professional services for the State as part of a contract awarded to a third party by the Judicial Branch of State Government, for a period of three years following the effective date of retirement.

When the needs of the Executive Branch of State government require the services of an employee who elects to retire and receive a benefit, a State department may delay the effective date of retirement of the employee until the first day of any calendar month after August 1, 2008, but not later than July 1, 2009. For each such delayed retirement, the State department must request the approval of the State Treasurer by submitting in writing an explanation of the needs of the department, the services required of the employee, and the reasons why that particular employee's services are so essential as to necessitate a delay. The delay will be effective only upon approval of the request by the State Treasurer. A request by an eligible State employee for a delay in the effective date of retirement, whether the employee provides reasons for the delay or not, will not be considered by the State Treasurer unless the State department submits a request for a delay to the State Treasurer with the explanation described above.

When the needs of the Judicial Branch of State Government require the services of an employee who elects to retire and receive a benefit, the Judiciary may delay the effective date of retirement of the employee until the first day of any calendar month after August 1, 2008, but not later than July 1, 2009, pursuant to protocols to be issued by the Chief Justice of the Supreme Court.

An eligible State employee or an eligible Judiciary employee who applies to retire and receive the benefits will be deemed to consent, by that application, to a delay in the employee's effective date of retirement with regard to an eligible state employee, if the State department requests and receives approval for such a delay or, with regard to an eligible Judiciary employee, if the Chief Justice determines

SIGNIFICANT LEGISLATION, *continued*

that such a delay is appropriate. Such an employee's receipt of the benefits provided by this law will be conditioned upon faithful performance of service by the employee during the period of delay.

A request by an eligible State employee or an eligible Judiciary employee for a delay in the effective date of retirement, whether the employee provides reasons for the delay or not, will not be sufficient reason to approve a delay.

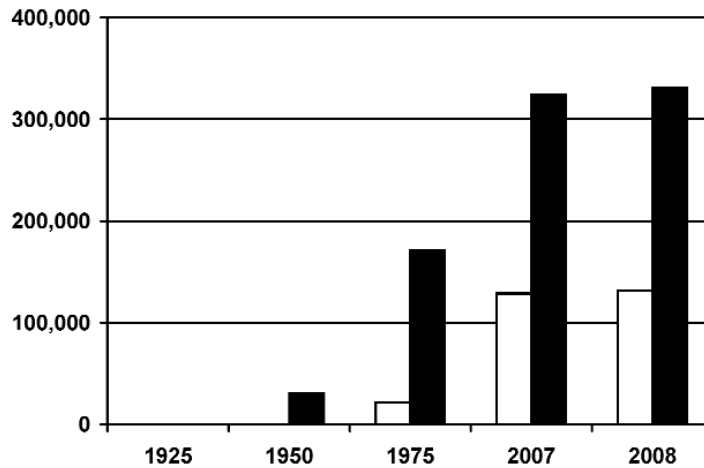
The Division of Pensions and Benefits in the Department of Treasury will report in writing to the Joint Budget Oversight Committee beginning on August 15, 2008, and annually thereafter on or before August 15, through 2014, on the results of the additional retirement benefits provided.

The law limits the hiring of replacements for individuals taking advantage of the retirement incentives. It provides that the number of employees hired in the Executive Branch to fill the vacancies created directly or indirectly because eligible employees retired to receive additional retirement benefits pursuant to the law shall not exceed, in total for all departments in the Executive Branch of State government, 10 percent of the total number of employees who retired pursuant this law. A similar separate limitation applies to replacement in the Judiciary,

In addition, the State Treasurer shall report to the Joint Budget Oversight Committee every six months for the first two years and annually thereafter, on the impact of that act on the State workforce, including an analysis of the allocation of position reductions that occur in each department and division as a result of that act and the plans adopted by each department to maintain the essential governmental services provided by that department.

MEMBERSHIP

- As of June 30, 2008, the active membership of the System totaled 330,523. This includes 97,831 State employees and 232,692 employees from 1,690 participating local employers. Inactive membership included is 54,751.
- During fiscal year 2008, there were 131,715 retirees and beneficiaries receiving annual pensions totaling \$2,023,571,985. (*This includes cost-of-living increases paid under the provisions of the Pension Adjustment Act.*)
- Beneficiaries of deceased active and retired members received lump sum death benefits in the amount of \$125,809,087.
- The System's assets totaled \$31,790,946,681 at the close of the fiscal year 2008.



MEMBERSHIP ACTIVITY

During fiscal year 2008, the following transactions were processed by the Division of Pensions and Benefits on behalf of the membership of the Public Employees' Retirement System of New Jersey.

- Enrollments - 24,310 new members were enrolled in PERS during fiscal year 2008.
- Loans - 72,497 loans were issued to members. The total loans receivable as of June 30, 2008 is \$428,260,732.
- Retirement - 8,401 members retired under the following retirement types:

<u>TYPE OF RETIREMENT</u>		<u>OPTIONS SELECTIONS</u>	
Service	4,674	Maximum	4,311
Early	570	Option 1	603
Ordinary Disability	1,031	Option 2	146
Accidental Disability	46	Option 3	57
Accidental Death	2	Option 4	15
Veteran	507	Option A	1,371
Deferred	422	Option B	525
Over 55 — Early	1,105	Option C	832
Chapter 366	23	Option D	540
Other	21	Other	1
Total	8,401	Total	8,401



KPMG LLP
Suite 402
301 Carnegie Center
Princeton, NJ 08540-6227

Independent Auditors' Report

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

We have audited the accompanying statements of fiduciary net assets of the State of New Jersey Public Employees' Retirement System (the System) as of June 30, 2008 and 2007, and the related statements of changes in fiduciary net assets for the years then ended. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control over financial reporting. Accordingly, we express no such opinion. An audit 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 financial position of the State of New Jersey Public Employees' Retirement System as of June 30, 2008 and 2007, and the changes in its financial position for the years then ended in conformity with U.S. generally accepted accounting principles.

As discussed in note 1 to the financial statements, the System adopted Governmental Accounting Standards Board (GASB) Statement No. 50, *Pension Disclosures* in 2008.

Management's Discussion and Analysis and the supplementary information included in the schedule of funding progress and schedule of employer contributions (schedules 1 and 2) are not a required part of the basic financial statements but are supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.



Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the System's basic financial statements. The 2008 schedule of changes in fiduciary net assets by fund (schedule 3) is presented for purposes of additional analysis and is not a required part of the basic financial statements of the System. Such information has been subjected to the auditing procedures applied in the audit of the 2008 basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the 2008 basic financial statements taken as a whole.

KPMG LLP

April 29, 2009

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Management's Discussion and Analysis

June 30, 2008 and 2007

Our discussion and analysis of the financial performance of the Public Employees' Retirement System (the System or PERS) financial performance provides an overview of the System's financial activities for the fiscal years ended June 30, 2008 and 2007. Please read it in conjunction with the basic financial statements and financial statement footnotes which follow this discussion.

Financial Highlights

2008 – 2007

- Net assets held in trust for pension benefits decreased by \$1,138,090,461 as a result of fiscal year 2008's operations from \$28,375,046,264 to \$27,236,955,803.
- Additions for the year are \$1,126,550,853, which are comprised of member and employer pension contributions of \$1,518,259,542 and an investment loss of \$391,708,689.
- Deductions for the year are \$2,264,641,314, which are comprised of benefit and refund payments of \$2,242,972,043 and administrative expenses of \$21,669,271.

2007 – 2006

- Net assets held in trust for pension benefits increased by \$3,066,201,508 as a result of fiscal year 2007's operations from \$25,308,844,756 to \$28,375,046,264.
- Additions for the year are \$5,140,088,340, which are comprised of member and employer pension contributions of \$1,329,122,958 and investment income of \$3,810,965,382.
- Deductions for the year are \$2,073,886,832, which are comprised of benefit and refund payments of \$2,054,380,082 and administrative expenses of \$19,506,750.

The Statements of Fiduciary Net Assets and the Statements of Changes in Fiduciary Net Assets

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

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

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Management's Discussion and Analysis

June 30, 2008 and 2007

Financial Analysis

Summary of Fiduciary Net Assets

2008 – 2007

	<u>2008</u>	<u>2007</u>	<u>Increase</u>
Assets	\$ 31,790,946,681	34,640,923,133	(2,849,976,452)
Liabilities	4,553,990,878	6,265,876,869	(1,711,885,991)
Net assets	<u>\$ 27,236,955,803</u>	<u>28,375,046,264</u>	<u>(1,138,090,461)</u>

The System's assets primarily consist of investments, securities lending collateral, contributions due from members and participating employers, accrued investment income, and members' loans receivable. Between fiscal years 2007 and 2008, total assets decreased by \$2.8 billion or 8.2% mainly due to a decrease in the fair value of investments and the securities lending collateral. Employer contributions receivables include contribution receivables from local employers for appropriations and early retirement incentive programs due April 1, 2009.

Liabilities consist of retirement benefits payable to retirees and beneficiaries, contributory and non-contributory group insurance premiums payable to the System's insurance provider, securities lending collateral and rebates payable and, classified under accounts payable and accrued expenses, liabilities of PERS for unclaimed member accounts and checks issued to members that have not been negotiated by the members but remain due and payable. Total liabilities decreased by a net \$1.7 billion or 27.3% over last year due to a decrease in the securities lending collateral and rebates payable of \$1.8 billion and an increase of \$133.3 million in retirement benefits payable due to full accrual of the July 1, 2008 payroll and other payables.

