

STATE OF NEW JERSEY
TEACHERS' PENSION AND
ANNUITY FUND



1988
Annual Report

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**DEPARTMENT OF
THE TREASURY**

**DIVISION OF
PENSIONS**

FEATHER O'CONNOR
Treasurer

DOUGLAS R. FORRESTER
Director

**STATE OF NEW JERSEY
TEACHERS' PENSION AND ANNUITY FUND**

50 West State Street
Trenton, New Jersey 08625

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To His Excellency
Thomas H. Kean
Governor of the State of New Jersey

Dear Sir:

The board of trustees of the Teachers' Pension and Annuity Fund is pleased to present the Sixty-Ninth Annual Report in compliance with the provisions of N.J.S.A. 18A:66-59.

Respectfully submitted,

DOLORES MARSH,
Chairperson

Annual Report

Chapter 247, Laws of 1987, permits TPAF members to purchase service credit for previous service rendered in schools operated within the United States by the United States government for the instruction of children of the employees of the United States government. Previously, only credit for such service rendered outside of the United States was eligible for purchase by TPAF members. This law was approved and became effective on August 25, 1987.

Chapter 385, Laws of 1987, provides that pension adjustment benefits and the health care benefits for qualified retirees under the provisions of Chapter 384, Laws of 1987, shall be paid by the TPAF out of the contingent reserve fund and shall be funded in a manner similar to that provided for the funding of employer obligations for retirement benefits. It provides for a redetermination of the unfunded accrued liability of the fund as of March 31, 1987, and for a new schedule for accrued liability contributions. The new schedule will begin with July 1, 1987, and will run for a period determined by the State Treasurer with the advice of the Director of the Division of Pensions but not exceeding a period of 40 years. This law was approved on January 8, 1988, to become effective on June 1, 1988.

Chapter 446, Laws of 1987, guarantees that TPAF members and/or their beneficiaries will receive in benefits an amount equal to at least the member's accumulated personal contributions to the TPAF plus the regular interest that was computed at the time of the member's retirement. If the total amount of benefits paid to a retirant who does not elect an optional settlement or to both the retirant and his or her beneficiary under an optional settlement is less than the amount of the member's accumulated personal contributions plus the regular interest computed at the time of his or her retirement, the balance shall be paid in a lump sum to the member's designated beneficiary or to the member's estate if such funds cannot be paid to a designated beneficiary. This law was approved and became effective on January 19, 1988.

MEMBERSHIP

A summary of the membership activity for the fiscal year ended June 30, 1988, follows:

- 6,350—enrollments
- 2,069—retirements
- 1,877—active accounts terminated through separation from employment
- 160—deaths before retirement.

Comparative data on membership for selected June 30 periods since 1919 follow:

<u>June 30</u>	<u>Active</u>	<u>Retirants and Beneficiaries</u>	<u>Total</u>
1920	6,092	581	6,673
1925	18,508	1,008	19,516
1930	25,550	1,347	26,897
1935	26,651	2,097	28,748
1940	29,328	2,557	31,885
1945	30,572	3,286	33,858
1950	32,082	4,211	36,923
1955	39,612	5,318	44,930
1960	57,515	8,083	65,598
1965	74,608	12,503	87,111
1970	98,558	14,532	113,090
1975	109,634	19,888	129,522
1980	111,987	24,839	136,826
1985	109,153	29,021	138,174
1987	102,430	30,961	133,391
1988	114,087	31,942	146,029

**Retirements by Type and Option
July 1, 1987—June 30, 1988**

<u>Service</u>	<u>Early</u>	<u>Deferred</u>	<u>Ordinary Disability</u>	<u>Accidental Disability</u>	<u>Veteran</u>	<u>Accidental Death</u>
853	384	135	89	4	75	0
	<u>Maximum</u>	<u>Option I</u>	<u>Option II</u>	<u>Option III</u>	<u>Option IV</u>	
	882	330	176	130	22	

Standard Retirement Payroll, June 30, 1988

Regular Allowances—31,942 retirees and beneficiaries	\$21,971,244
Pension Adjustment Act—	7,183,492
Gross Payroll, month of June 1987	\$29,154,763