Net assets held in trust for pension benefits decreased by \$1.1 billion or 4.0%.

2007 – 2006

	<u>2007</u>	<u>2006</u>	<u>Increase</u>
Assets	\$ 34,640,923,133	30,103,200,419	4,537,722,714
Liabilities	6,265,876,869	4,794,355,663	1,471,521,206
Net assets	<u>\$ 28,375,046,264</u>	<u>25,308,844,756</u>	<u>3,066,201,508</u>

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Management's Discussion and Analysis

June 30, 2008 and 2007

The System's assets consist of cash, securities lending collateral, investments, and contributions due from members and participating employers. Between fiscal years 2006 and 2007, total assets increased by \$4.5 billion or 15.1%. The total assets increased due to an increase in contributions receivable from employers, an overall increase in the fair value of investments, and an increase in securities lending collateral.

Employer contributions receivables include contribution receivables from local employers for appropriations due April 1, 2008 based on Chapter 108, P.L. 2003, which provided that the State Treasurer will reduce local employer PERS normal and accrued liability contributions to be a percentage of the amount certified annually by the PERS to 80% for payments due in State fiscal year 2008.

Liabilities consist of pension and death benefit payments owed to members and beneficiaries, noncontributory group insurance premiums owed to the System's insurance provider, securities lending collateral and rebates payable, and other payables. Total liabilities increased by \$1.5 billion or 30.7% over last year. This is mainly due to an increase in securities lending collateral and rebates payable and in benefits payable to retirees and beneficiaries.

Net assets held in trust for pension benefits increased by \$3.1 billion or 12.1%.

Summary of Additions to Fiduciary Net Assets

2008 – 2007

	<u>2008</u>	<u>2007</u>	<u>Increase (decrease)</u>
Member contributions	\$ 705,903,439	654,493,521	51,409,918
Employer contributions	812,356,103	674,629,437	137,726,666
Net investment income (loss)	<u>(391,708,689)</u>	<u>3,810,965,382</u>	<u>(4,202,674,071)</u>
Totals	<u>\$ 1,126,550,853</u>	<u>5,140,088,340</u>	<u>(4,013,537,487)</u>

Additions consist of member and employer contributions and earnings from investment activities. Member contributions increased by \$51.4 million or 7.9% due to normal salary and membership increases.

Employer contributions increased by \$137.7 million or 20.4% over last year.

The State made a contribution of \$206.3 million for fiscal year 2008. The amount contributed in fiscal year 2008 was equal to approximately 39% of the actuarially determined amount. Also, the employer contributions include accrued appropriations due April 1, 2008 and early retirement incentive benefits billed to local employers.

Net investment income decreased by \$4.2 billion or 110.3% due to a decrease in the net appreciation of the fair value of investments.

The total investment return for all pension funds was estimated to be 2.66% loss compared to 17.1% gain in the prior year.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Management's Discussion and Analysis

June 30, 2008 and 2007

2007 – 2006

	<u>2007</u>	<u>2006</u>	<u>Increase</u>
Member contributions	\$ 654,493,521	630,322,617	24,170,904
Employer contributions	674,629,437	322,613,192	352,016,245
Net investment income	<u>3,810,965,382</u>	<u>2,338,406,222</u>	<u>1,472,559,160</u>
Totals	<u>\$ 5,140,088,340</u>	<u>3,291,342,031</u>	<u>1,848,746,309</u>

Additions primarily consist of member and employer contributions and earnings from investment activities. Member contributions increased by \$24.2 million or 3.8% due to normal salary increases.

Employer contributions increased by \$352.0 million or 109.1% over last year.

The State made a contribution of \$192.9 million for fiscal year 2007, the first significant contribution to the System since fiscal year 1997. The amount contributed in fiscal year 2007 was equal to approximately 57.5% of the actuarially determined amount. Also, the employer contributions include accrued appropriations due April 1, 2008 and early retirement incentive benefits billed to local employers.

Investment and other revenues increased by \$1.5 billion or 63.0% due to an increase in net appreciation in fair value of investments.

The total investment return for all pension funds was estimated to be 17.1% compared to 9.7% in the prior year.

Summary of Deductions from Fiduciary Net Assets

2008 – 2007

	<u>2008</u>	<u>2007</u>	<u>Increase</u>
Benefits	\$ 2,149,381,072	1,977,034,746	172,346,326
Refunds of contributions	93,590,971	77,345,336	16,245,635
Administrative expenses	<u>21,669,271</u>	<u>19,506,750</u>	<u>2,162,521</u>
Totals	<u>\$ 2,264,641,314</u>	<u>2,073,886,832</u>	<u>190,754,482</u>

Deductions are mainly comprised of pension benefit payments to retirees and beneficiaries, refunds of contributions to former members, and administrative costs incurred by the System. Benefit payments increased by \$172.3 million or 8.7% partly due to an increase in the number of retirees. The amount of refunds processed increased by \$16.2 million or 21.0%. Administrative expenses increased by \$2.2 million or 11.1%.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Management's Discussion and Analysis

June 30, 2008 and 2007

2007 – 2006

	<u>2007</u>	<u>2006</u>	<u>Increase</u>
Benefits	\$ 1,977,034,746	1,809,376,698	167,658,048
Refunds of contributions	77,345,336	70,271,522	7,073,814
Administrative expenses	19,506,750	17,365,728	2,141,022
Totals	<u>\$ 2,073,886,832</u>	<u>1,897,013,948</u>	<u>176,872,884</u>

Deductions are mainly comprised of pension benefit payments to retirees and beneficiaries, refunds of contributions to former members, and administrative costs incurred by the System. Benefit payments increased by \$167.7 million or 9.3% partly due to an increase in the number of retirees. The amount of refunds processed increased by \$7.1 million or 10.1%. Administrative expenses have increased by \$2.1 million or 12.3%.

Retirement System as a Whole

The overall funded ratios of 76.0% for fiscal year 2008 and 78.0% for fiscal year 2007 indicate that the System is reasonably funded.

Contacting System Financial Management

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

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Statements of Fiduciary Net Assets

June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Assets:		
Cash	3,234,492	—
Securities lending collateral	\$ 4,331,393,425	6,189,377,299
Investments, at fair value:		
Cash Management Fund	1,247,221,461	1,042,670,402
Bonds	37,487,274	72,403,031
Common Pension Fund A	7,700,330,505	10,361,222,471
Common Pension Fund B	7,192,937,262	7,152,080,186
Common Pension Fund D	5,632,458,523	5,649,171,869
Common Pension Fund E	3,371,839,578	2,123,723,024
Mortgages	51,055,130	60,626,217
Total investments	<u>25,233,329,733</u>	<u>26,461,897,200</u>
Receivables:		
Contributions:		
Members	77,944,271	74,639,159
Employers	1,451,708,782	1,258,945,811
Accrued interest and dividends	260,338,191	172,961,771
Members' loans	428,260,732	479,776,089
Other	4,737,055	3,325,804
Total receivables	<u>2,222,989,031</u>	<u>1,989,648,634</u>
Total assets	<u>31,790,946,681</u>	<u>34,640,923,133</u>
Liabilities:		
Accounts payable and accrued expenses	36,483,509	24,492,545
Retirement benefits payable	177,801,277	44,458,326
Non-contributory group insurance premiums payable	8,312,667	6,751,294
Cash overdraft	—	797,405
Securities lending collateral and rebates payable	4,331,393,425	6,189,377,299
Total liabilities	<u>4,553,990,878</u>	<u>6,265,876,869</u>
Net Assets:		
Held in trust for pension benefits	\$ <u>27,236,955,803</u>	<u>28,375,046,264</u>

See schedule of funding progress on pages 42-43.

See accompanying notes to financial statements.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Statements of Changes in Fiduciary Net Assets

Years ended June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Additions:		
Contributions:		
Members	\$ 705,903,439	654,493,521
Employers	812,356,103	674,629,437
Total contributions	<u>1,518,259,542</u>	<u>1,329,122,958</u>
Investment income:		
Net (depreciation) appreciation in fair value of investments	(1,321,131,720)	3,014,223,973
Interest	704,634,268	581,860,217
Dividends	231,079,450	221,326,372
	<u>(385,418,002)</u>	<u>3,817,410,562</u>
Less investment expense	<u>6,290,687</u>	<u>6,445,180</u>
Net investment (loss) income	<u>(391,708,689)</u>	<u>3,810,965,382</u>
Total additions	<u>1,126,550,853</u>	<u>5,140,088,340</u>
Deductions:		
Benefits	2,149,381,072	1,977,034,746
Refunds of contributions	93,590,971	77,345,336
Administrative and miscellaneous expenses	21,669,271	19,506,750
Total deductions	<u>2,264,641,314</u>	<u>2,073,886,832</u>
Change in net assets	(1,138,090,461)	3,066,201,508
Net assets - beginning of year	<u>28,375,046,264</u>	<u>25,308,844,756</u>
Net assets - end of year	<u>\$ 27,236,955,803</u>	<u>28,375,046,264</u>

See accompanying notes to financial statements.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

(1) Description of the System

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

At June 30, 2007 and 2006, the dates of the most recent actuarial valuations, participating employers consisted of the following:

	2007	2006
State of New Jersey	1	1
County agencies	65	66
Municipalities	580	576
School districts	558	588
Other public agencies	487	446
Total	1,691	1,677

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

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

The System adopted Governmental Accounting Standards Board (GASB) Statement No. 43, "*Financial Reporting for Postemployment Benefit Plans Other than Pension Plans*" (OPEB) as of July 1, 2006. Prior to the adoption, the Post-Retirement Medical Fund (PRM) of PERS was reported as a trust fund and was combined with the PERS pension trust fund plan. As a result of the implementation of GASB Statement No. 43, PRM of PERS is combined with the State Health Benefits Program Fund (SHBP) and the Prescription Drug Program Fund (PDP) and reported as Health Benefit Program Funds. Specifically, SHBP-State, PDP-State, and PRM of PERS are combined and reported as a trust fund classified as a single employer plan. Certain amounts included in the PERS PRM are legally required to be transferred to the SHBP and are recorded as additions and deductions in PERS PRM and SHBP. All interfund transactions have been eliminated in the financial statements of the SHBP.