Comparative data on the standard retirement payroll for selected June 30 periods follow:

<u>June 30</u>	<u>Number</u>	<u>Payroll</u>
1920	581	\$ 409,605
1930	1,347	1,497,161
1940	2,557	3,385,468
1950	4,211	6,089,106
1955	5,318	8,599,206
1960	8,083	17,867,652*
1965	12,503	35,779,826
1970	14,538	48,953,885*
1975	19,888	93,546,957*
1980	24,839	169,018,512*
1985	29,021	269,257,406*
1987	30,961	315,503,804*
1988	31,942	341,404,852*

*Includes benefits paid under the provisions of the Pension Adjustment Act.

Group Life Insurance Claims: (Cash Basis)

ACTIVE MEMBERS

<u>Number</u>	<u>Settlement</u>	<u>Amount</u>
156	Cash Lump Sum	\$17,975,077
3	Reserve—Monthly Annuities	326,253
159	Total active member death claims	\$18,301,330

RETIRED MEMBERS

1,078	Regular Retirants (Death after age 60)— Lump Sum	\$ 6,017,169
23	Disability Retirants (Death before age 60)— Lump Sum	1,037,861
1,101	Total death claims—retirants	\$ 7,055,030
1,260	Total claims—active and retired members	<u>\$25,356,360</u>

Summary of Claim Charges (Cash Basis)

NONCONTRIBUTORY PLAN:

Active Members	159	\$ 8,100,258	
Retirees	<u>1,101</u>	<u>4,055,928</u>	\$12,156,186

CONTRIBUTORY PLAN:

Active Members	151	\$10,201,072	
Retirees	<u>717</u>	<u>2,999,102</u>	<u>13,200,174</u>
			<u>\$25,356,360</u>

Return of Contributions:

a) 1,877 members withdrew from the fund and received a return of their pension contributions with interest totaling		\$5,997,691
b) The survivors of 160 members, who died before retirement, received a return of the member's contribution with interest totaling		3,190,297
c) Settlement of expired accounts		<u>295,320</u>
Total		\$9,483,308

Loans:

24,128 members applied for and received loans on their accounts totaling \$71,732,740.

UNCLAIMED ACCOUNTS

Unclaimed accounts, June 30, 1987		\$2,031,901
Memberships discontinued and not settled during 1987-88	401	
Memberships discontinued and settled in 1986-87	<u>32,073</u>	
Added in fiscal year		<u>32,474</u>
		\$2,064,375

Less:

Cash settlements during fiscal year	\$295,320	
Cash escheat to State Treasurer	483,222	
Transferred to new accounts	<u>11,154</u>	<u>789,696</u>
BALANCE, JUNE 30, 1988		<u>\$1,274,679</u>

Lists of the new additions during 1987-88 have been sent to all employing units with a request that they circulate copies among their memberships in an effort to ascertain the whereabouts of the listed former members and advise the Division of Pensions.

Ernst & Whinney

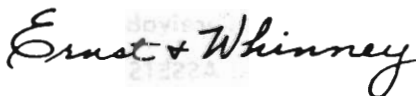
Suite 200
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Princeton, New Jersey 08540
609/243-0303

Board of Trustees
State of New Jersey
Teachers' Pension and Annuity Fund

We have audited the accompanying component unit financial statements of the State of New Jersey Teachers' Pension and Annuity Fund as of June 30, 1988 and 1987. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the component unit financial statements referred to above present fairly, in all material respects, the financial position of the State of New Jersey Teachers' Pension and Annuity Fund at June 30, 1988 and 1987, and the results of its operations and changes in its financial position for the years then ended in conformity with generally accepted accounting principles.



Princeton, New Jersey
October 28, 1988

**STATE OF NEW JERSEY
 TEACHERS' PENSION AND ANNUITY FUND**

June 30,
1988 1987

ASSETS

Investments, at cost:

Bonds (market value of \$223,721,338 in 1988 and \$290,278,891 in 1987)	\$ 242,115,938	\$ 318,790,164
Common Pension Fund A (market value of \$3,917,534,107 in 1988 and \$4,383,464,727 in 1987)	3,081,636,953	2,719,701,263
Common Pension Fund B (market value of \$2,901,307,710 in 1988 and \$2,494,195,157 in 1987)	2,906,164,056	2,449,785,848
Cash Management Fund (market value of \$257,210,611 in 1988 and \$153,128,400 in 1987)	257,210,611	153,128,400
Mortgages (market value of \$1,031,726,438 in 1988 and \$891,849,642 in 1987)	<u>1,047,842,080</u>	<u>915,518,862</u>
Total Investments	<u>7,534,969,638</u>	<u>6,556,924,537</u>

Receivables:

Contributions:		
Members	38,417,245	34,179,000
Employers	108,468	132,849
Investments:		
Accrued interest	83,170,776	73,023,211
Dividends	28,138,798	25,329,253
Members' loans	116,166,466	115,183,148
Due from Pension Adjustment Fund	0	6,725,800
Other	<u>19,545,124</u>	<u>10,359,862</u>
Total Receivables	<u>285,546,877</u>	<u>264,933,123</u>
TOTAL ASSETS	<u><u>\$7,820,516,515</u></u>	<u><u>\$6,821,857,660</u></u>

June 30,
1988 1987

LIABILITIES AND FUND BALANCES

Liabilities:

Retirement benefits payable	\$	29,594,520	\$	26,605,673
Death benefits payable		1,380,471		3,027,450
Cash overdraft		4,757,854		3,636,377
Payable for investments purchased		64,505,639		0
Accounts payable and accrued expenses		3,620,480		1,027,119
Due to general fund		118,792,559		0
Total Liabilities		222,651,523		34,296,619

Fund Balances:

Members' annuity savings fund and accumulative interest		1,595,151,563		1,448,688,767
Contingent reserve fund		2,271,076,205		3,095,578,322
Retirement reserve fund		3,610,097,599		2,131,945,998
Special reserve fund		74,932,725		65,229,124
Contributory group insurance premium fund		46,606,900		46,118,830
Other fund		0		0
Total Fund Balances		7,597,864,992		6,787,561,041

**TOTAL LIABILITIES AND
 FUND BALANCES**

\$7,820,516,515	\$6,821,857,660
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See notes to financial statements.

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN FUND BALANCES

**STATE OF NEW JERSEY
TEACHERS' PENSION AND ANNUITY FUND**

	Fund Balances						Totals	
	Members' Annuity Savings Fund and Accumulative Interest	Contingent Reserve Fund	Retirement Reserve Fund	Special Reserve Fund	Contributory Group Insurance Premium Fund	Other Fund	Year Ended June 30, 1988	1987
REVENUES								
Contributions:								
Members	\$ 135,126,715				\$12,514,807		\$ 147,641,522	\$ 138,442,900
Employers		\$ 359,773,275					359,773,275	321,560,276
Investment revenue	84,588,024	406,981,773	\$ 221,694,196	\$ 9,703,601	3,100,245		726,067,839	721,155,281
Pension Adjustment Fund							0	84,566,784
Other						\$486,873	486,873	460,477
TOTAL REVENUES	<u>219,714,739</u>	<u>766,755,048</u>	<u>221,694,196</u>	<u>9,703,601</u>	<u>15,615,052</u>	<u>486,873</u>	<u>1,233,969,509</u>	<u>1,266,185,718</u>
EXPENSES								
Benefit payments			263,410,016				263,410,016	238,230,268
Withdrawals	9,210,015						9,210,015	11,198,343
Noncontributory group insurance death benefits		14,723,615					14,723,615	11,745,440
Pension Adjustment Fund			113,798,325				113,798,325	24,013,503
Other		7,300,296			15,126,982	96,309	22,523,587	18,366,082
TOTAL EXPENSES	<u>9,210,015</u>	<u>22,023,911</u>	<u>377,208,341</u>	<u>0</u>	<u>15,126,982</u>	<u>96,309</u>	<u>423,665,558</u>	<u>364,353,726</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES	210,504,724	744,731,137	(155,514,145)	9,703,601	488,070	390,564	810,303,951	901,831,992