In 2008, the System adopted the provisions of GASB Statement No. 50, "*Pension Disclosures*."

Vesting and Benefit Provisions

The vesting and benefit provisions are set by N.J.S.A. 43:15A and 43:3B. The PERS provides retirement, death and disability benefits. All benefits vest after eight to ten years of service, except for medical

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

benefits, which vest after 25 years of service or under the disability provisions of the System. Retirement benefits for age and service are available at age 60 and are generally determined to be 1/55 of final average salary for each year of service credit (as defined). Final average salary equals the average salary for the final three years of service prior to retirement (or highest three years' compensation if other than the final three years). Members may seek early retirement after achieving 25 years service credit, as defined, or they may elect deferred retirement after achieving eight to ten years of service credit, in which case benefits would begin the first day of the month after the member attains normal retirement age.

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

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

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

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

Chapter 103, P.L. 2007 amended the early retirement reduction formula for members hired on or after July 1, 2007 and retiring with 25 years of service to be reduced by 1 percent for every year under age 60 to age 55 plus 3 percent for every year under age 55.

Significant Legislation

Chapter 103, P.L. 2007, certain parts effective July 1, 2007, provided for the following: changed contribution rate of the PERS to 5.5% of annual compensation; imposed an annual maximum wage contribution base; and amended the early retirement reduction formula for the new members. If a person became a member on or after July 1, 2007, that person must be at least 60 years of age in order to retire without a reduction in their retirement allowance. The legislation also eliminated the funding for the postretirement medical benefits through the PERS.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

Chapter 92, P.L. 2007 implemented certain recommendations contained in the December 1, 2006 report of the Joint Legislative Committee on Public Employee Benefits Reform. Effective July 1, 2007, the legislation closed the Workers' Compensation Judges Part of PERS to new members. Effective January 1, 2008, the new pension loan interest rate became 4.69% per year, and an \$8.00 processing fee per loan was charged. The legislation also removed language from existing law that permits the State Treasurer to reduce employer pension contributions needed to fund the system when excess assets are available.

Chapter 21, P.L. 2008, effective June 24, 2008, provided early retirement incentive program to eligible State employees in the Executive Branch of State government and eligible Judiciary employees in the Judicial Branch of State government who apply to retire on or after March 1, 2008 but by July 15, 2008 and retire by August 1, 2008.

Membership

Membership in the System consisted of the following at June 30, 2007 and 2006, the dates of the most recent actuarial valuations:

	2007	2006
Retirees and beneficiaries receiving benefits currently and terminated employees entitled to benefits but not yet receiving them	130,686	126,592
Active members:		
Vested	140,400	140,306
Non-vested	178,853	177,434
Total active members	319,253	317,740
Total	449,939	444,332

(2) Summary of Significant Accounting Policies

Measurement Focus and Basis of Accounting

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. The System is accounted for using an economic resources measurement focus.

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

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

Investments

The Division of Investment, Department of the Treasury, State of New Jersey (Division of Investment) manages and invests certain assets of seven of the defined benefit plans (PERS, TPAF, JRS, PFRS, CPFPPF, SPRS and POPF). The Division of Investment separately reports the assets, liabilities and net assets of the underlying investment portfolio of the seven defined benefit plans in its Pension Fund report. The Division of Investment accounts included in the Pension Fund report are: Common Fund A, Common Fund B, Common Fund D, Common Fund E, Police and Firemen's Mortgage Program accounts and other investments owned directly by the seven defined benefit pension plans. Common Fund A invests primarily in domestic equity securities. Common Fund B invests primarily in domestic fixed income securities. Common Fund D invests primarily in foreign equity and fixed income securities. Common Fund E invests primarily in alternative investments which includes private equity, real assets and absolute return strategy investments. The Police and Firemen's Retirement System includes a mortgage loan program administered by the New Jersey Housing and Mortgage Finance Agency that provides participants with mortgages from the program at rates which are fixed by formula. The law establishing the program provides that the System may not sell the mortgages, and no independent market exists for them.

Investments are reported at fair value as follows:

- U.S. Government and Agency, Foreign and Corporate obligations – prices quoted by a major dealer in such securities.
- Common Stock and Equity Funds, Foreign Equity Securities, Forward Foreign Exchange Contracts – closing prices as reported on the primary market or exchange on which they trade.
- Money Market Instruments – amortized cost which approximates fair value.
- Cash Management Fund – closing bid price on the last day of trading during the period as determined by the Transfer Agent.
- Alternative investments (private equity, real estate, commodity, and absolute return strategy funds) – estimated fair value provided by the general partner and/or investment manager and reviewed by management. The inputs into the determinations of fair value (particularly for private equity and real estate) require significant management judgment or estimation. Because by their very nature, alternative investments are not always readily marketable, their estimated value is subject to uncertainty and therefore may differ significantly from the value that would be used if a ready market for such investments existed. The development of fair value is further complicated by (1) the current lack of liquidity in the financial system and (2) the extreme levels of volatility in the market for public equity in general and for debt securities linked to these asset classes. For these reasons, the realized value received upon the sale of these investments in the open market might be different from the fair value reported in the financial statements.

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

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

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

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

Securities Lending

The State Investment Council policies permit Common Funds A, B and D and several of the direct pension plan portfolios to participate in securities lending programs, whereby securities are loaned to brokers or other borrowers and, in return, the pension funds have rights to the collateral received. All of the securities held in Common Funds A, B and D, and certain securities held directly by the pension plans, are eligible for the securities lending program. Collateral received may consist of cash, letters of credit, or government securities having a market value equal to or exceeding 102% (U.S. dollar denominated) or 105% (non-U.S. dollar denominated) of the value of the loaned securities at the time the loan is made. For Common Funds A and B, in the event that the market value of the collateral falls below 101% of the market value of all the outstanding loaned securities to an individual borrower, additional collateral shall be transferred by the borrower to the respective funds no later than the close of the next business day so that the market value of such additional collateral, when added to the market value of the other collateral, shall equal 102% of the market value of the loaned securities. For Common Fund D, in the event that the market value of the collateral falls below the collateral requirement of either 102% or 105% (depending on whether the securities are denominated in U.S. dollars or a foreign currency, respectively) of the market value of the outstanding loaned securities to an individual borrower, additional collateral shall be transferred in an amount that will increase the aggregate of the borrower's collateral to meet the collateral requirements. The securities lending contracts do not allow the Common Funds to pledge or sell any collateral securities unless the borrower defaults. As of June 30, 2008 and 2007, the Common Funds have no aggregate credit risk exposure to brokers because the collateral amount held by the Common Funds exceeded the market value of the securities on loan.

The contracts with the Common Funds' securities lending agent require them to indemnify the Common Funds if the brokers or other borrowers fail to return the securities or fail to pay the Common Funds for income distributions on the securities while they are on loan. The Common Fund D securities lending agent also indemnifies the Common Funds for any loss of principal or interest on the invested collateral. For any losses on the investment collateral in Common Funds A or B or other pension plan portfolios, the

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

lending fee paid to the lending agent shall be reduced by 25% of the amount of such loss, up to an amount not to exceed 75% of the previous six months' securities lending fees. The securities loans can be terminated by notification by either the borrower or the Common Funds. The term to maturity of the securities loans is generally matched with the term to maturity of the investment (or, in the case of floating rate notes, to the next interest rate reset date) of the cash collateral.

Derivatives

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

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

There were no foreign forward currency contracts at June 30, 2007. The fair value of foreign forward currency contracts held directly by the Common Funds as of June 30, 2008 was as follows:

Forward currency receivable	\$	1,353,214,830
Forward currency payable		1,358,471,309
Net unrealized loss		5,256,479

The Common Funds utilize covered call and put options in an effort to add value to or reduce the risk level in the portfolio. Options are agreements that give the owner of the option the right, but not obligation, to buy (in the case of a call option) or to sell (in the case of a put option) a specific amount of an asset for a specific price (called the strike price) on or before a specified expiration date. The Common Funds enter into covered calls when they write (or sell) call options on underlying stocks held by the Common Funds or stock indices. The Common Funds enter into covered put options when they purchase put options on underlying stocks held by the Common Funds or stock indices. The purchaser of put options pays a premium at the outset of the agreement and stands to gain from an unfavorable change (i.e., a decrease) in the price of the instrument underlying the option. The writer of call options receives a premium at the outset of the agreement and bears the risk of an unfavorable change (i.e., an increase) in the price of the instrument underlying the option. The Common Funds had written call options on 5,661,100 shares with a fair value of \$895,504 at June 30, 2008. The Common Funds owned 880,000 put option contracts on the S&P 500 index with a fair value of \$72,334,000 at June 30, 2008.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

Certain alternative investment funds and partnerships may use derivative instruments to hedge against market risk and to enhance investment returns. At any point during the year, the Common Funds may have additional exposure to derivatives primarily through limited liability vehicles such as limited partnerships and commingled investment funds.

The Common Funds recognize the fair value of all derivative instruments as either an asset or liability on the financial statements with the offsetting gains or losses recognized in earnings.

Members' Loans

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

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

Chapter 92, P.L. 2007 eliminated the 4% fixed rate of interest for loans from the defined benefit plans and provided that the rate of interest will be set by the State Treasurer at a commercially reasonable rate as required by the Internal Revenue Code and permitted that an administrative processing fee may be charged for such loans. As such, effective January 1, 2008, the new pension loan interest rate became 4.69% per year, and an \$8.00 processing fee per loan was charged.

Administrative Expenses

The System is administered by the State of New Jersey Division of Pensions and Benefits. Administrative expenses are paid by the System to the State of New Jersey, Department of the Treasury, and are included in the accompanying financial statements.

Funded Status and Funding Progress

The required supplementary information regarding the funded status and funding progress is based on actuarial valuations which involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. These amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the probability of future events.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

The required schedule of funding progress presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Actuarial calculations reflect a long-term perspective and are based on the benefits provided under State statutes in effect at the time of each valuation and also consider the pattern of the sharing of costs between the employer and members at that point in time. The projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects of legal or contractual funding limitations on the pattern of cost sharing between the employer and members in the future.

Actuarial Methods and Assumptions

In the June 30, 2007 and 2006 actuarial valuations, the projected unit credit was used as actuarial cost method, and the five year average of market value was used as the asset valuation method for the System. The actuarial assumptions included (a) 8.25% for investment rate of return and (b) 5.45% for projected salary increases.

	State		Local	
	June 30, 2007	June 30, 2006	June 30, 2007	June 30, 2006
Actuarial valuation date				
Actuarial value of assets	\$ 11,024,255,608	\$ 10,668,645,162	\$ 17,690,520,507	\$ 16,699,827,172
Actuarial accrued liability	16,028,875,601	14,797,684,446	21,764,214,593	20,273,979,840
Unfunded (overfunded)				
actuarial accrued liability	5,004,619,993	4,129,039,284	4,073,694,086	3,574,152,668
Funded ratio	68.8%	72.1%	81.3%	82.4%
Covered payroll	\$ 4,434,933,181	\$ 4,253,564,219	\$ 6,983,534,635	\$ 6,730,309,209
Unfunded (overfunded)				
actuarial accrued liability				
as a percentage of				
covered payroll	112.8%	97.1%	58.3%	53.1%
Actuarial cost method	Projected unit credit	Projected unit credit	Projected unit credit	Projected unit credit
Asset valuation method	5 year average of market value	5 year average of market value	5 year average of market value	5 year average of market value
Amortization method	Level percent, open	Level percent, open	Level percent, open	Level percent, open
Payroll growth rate for amortization	4%	4%	4%	4%
Remaining amortization period	30 years	30 years	30 years	30 years
Actuarial assumptions:				
Interest rate	8.25%	8.25%	8.25%	8.25%
Salary range	5.45%	5.45%	5.45%	5.45%
Cost-of-living adjustments	1.80%	1.80%	1.80%	1.80%

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

(3) Investments

The System is invested in Common Fund A, Common Fund B, Common Fund D, Common Fund E, and other investments, including bonds and mortgage backed securities, which represent 31.72%, 34.34%, 31.44%, 33.31%, and 3.51%, respectively, of each investment total of the Pension Fund as of June 30, 2008.

The System is invested in Common Fund A, Common Fund B, Common Fund D, Common Fund E, and other investments, including bonds and mortgage backed securities, which represent 31.18%, 34.16%, 31.89%, 34.98%, and 4.63%, respectively, of each investment total of the Pension Fund as of June 30, 2007.

Pension funds' investments as of June 30 are as follows:

	2008	2007
Domestic equities	\$ 23,849,523,038	31,474,841,997
International equities	14,728,747,252	17,174,769,178
Domestic fixed income	20,276,259,245	19,648,980,451
International fixed income	2,913,035,116	996,400,682
Commodity funds	975,518,400	502,393,611
Police and Fireman's mortgages	1,288,049,378	1,109,584,450
Private equity	2,850,167,142	1,159,903,960
Real estate	1,916,228,663	1,003,932,926
Absolute return strategy funds	3,739,013,571	2,340,519,278
	\$ 72,536,541,805	75,411,326,533

New Jersey state statute provides for a State Investment Council (Council) and a Director. Investment authority is vested in the Director of the Division of Investment and the role of the Council is to formulate investment policies. The Council issues regulations which establish guidelines for permissible investments which include domestic and international equities and exchange traded funds, covered call and put options, equity futures contracts, obligations of the U.S. Treasury, government agencies, corporations, finance companies and banks, obligations of international corporations, governments and agencies, interest rate swap transactions, fixed income exchange traded funds, U.S. Treasury futures contracts, New Jersey State and Municipal general obligations, public authority revenue obligations, collateralized notes and mortgages, commercial paper, certificates of deposit, repurchase agreements, bankers acceptances, guaranteed income contracts, funding agreements, money market funds, private equity, real estate, other real assets and absolute return strategy funds and the State of New Jersey Cash Management Fund (CMF). The CMF is a short-term cash fund and is open to state and certain non-state participants.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

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

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

Custodial credit risk, as it relates to investments, is the risk that in the event of the failure of the counterparty to a transaction, the pension funds will not be able to recover the value of investment or collateral securities that are in the possession of the third party. The pension funds' investment securities are not exposed to custodial credit risk as they are held in segregated trust accounts in the name of the pension funds with the custodians.

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The credit risk of a debt instrument is evaluated by nationally recognized statistical rating agencies such as Moody's Investors Service, Inc. (Moody's), Standard & Poor's Corporation (S&P), and Fitch Ratings (Fitch). Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. There are no restrictions in the amount that can be invested in United States Treasury and Government agency obligations. Council regulations require minimum credit ratings for certain categories of fixed income obligations held directly by the pension funds and limit the amount that can be invested in any one issuer or issue.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

These limits for the period July 1, 2006 through September 4, 2006 were as follows:

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

(1) Short term ratings (e.g. P-1, A-1, F-1) are used for commercial paper and certificates of deposit.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

Effective September 5, 2006, the following limits became effective:

Category	Minimum rating ⁽¹⁾			Limitation of issuer's outstanding debt	Limitation of issue	Other limitations
	Moody's	S&P	Fitch			
Corporate obligations	Baa3	BBB-	BBB-	10%	25%	Not more than 5% of fund assets can be invested in one corporation
U.S. finance company debt and bank debentures	Baa3	BBB-	BBB-	10%	25%	Not more than 5% of fund assets can be invested in one corporation
International corporate obligations	Baa3	BBB-	BBB-	10%	25%	Not more than 5% of fund assets can be invested in any one issuer with maturities exceeding 12 months; not more than 10% of fund assets can be invested in this category
International government and agency obligations	Aa3	AA-	AA-	25%	Greater of 25% or \$10 million	Not more than 1% of fund assets can be invested in any one issuer
Collateralized notes and mortgages	Baa3	BBB-	BBB-	—	25%	Not more than 5% of fund assets can be invested in any one issue; not more than 10% of fund assets (or 20% of Fund B assets) can be invested in this category
Commercial paper	P-1	A-1	F1	—	—	—
Certificates of deposit and Banker's acceptances:						Certificates of deposit and banker's acceptances cannot exceed 10% of issuer's primary capital
Domestic	A3/P-1	A-/A-1	A-/F1	—	—	
International	Aa3/P-1	AA-/A-1	AA-/F1	—	—	
Guaranteed income contracts and funding agreements	A3	A-	A-	—	—	—
Money market funds	—	—	—	—	—	Not more than 10% of fund assets can be invested in money market funds; limited to 5% of shares or units outstanding

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

Category	Minimum rating ⁽¹⁾			Limitation of issuer's outstanding debt	Limitation of issue	Other limitations
	Moody's	S&P	Fitch			
Interest rate swap transactions	A3	A-	A-	—	—	Notional value of net exposure to any one counterparty shall not exceed 10% of fund assets
Repurchase agreements	Aa3	AA-	AA-	—	—	—
NJ state & municipal obligations	A3	A-	A-	10%	10%	Not more than 10% of fund assets can be invested in debt of any one political entity maturing more than 12 months from purchase
Public authority revenue obligations	A3	A-	A-	—	10%	Not more than 2% of fund assets can be invested in any one public authority
Mortgage backed pass-through securities	A3	A-	A-	—	—	Not more than 5% of fund assets can be invested in any one issue
Mortgage backed senior debt securities	—	—	—	—	25%	Not more than 5% of fund assets can be invested in any one issue

(1) Short term ratings (e.g. P-1, A-1, F-1) are used for commercial paper and certificates of deposit.

Effective August 20, 2007, up to 5% of the market value of the combined assets of the pension and annuity funds may be invested in corporate obligations, finance company debt, bank debentures, international corporate obligations, collateralized notes, and mortgages and mortgage backed pass-through securities that do not meet the minimum credit rating requirements set forth above; prior to that, the limitation was 5% of the market value of Common Fund B.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

For securities in the fixed income portfolio, the following tables disclose aggregate market value, by major credit quality rating category at June 30, 2008 and 2007:

(In thousands)	June 30, 2008						
	Moody's rating						
	Aaa	Aa	A	Baa	Ba	B	Caa
United States Treasury TIPS	\$ 3,573,893	—	—	—	—	—	—
United States Treasury Bonds	3,914,404	—	—	—	—	—	—
United States Treasury Strips	622,327	—	—	—	—	—	—
Title XI Merchant Marine Notes	2,646	—	—	—	—	—	—
United States Government Agency Federal Home Loan Bank Notes and Bonds	78,910 120,820	— —	— —	— —	— —	— —	— —
Federal Home Loan Discounted Bonds	6,670	—	—	—	—	—	—
Floating Rate Notes	28,070	—	—	—	—	—	—
Tennessee Valley Authority Strips	166,919	—	—	—	—	—	—
Domestic Corporate Obligations	428,516	674,633	3,024,990	2,642,103	90,580	41,315	84,813
Domestic Corporate Discounted Obligations	105,177	—	4,879	—	—	—	—
International Corporate Obligations	—	—	205,817	193,352	—	—	—
Real Estate Investment Trust Obligations	—	—	—	19,391	—	—	—
Finance Company Debt	385,235	476,076	744,296	268,772	—	86,584	64,347
Foreign Government Obligations	1,077,186	150,700	—	—	—	—	—
Foreign Government Discount Obligations	879,287	—	—	—	—	—	—
Adjustable Rate Municipal Bonds	31,000	135,665	135,000	—	—	—	—
International Bonds and Notes	298,755	20,274	67,775	19,889	—	—	—
Remic/FHLMC	546,377	—	—	—	—	—	—
Remic/FNMA	50,343	—	—	—	—	—	—
SBA Pass-through Certificates	100,373	—	—	—	—	—	—
GNMA Mortgage Backed Certificates	148,306	—	—	—	—	—	—
FHLM Mortgage Backed Certificates	440,058	—	—	—	—	—	—
FNMA Mortgage Backed Certificates	448,589	—	—	—	—	—	—
Asset Backed Obligations	63,791	119,057	—	139,267	—	—	—
Private Export Obligations	85,742	—	—	—	—	—	—
Exchange Traded Securities	—	—	131,820	—	—	4,700	—
	<u>\$ 13,603,394</u>	<u>1,576,405</u>	<u>4,314,577</u>	<u>3,282,774</u>	<u>90,580</u>	<u>132,599</u>	<u>149,160</u>

The 2008 table does not include certain exchange traded funds (ETFs) totaling \$39,805,000 which invest in an underlying portfolio of fixed income securities and do not have a Moody's rating. The Police and Firemen's Mortgages and the Cash Management fund are unrated.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

(In thousands)	June 30, 2007			
	Moody's rating			
	Aaa	Aa	A	Baa
United States Treasury Notes	\$ 2,038,229	—	—	—
United States Treasury TIPS	1,875,022	—	—	—
United States Treasury Bonds	5,187,546	—	—	—
United States Treasury Strips	39,649	—	—	—
Title XI Merchant Marine Notes	2,786	—	—	—
Federal Agricultural Mortgage Corp. Notes	95,295	—	—	—
Federal Farm Credit Bank Bonds	50,227	—	—	—
Federal Home Loan Bank Bonds	289,167	—	—	—
Federal Home Loan Bank Discounted Notes	96,345	—	—	—
Federal National Mortgage Association Notes	96,355	—	—	—
Resolution Funding Corp. Obligations	6,466	—	—	—
Tennessee Valley Authority Strips	72,610	—	—	—
Floating Rate Notes	9,999	20,038	—	—
Domestic Corporate Obligations	427,646	760,349	2,093,792	2,020,011
International Corporate Obligations	—	—	47,912	35,330
Real Estate Investment Trust Obligations	—	—	—	34,025
Finance Company Debt	293,489	296,882	498,203	9,240
International Bonds and Notes	404,960	64,583	48,200	—
Foreign Government Obligations	302,900	92,516	—	—
Remic/FHLMC	952,817	—	—	—
Remic/FNMA	66,490	—	—	—
Remic/GNMA	17,969	—	—	—
GNMA Mortgage Backed Certificates	64,206	—	—	—
FHLM Mortgage Backed Certificates	939,992	—	—	—
FNMA Mortgage Backed Certificates	839,452	—	—	—
SBA Pass-through Certificates	9,700	—	—	—
Asset Backed Obligations	310,611	—	—	—
Private Export Obligations	56,771	—	—	—
Exchange Traded Securities	—	—	52,290	—
	<u>\$ 14,546,699</u>	<u>1,234,368</u>	<u>2,740,397</u>	<u>2,098,606</u>

The 2007 table does not include certain corporate obligations totaling \$25,310,000 which have an S&P rating of A and do not have a Moody's rating. The Police and Firemen's Mortgages and the Cash Management Fund are unrated.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Commercial paper must mature within 270 days. Certificates of deposits and bankers acceptances are limited to a term of one year or less. The maturity requirement for repurchase agreements was 15 days through September 4, 2006; this was revised to 30 days effective September 5, 2006. The investment in guaranteed income contracts and funding agreements is limited to a term of 10 years or less.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

The following tables summarize the maturities (or, in the case of Remics, Police and Firemen's Mortgages and mortgage-backed securities, the expected average life) of the fixed income portfolio at June 30, 2008 and 2007:

(In thousands)	June 30, 2008				
	Total	Maturities in years			
		market value	Less than 1	1-5	6-10
United States Treasury TIPS	\$ 3,573,893	—	—	369,231	3,204,662
United States Treasury Bonds	3,914,404	—	—	—	3,914,404
United States Treasury Strips	622,327	—	—	—	622,327
Title XI Merchant Marine Notes	2,646	—	—	—	2,646
United States Government Agency	78,910	—	—	—	78,910
Federal Home Loan Bank Notes and Bonds	120,820	—	—	38,492	82,328
Federal Home Loan Discounted Bonds	6,670	—	—	—	6,670
Floating Rate Notes	28,071	—	18,071	10,000	—
Tennessee Valley Authority Strips	166,919	—	—	—	166,919
Domestic Corporate Obligations	6,986,947	4,993	756,272	1,655,983	4,569,699
Domestic Corporate Discounted Obligations	110,056	—	8,234	—	101,822
International Corporate Obligations	399,169	—	—	69,560	329,609
Real Estate Investment Trust Obligations	19,391	—	19,391	—	—
Finance Company Debt	2,025,311	154,379	183,305	989,819	697,808
Foreign Government Obligations	1,227,887	70,477	230,400	45,001	882,009
Foreign Government Discount Obligations	879,287	879,287	—	—	—
Adjustable Rate Municipal Bonds	301,665	—	—	—	301,665
International Bonds and Notes	406,693	—	25,795	196,102	184,796
Remic/FHLMC	546,377	—	—	19,647	526,730
Remic/FNMA	50,343	—	—	—	50,343
SBA Pass-through Certificates	100,373	—	—	100,373	—
Police and Firemen's Mortgages	1,288,049	—	—	—	1,288,049
GNMA Mortgage Backed Certificates	148,306	—	—	—	148,306
FHLM Mortgage Backed Certificates	440,058	6	181	1,820	438,051
FNMA Mortgage Backed Certificates	448,589	339	2,146	11,959	434,145
Asset Backed Obligations	322,115	—	31,144	14,594	276,377
Private Export Obligations	85,743	12,547	21,219	51,977	—
	<u>\$ 24,301,019</u>	<u>1,122,028</u>	<u>1,296,158</u>	<u>3,574,558</u>	<u>18,308,275</u>

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

(In thousands)	June 30, 2007				
	Total	Maturities in years			
		market value	Less than 1	1-5	6-10
Fixed income investment type					
United States Treasury Notes	\$ 2,038,229	148,736	447,759	1,441,734	—
United States Treasury TIPS	1,875,022	—	185,141	762,104	927,777
United States Treasury Bonds	5,187,546	—	—	86,215	5,101,331
United States Treasury Strips	39,649	—	—	—	39,649
Title XI Merchant Marine Notes	2,786	—	—	—	2,786
Federal Agricultural Mortgage Corp. Notes	95,295	—	95,295	—	—
Federal Farm Credit Bank Bonds	50,227	20,114	30,113	—	—
Federal Home Loan Bank Bonds	289,167	18,107	250,170	20,890	—
Federal Home Loan Bank Discounted Notes	96,345	—	—	—	96,345
Federal National Mortgage Association Notes	96,355	—	96,355	—	—
Resolution Funding Corp. Obligations	6,466	—	—	—	6,466
Floating Rate Notes	30,037	—	20,038	9,999	—
Tennessee Valley Authority Strips	72,610	—	—	—	72,610
Domestic Corporate Obligations	5,327,108	127,673	850,539	959,663	3,389,233
International Corporate Obligations	83,242	—	—	—	83,242
Real Estate Investment Trust Obligations	34,025	—	19,574	14,451	—
Finance Company Debt	1,097,814	59,175	552,626	243,679	242,334
Foreign Government Obligations	395,416	64,184	244,266	67,973	18,993
International Bonds and Notes	517,743	69,410	128,538	110,541	209,254
Remic/FHLMC	952,817	—	—	39,882	912,935
Remic/FNMA	66,490	—	—	18,036	48,454
Remic/GNMA	17,969	—	—	—	17,969
SBA Pass-through Certificates	9,700	—	—	9,700	—
Police and Firemen's Mortgages	1,109,585	425	839	9,292	1,099,029
GNMA Mortgage Backed Certificates	64,206	131	36	—	64,039
FHLM Mortgage Backed Certificates	939,992	—	68	2,644	937,280
FNMA Mortgage Backed Certificates	839,452	171	5,284	16,137	817,860
Asset Backed Obligations	310,611	—	59,947	59,978	190,686
Private Export Obligations	56,771	—	32,490	24,281	—
	<u>\$ 21,702,675</u>	<u>508,126</u>	<u>3,019,078</u>	<u>3,897,199</u>	<u>14,278,272</u>

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The pension funds invest in global markets. Effective August 20, 2007, the market value of international preferred and common stocks and issues convertible into common stocks, when combined with the market value of international government and agency obligations, cannot exceed 30% of the market value of the pension funds; previously, this limitation was 22%. Effective September 5, 2006, the market value of emerging market securities cannot exceed more than 1.5 times the percentage derived by dividing the total market capitalization of companies included in the Morgan Stanley Capital International (MSCI) Emerging Market Index by the total market capitalization of the companies included in the MSCI All-Country World Ex-United States Index of the total market value of the assets held by Common Fund D. Prior to September 5, 2006, not more than 5% of the value of the assets held by Common Fund D can be invested in companies incorporated in emerging market countries. Not more than 10% of the market value of the emerging market securities can be invested in the common and preferred stock of any one corporation; the total amount of stock purchased of any one corporation cannot exceed 5% of its stock

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

classes eligible to vote. Council regulations permit the pension funds to enter into foreign exchange contracts for the purpose of hedging the international portfolio. The pension funds held forward contracts totaling approximately \$1.4 billion (with a \$5.3 million net exposure) at June 30, 2008. The pension funds did not have a forward contract exposure at June 30, 2007.

The pension funds had the following foreign currency exposure (expressed in U.S. dollars and in thousands) at June 30, 2008 and 2007:

June 30, 2008				
<u>Currency</u>	<u>Total market value</u>	<u>Equities</u>	<u>Foreign government obligations</u>	<u>Alternative investments</u>
Australian dollar	\$ 614,583	456,834	157,749	—
Brazilian Real	118,301	118,301	—	—
Canadian dollar	546,560	546,560	—	—
Chilean peso	1,286	1,286	—	—
Czech koruna	4,512	4,512	—	—
Danish krone	205,512	205,512	—	—
Euro	6,983,288	5,829,751	1,005,136	148,401
Egyptian pound	20,424	20,424	—	—
Hong Kong dollar	263,291	263,291	—	—
Hungarian forint	6,528	6,528	—	—
Indonesian rupiah	22,783	22,783	—	—
Israeli shekel	14,716	14,716	—	—
Japanese yen	2,822,687	1,943,400	879,287	—
Malaysian ringgit	18,557	18,557	—	—
Mexican peso	19,444	19,444	—	—
New Zealand dollar	18,052	18,052	—	—
Norwegian krone	451,099	451,099	—	—
Omani rial	1,991	1,991	—	—
Pakistan rupee	2,679	2,679	—	—
Philippines peso	1,050	1,050	—	—
Polish peso	9,910	9,910	—	—
Qatar rial	4,497	4,497	—	—
Singapore dollar	135,551	135,551	—	—
South African rand	69,675	69,675	—	—
South Korean won	110,363	110,363	—	—
Swedish krona	521,596	521,596	—	—
Swiss franc	1,460,269	1,460,269	—	—
New Taiwan dollar	13,978	13,978	—	—
Thailand baht	17,001	17,001	—	—
Turkish lira	27,871	27,871	—	—
British pound sterling	1,970,705	1,916,931	—	53,774
	<u>\$ 16,478,759</u>	<u>14,234,412</u>	<u>2,042,172</u>	<u>202,175</u>

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

June 30, 2007				
Currency	Total market value	Equities	Foreign government obligations	Alternative Investments
Australian dollar	\$ 472,778	472,778	—	—
Canadian dollar	700,076	700,076	—	—
Danish krone	236,914	236,914	—	—
Euro	5,777,859	5,466,997	278,743	32,119
Hong Kong dollar	187,292	187,292	—	—
Japanese yen	4,377,681	4,377,681	—	—
Mexican peso	74,710	74,710	—	—
New Zealand dollar	26,505	26,505	—	—
Norwegian krone	426,080	426,080	—	—
Pound sterling	2,077,051	2,051,057	—	25,994
Singapore dollar	151,674	151,674	—	—
South Korean won	175,851	175,851	—	—
Swedish krona	897,683	897,683	—	—
Swiss franc	1,702,575	1,702,575	—	—
	\$ 17,284,729	16,947,873	278,743	58,113

The pension funds' interests in alternative investments may contain elements of credit, currency and market risk. Such risks include, but are not limited to, limited liquidity, absence of regulatory oversight, dependence upon key individuals, emphasis on speculative investments (both derivatives and non-marketable investments), and nondisclosure of portfolio composition. Effective September 5, 2006, Council regulations require that not more than 18% of the market value of the Pension Fund can be invested in alternative investments, with the individual categories of real estate, real assets, private equity and absolute return strategy investments limited to 7%. On August 18, 2008 the overall limitation was revised to 28%. Not more than 5% of the market value of Common Fund E, plus outstanding commitments, may be committed to any one partnership or investment, without the prior written approval of the Council. The investments in Common Fund E cannot comprise more than 20% of any one investment manager's total assets.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

(4) Securities Lending Collateral

The System's share in the securities lending program is 33.75% and 33.48% of the total market value of the collateral at June 30, 2008 and 2007, respectively.

The securities lending collateral is subject to various risks. Among these risks are credit risk, concentration of credit risk, and interest rate risk. Agreements with the lending agents require minimum credit ratings for certain categories of fixed income obligations and limit the amount that can be invested in any one issuer or issue. These limits are consistent with Council regulations and internal policies for funds managed by the Division of Investment. These limits for the period July 1, 2006 through September 4, 2006 were as follows:

<u>Category</u>	<u>Minimum rating</u>		<u>Limitation of issuer's outstanding debt</u>	<u>Limitation of issue</u>	<u>Other limitations</u>
	<u>Moody's</u>	<u>S&P</u>			
Certificates of deposit/ Banker's acceptances (rating applies to international)	Aa3/P-1	—	—	—	Uncollateralized certificates of deposit and banker's acceptances cannot exceed 10% of issuer's primary capital; dollar limits by issuer
Guaranteed income contracts	P-1	—	—	—	Limited to 5% of the assets of the collateral portfolio; A+ rating from A.M. Best for insurance companies
Money market funds	—	—	—	—	Limited to 10% of the assets of the collateral portfolio; limited to approved money market funds

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

Effective September 5, 2006, the following limits became effective:

Category	Minimum rating			Limitation of issuer's outstanding debt	Limitation of issue	Other limitations
	Moody's	S&P	Fitch			
Corporate obligations	Baa3	BBB-	BBB-	10%	25%	—
U.S. finance company debt and bank debentures	Baa3	BBB-	BBB-	10%	25%	—
Collateralized notes and mortgages	Baa3	BBB-	BBB-	—	25%	Limited to not more than 10% of the assets of the collateral portfolio
Commercial paper	P-1	A-1	F1	—	—	Dollar limits by issuer
Certificates of deposit/ Banker's acceptances:						Certificates of deposit and banker's acceptances' cannot exceed 10% of issuer's primary capital; dollar limits by issuer
Domestic	A3/P-1	A-/A-1	A-/F1	—	—	
International	Aa3/P-1	AA-/A-1	AA-/F1	—	—	
Guaranteed income contracts and funding agreements	A3	A-	A-	—	—	Limited to 5% of the assets of the collateral portfolio
Money market funds	—	—	—	—	—	Limited to 10% of the assets of the collateral portfolio; limited to approved money market funds

All investments in the collateral portfolio must mature or are to be redeemed within one year, except that up to 25% of the portfolio may be invested in eligible securities which mature within 25 months; provided, however, that the average maturity of all investments shall not exceed one year.

Maturities of corporate obligations, U.S. finance company debt, bank debentures, collateralized notes and mortgages, guaranteed income contracts, and funding agreements must be less than 25 months. Commercial paper maturities cannot exceed 270 days. Repurchase agreement maturities cannot exceed 30 days. Certificates of deposit and banker's acceptances must mature in one year or less.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

The collateral for repurchase agreements is limited to obligations of the U.S. Government or certain U.S. Government agencies, collateralized notes and mortgages and corporate obligations meeting certain minimum rating criteria.

Total exposure to any individual issuer is limited, except for U.S. Treasury and Government agency obligations. For money market funds, the total amount of shares or units purchased or acquired of any money market fund shall not exceed 5% of the shares or units outstanding of said money market fund. For Collateralized notes and mortgages, not more than 2% and 5% of the assets of the collateral portfolio shall be invested in the obligations of any one issuer and issue, respectively. For Guaranteed income contracts and funding agreements, the total investment in any one issuer shall be limited to 2.5% of the collateral portfolio. The Division of Investment sets individual issuer limits for Commercial paper and Certificate of deposits. For Corporate obligations, U.S. finance company debt, Bank debentures and Bankers acceptances, exposure to any one issuer shall be limited to the following percentages of the collateral portfolio in accordance with the issuer's rating from Moody's: Aaa (4%), Aa (3%), A (2%), and Baa (1%).

For securities exposed to credit risk in the collateral portfolio, the following tables disclose aggregate market value, by major credit quality rating category at June 30, 2008 and 2007. In those cases where an issuer and/or security have both a long-term and short-term rating, the short-term rating is presented.

		June 30, 2008									
		Rating									
(In thousands)		Aaa/AAA	Aaa/AA	Aa/AAA	Aa/AA	Aa/A	A/A	AA/A	A/Baa	Baa/BBB	Not rated
Corporate obligations	\$	711,148	269,317	224,455	2,835,773	570,502	1,796,638	9,988	142,151	139,676	—
Commercial paper		—	—	—	—	200,000	—	—	—	—	—
Certificates of deposit		—	—	—	608,740	753,645	—	—	—	—	—
Repurchase agreements		—	—	—	—	35,000	—	—	—	—	3,110,553
Asset backed securities		431,457	—	—	104,024	—	—	—	—	—	—
Money market funds		510,879	—	—	—	—	—	—	—	—	377,993
Cash		—	—	—	—	—	—	—	—	—	474
	\$	<u>1,653,484</u>	<u>269,317</u>	<u>224,455</u>	<u>3,548,537</u>	<u>1,559,147</u>	<u>1,796,638</u>	<u>9,988</u>	<u>142,151</u>	<u>139,676</u>	<u>3,489,020</u>

		June 30, 2007					
		Rating					
(In thousands)		Aaa/AAA	Aa/AA	A/A	Baa/BBB	P1	Not rated
Corporate obligations	\$	1,142,643	3,209,558	2,712,377	217,479	713,321	—
Commercial paper		—	—	—	—	3,594,013	—
Certificates of deposit		—	99,985	—	—	1,032,601	—
Repurchase agreements		—	—	—	—	—	1,765,830
Funding agreements		—	—	—	—	700,000	—
Money market funds		10,763	1,730,000	500,000	—	—	285,379
Collateralized notes		150,200	5,005	—	—	618,881	—
Cash		—	—	—	—	—	113
	\$	<u>1,303,606</u>	<u>5,044,548</u>	<u>3,212,377</u>	<u>217,479</u>	<u>6,658,816</u>	<u>2,051,322</u>

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

The following tables summarize the maturities of the collateral portfolio at June 30, 2008 and 2007:

(In thousands)	June 30, 2008		
	Total	Maturities	
	market value	Less than one year	One year to 25 months
Corporate obligations	\$ 6,699,648	5,115,159	1,584,489
Commercial paper	200,000	200,000	—
Certificates of deposit	1,362,384	1,362,384	—
Repurchase agreements	3,145,553	3,145,553	—
Money market funds	888,872	888,872	—
Asset backed securities	535,482	535,482	—
	\$ 12,831,939	11,247,450	1,584,489

(In thousands)	June 30, 2007		
	Total	Maturities	
	market value	Less than one year	One year to 25 months
Corporate obligations	\$ 7,995,378	4,154,943	3,840,435
Commercial paper	3,594,013	3,594,013	—
Certificates of deposit	1,132,586	1,132,586	—
Repurchase agreements	1,765,830	1,765,830	—
Funding agreements	700,000	700,000	—
Money market funds	2,526,142	2,526,142	—
Collateralized notes	774,086	769,081	5,005
	\$ 18,488,035	14,642,595	3,845,440

As of June 30, 2008, the pension funds had outstanding loaned investment securities with an aggregate market value of \$12,580,839,859 and received cash collateral with an aggregate fair value of \$12,793,553,099 and non-cash collateral of \$70,403,098. As of June 30, 2007, the Pension Fund had outstanding loaned investment securities with an aggregate market value of \$18,034,823,201 and received cash collateral of \$18,423,399,432 and non-cash collateral of \$4,471,761. In accordance with GASB accounting standards, the non-cash collateral is not reflected in the accompanying financial statements. There were no material violations of legal or contractual provisions, no borrower or lending agent default losses, and no recoveries or prior-period losses during the year.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

(5) Contributions

The contribution policy is set by N.J.S.A. 43:15A and requires contributions by active members and contributing employers. Plan member and employer contributions may be amended by State of New Jersey legislation. Members contribute at a uniform rate. The full normal employee contribution rate became 5.5% of annual compensation, effective July 1, 2007 for most PERS state employees and effective July 1, 2008 for PERS local employees, based on Chapter 103, P.L. 2007. The rate for members who are eligible for the Prosecutors Part of PERS (Chapter 366, P.L. 2001) is 7.5% of base salary. Employers are required to contribute at an actuarially determined rate. The annual employer contributions include funding for basic retirement allowances, cost-of-living adjustments, and noncontributory death benefits.

Chapter 103, P.L. 2007 also provided that for members hired on or after July 1, 2007, the amount of compensation used for employer and member contributions and benefits under the PERS cannot exceed the annual maximum wage contribution base for Social Security, pursuant to the Federal Insurance Contributions Act.

Chapter 108, P.L. 2003 provided that the State Treasurer will reduce local employer PERS normal and accrued liability contributions to be a percentage of the amount certified annually by the PERS as follows: 20% for payments due in State fiscal year 2005; not more than 40% in fiscal year 2006; not more than 60% in fiscal year 2007; and not more than 80% in fiscal year 2008.

The State made a contribution of \$206.31 million, excluding the State's contribution of non-contributory group insurance (NCGI) of \$27.73 million, early retirement incentives (ERI) of \$41.88 million, and others of \$3.97 million for fiscal year 2008. The State made a contribution of \$192.95 million, excluding the State's contribution of NCGI of \$23.51 million, ERI of \$37.93 million, and others of \$2.01 million for fiscal year 2007. The amounts contributed in fiscal years 2008 and 2007 are equal to 38.89% and 50.78% of the actuarially determined amounts, respectively.

Beginning with the July 1, 2007 valuation, Chapter 92, P.L. 2007 removed language from existing law that permits the State Treasurer to reduce the employer normal contributions and employee contributions needed to fund the PERS when excess assets are available.

(6) Funds

PERS maintains the following legally required funds as follows:

Members' Annuity Savings and Accumulative Interest Fund (2008 – \$9,192,154,747; 2007 – \$8,530,151,309)

The Members' Annuity Savings Fund (ASF) is credited with all contributions made by active members of the System. Interest earned on member contributions is credited to the Accumulative Interest Fund. Member withdrawals are paid out of this Fund.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

Contingent Reserve Fund (2008 – \$-1,567,146,929; 2007 – \$1,467,366,773)

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

Retirement Reserve Fund (2008 – \$18,937,443,630; 2007 – \$17,419,836,954)

The Retirement Reserve Fund is the account from which retirement benefits including cost-of-living adjustments are paid. Upon retirement of a member, accumulated contributions, together with accumulated interest, are transferred to the Retirement Reserve Fund from the Members' ASF and Accumulative Interest Fund. Any additional reserves needed for the retirement and cost-of-living benefits are transferred from the Contingent Reserve Fund. Annually, interest as determined by the State Treasurer (8.25% for fiscal years 2008 and 2007) is credited to the Retirement Reserve Fund.

Special Reserve Fund (2008 – \$0; 2007 – \$261,992,402)

The Special Reserve Fund is the fund to which excess earnings and gains from sales and maturities of investments are transferred and against which any losses from the sales of securities are applied. The maximum limit on the accumulation of this account is 1% of the market value of the investments allocated to the System, excluding Cash Management Fund investments and bonds allocated to the Contributory Group Insurance Premium Fund amounted to \$286.48 million as of June 30, 2008. Amounts in excess of 1% are credited to the Contingent Reserve Fund.

Contributory Group Insurance Premium Fund (2008 – \$283,850,009; 2007 – \$262,851,256)

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

Non-Contributory Group Insurance Premium Fund-Local (2008 – \$-32,892,997; 2007 – \$-11,589,626)

The Non-Contributory Group Insurance Premium Fund represents the accumulation of employer group insurance contributions in excess of premiums disbursed to the insurance carrier since the inception of the non-contributory death benefit program plus reserves held by the insurance carrier. Members are eligible by statute for the non-contributory group insurance plan in the first year of membership. PERS-Local maintained a negative balance which represents a restricted asset.

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Notes to Financial Statements

June 30, 2008 and 2007

Benefit Enhancement Reserve Fund (2008 – \$423,547,343; 2007 – \$444,437,196)

The Benefit Enhancement Reserve Fund is a special reserve fund from which the required normal contributions to provide benefit increases under Chapter 353, P.L. 2001 and Chapter 133, P.L. 2001 will be charged. The fund was established in 2002 and credited with excess assets equivalent to member contributions for fiscal years 2000 and 2001 by transferring reserves in the Contingent Reserve Fund to the Benefit Enhancement Fund. Additional transfers will be made, as required, to maintain a fund balance equal to the present value of expected additional normal contributions due to the increased benefits.

(7) Income Tax Status

Based on a May 2007 declaration of an outside tax council retained by the Attorney General of the State of New Jersey, the System complies with the qualification requirements of Section 401(a) of the Internal Revenue Code.

(8) Subsequent Events

Significant Legislation

Chapter 89, P.L. 2008, effective November 1, 2008, increased PERS retirement age. If a person becomes a member on or after November 1, 2008, that person must be at least 62 years of age in order to retire without a reduction in their retirement allowance.

Chapter 19, P.L. 2009, effective March 17, 2009 gives local PERS employers the option to defer 50% of their contributions in fiscal year 2009 the normal and accrued liability and pay 50 percent of the certified amount as determined by the actuary or pay the full 100% certified amounts.

Investment Performance

Subsequent to the June 30, 2008 fiscal year end, global financial markets suffered significant declines in value attributable to significant strains on many of the world's largest financial institutions. These difficulties, which were caused by a combination of liquidity constraints and continued write downs of mortgage-related assets, have resulted in a global economic downturn that has negatively impacted the value of most financial assets.

The investment assets of the Pension Funds have also incurred a considerable decline in value since June 30, 2008 due to these unfavorable market conditions. As of December 31, 2008 the fair value of the portfolio declined by approximately 17.9% due to these factors. Readers of this financial statement should check the New Jersey Division of Investment's website for more current information about the fair value of the pension funds' portfolio.

STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

Required Supplementary Information

Schedule of Funding Progress

(Unaudited - See accompanying independent auditors' report)

Actuarial valuation date	Actuarial value of assets (a)	Actuarial accrued liability (b)	Unfunded (overfunded) actuarial accrued liability (b - a)	Funded ratio (a / b)	Covered payroll (c)	Unfunded (overfunded) actuarial accrued liability as a percentage of covered payroll ((b - a) / c)
State:						
June 30, 1999	\$ 8,879,920,323	7,823,576,056	(1,056,344,267)	113.5%	\$ 2,928,470,790	(36.1)%
June 30, 2000	9,743,727,383	8,538,685,222	(1,205,042,161)	114.1	3,094,280,664	(38.9)
June 30, 2001	11,123,818,861	9,886,463,368	(1,237,355,493)	112.5	3,288,383,788	(37.6)
June 30, 2002	11,073,156,965	10,760,557,483	(312,599,482)	102.9	3,511,151,199	(8.9)
June 30, 2003	10,829,953,189	11,942,299,170	1,112,345,981	90.7	3,576,118,300	31.1
June 30, 2004	10,693,508,592	12,620,379,435	1,926,870,843	84.7	3,751,765,096	51.4
June 30, 2005	10,631,348,826	13,432,528,883	2,801,180,057	79.1	4,028,028,170	69.5
June 30, 2006	10,668,645,162	14,797,684,446	4,129,039,284	72.1	4,253,564,219	97.1
June 30, 2007	11,024,255,608	16,028,875,601	5,004,619,993	68.8	4,434,933,181	112.8
Local:						
June 30, 1999	\$ 13,171,311,650	11,163,283,877	(2,008,027,773)	118.0%	\$ 4,655,241,261	(43.1)%
June 30, 2000	14,380,511,913	12,007,160,806	(2,373,351,107)	119.8	4,910,962,708	(48.3)
June 30, 2001	16,625,288,260	13,819,038,491	(2,806,249,769)	120.3	5,240,338,738	(53.6)
June 30, 2002	16,503,081,054	14,929,334,103	(1,573,746,951)	110.5	5,534,322,805	(28.4)
June 30, 2003	16,406,284,200	15,887,012,746	(519,271,454)	103.3	5,811,726,702	(8.9)
June 30, 2004	16,414,022,003	17,077,938,057	663,916,054	96.1	6,140,413,756	10.8
June 30, 2005	16,482,040,944	18,341,857,304	1,859,816,360	89.9	6,416,265,644	29.0
June 30, 2006	16,699,827,172	20,273,979,840	3,574,152,668	82.4	6,730,309,209	53.1
June 30, 2007	17,690,520,507	21,764,214,593	4,073,694,086	81.3	6,983,534,635	58.3

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Required Supplementary Information

Schedule of Funding Progress – Additional Actuarial Information

(Unaudited - See accompanying independent auditors' report)

Significant actuarial methods and assumptions used in the most recent 2007 and 2006 actuarial valuations include the following:

	<u>June 30, 2007</u>	<u>June 30, 2006</u>
Actuarial cost method	Projected unit credit	Projected unit credit
Asset valuation method	5 year average of market value	5 year average of market value
Amortization method	Level percent, open	Level percent, open
Payroll growth rate for amortization	4.00%	4.00%
Remaining amortization period	30 years	30 years
Actuarial assumptions:		
Interest rate	8.25%	8.25%
Salary range	5.45%	5.45%
Cost-of-living adjustments	1.80%	1.80%

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

**STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Required Supplementary Information

Schedule of Employer Contributions

(Unaudited - See accompanying independent auditors' report)

<u>Year ended June 30,</u>		<u>Annual required contribution</u>	<u>Employer contributions⁽¹⁾⁽³⁾</u>	<u>Percentage contributed</u>
State:				
1999	\$	86,945,810	—	—%
2000		103,033,425	—	—
2001		85,078,620	—	—
2002		88,911,187	—	—
2003		44,636,619	—	—
2004		50,365,892	526,505 ⁽²⁾	1.0
2005		115,017,395	463,342 ⁽²⁾	0.4
2006		153,436,981	568,139 ⁽²⁾	0.4
2007		379,946,338	215,629,964	56.8
2008		530,531,787	206,828,570	39.0
Local:				
1999	\$	111,886,040	19,599,153	17.5%
2000		112,800,127	20,541,177	18.2
2001		88,717,727	21,670,774	24.4
2002		77,254,063	16,174,534	20.9
2003		—	16,987,033	N/A
2004		—	20,882,718	N/A
2005		29,425,853	56,916,883	193.4
2006		102,618,135	141,498,069	137.9
2007		382,344,230	242,230,174	63.4
2008		543,884,432	382,819,987	70.4

Notes to schedule:

(1) Excludes post-retirement medical contributions (State only) and contributions received from other State of New Jersey retirement systems for certain members who transferred their eligible prior service credit to the Public Employees' Retirement System. The local employer contributions from 1999 to 2004 consist of the required contributions under the early retirement incentive programs.

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

(2) The statutory required contributions which were reduced in anticipation of the provisions of the Appropriation Act of 2003 were covered by available excess assets in the Benefit Enhancement Fund. The amounts shown represented a fund transfer from the Second Injury Fund in accordance with Chapter 259, P.L. 2001.

(3) Differences between the amounts in the employer contribution column in this schedule and the amounts recorded in the financial statements and footnotes are attributed to timing differences between the 2007 actuarial valuations and the actual amounts received in fiscal year 2008. Employer contributions per this schedule represent anticipated contribution amounts determined at the time the actuarial valuations were prepared and finalized prior to the end of fiscal year 2008. The financial statements and footnotes reflect the actual amounts received in 2008.

STATE OF NEW JERSEY
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

Schedule of Changes in Fiduciary Net Assets by Fund

Year ended June 30, 2008

	Members' annuity savings and accumulative interest fund	Contingent reserve fund	Retirement reserve fund	Special reserve fund	Contributory group insurance premium fund	Benefit enhancement fund	Non-Contributory group insurance premium fund	Total
Additions:								
Contributions:								
Members	\$ 649,856,129	755,314,294	---	---	56,047,310	---	---	705,903,439
Employers	---	---	---	---	---	---	57,041,809	812,356,103
Total contributions	649,856,129	755,314,294	---	---	56,047,310	---	57,041,809	1,518,259,542
Distribution of net investment income (loss)	621,926,749	(2,539,295,103)	1,480,964,725	---	12,415,350	32,279,590	---	(391,708,689)
Total additions	1,271,782,878	(1,783,980,809)	1,480,964,725	---	68,462,660	32,279,590	57,041,809	1,126,550,853
Deductions:								
Benefit payments	---	---	2,023,571,985	---	47,463,907	---	78,345,180	2,149,381,072
Refunds of contributions	88,258,787	5,332,184	---	---	---	---	---	93,590,971
Administrative and miscellaneous expenses	---	21,669,271	---	---	---	---	---	21,669,271
Total deductions	88,258,787	27,001,455	2,023,571,985	---	47,463,907	---	78,345,180	2,264,641,314
Net increase (decrease) before transfers among reserves	1,183,524,091	(1,810,982,264)	(542,607,260)	---	20,998,753	32,279,590	(21,303,371)	(1,138,090,461)
Transfers among reserves:								
Retirements	(527,619,563)	(1,020,514,135)	1,548,133,698	---	---	---	---	---
Other	6,098,910	(203,017,303)	512,080,238	(261,992,402)	---	(53,169,443)	---	---
Net increase (decrease)	662,003,438	(3,034,513,702)	1,517,606,676	(261,992,402)	20,998,753	(20,889,853)	(21,303,371)	(1,138,090,461)
Net assets held in trust for pension benefits:								
Beginning of year	8,530,151,309	1,467,366,773	17,419,836,954	261,992,402	262,851,256	444,437,196	(11,589,626)	28,375,046,264
End of year	\$ 9,192,154,747	(1,567,146,929)	18,937,443,630	---	283,850,009	423,547,343	(32,892,997)	27,236,955,803