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN FUND BALANCES—Continued

STATE OF NEW JERSEY
TEACHERS' PENSION AND ANNUITY FUND

	Fund Balances						Totals	
	Members' Annuity Savings Fund and Accumulative Interest	Contingent Reserve Fund	Retirement Reserve Fund	Special Reserve Fund	Contributory Group Insurance Premium Fund	Other Fund	Year Ended 1988	June 30, 1987
	Transfers between funds:							
Retirements	(64,084,901)	(291,592,863)	355,677,764				0	0
Other	42,973	(1,277,640,391)	1,277,987,982			(390,564)	0	0
Fund balances at beginning of year	1,448,688,767	3,095,578,322	2,131,945,998	65,229,124	46,118,830	0	6,787,561,041	5,885,729,049
FUND BALANCES AT END OF YEAR	<u>\$1,595,151,563</u>	<u>\$2,271,076,205</u>	<u>\$3,610,097,599</u>	<u>\$74,932,725</u>	<u>\$46,606,900</u>	<u>\$ 0</u>	<u>\$7,597,864,992</u>	<u>\$6,787,561,041</u>

See notes to financial statements.

**STATE OF NEW JERSEY
 TEACHERS' PENSION AND ANNUITY FUND**

	Year Ended June 30,	
	1988	1987
	<hr/>	<hr/>
SOURCES OF FINANCIAL RESOURCES		
Excess of revenues over expenses	\$ 810,303,951	\$ 901,831,992
Items not requiring (providing) financial resources:		
Accretion and amortization—net	(3,395,108)	(3,229,916)
Net (gain) loss on sales and maturities of long-term investments	16,643,407	8,148,518
Net realized gain on Common Pension Funds A and B	(254,869,924)	(270,671,812)
	<hr/>	<hr/>
	568,682,326	619,781,746
Proceeds from sales and maturities of long-term investments	669,544,163	670,439,614
Decrease (increase) in Cash Management Fund	(104,082,211)	76,835,607
Decrease (increase) in members' loans	(983,318)	6,910,736
Decrease (increase) in other receivables	(2,459,462)	4,552,476
Increase (decrease) in death benefits payable	(1,646,979)	2,499,428
Increase in retirement benefits payable	2,988,847	1,735,394
Increase in payable for investments purchased	64,505,639	0
Increase in due to general fund	118,792,559	0
	<hr/>	<hr/>
TOTAL SOURCES OF FINANCIAL RESOURCES	1,315,341,564	1,382,755,001
USES OF FINANCIAL RESOURCES		
Purchases of long-term investments	1,301,885,428	1,358,473,385
Increase in contribution receivables	4,213,864	6,258,553
Increase in accrued investment income	12,951,110	11,616,573
Decrease (increase) in accounts payable and accrued expenses	(2,593,361)	1,275,301
	<hr/>	<hr/>
TOTAL USES OF FINANCIAL RESOURCES	1,316,463,041	1,377,623,812
	<hr/>	<hr/>

INCREASE (DECREASE) IN CASH	(1,121,477)	5,131,189
CASH OVERDRAFT, beginning of year	(3,636,377)	(8,767,566)
CASH OVERDRAFT, end of year	<u>(\$ 4,757,854)</u>	<u>(3,636,377)</u>

See notes to financial statements.

**STATE OF NEW JERSEY
TEACHERS' PENSION AND ANNUITY FUND**

June 30, 1988

NOTE A—SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Teachers' Pension and Annuity Fund (Fund) are prepared on the accrual basis of accounting and conform to generally accepted accounting principles.

Financial statement footnote disclosures are in accordance with Statement Number 5 of the Governmental Accounting Standards Board, "Disclosure of Pension Information by Public Employee Retirement Systems and State and Local Governmental Employers."

Valuation of Investments: Bonds with fixed maturities are reported at cost adjusted for amortization of premium or accretion of discounts on the straight-line basis for securities which mature within one year and the effective interest rate method for other securities.

Investments in the Common Pension Funds, commingled funds in which the State of New Jersey Pension Trust Funds are the sole participants, are valued at cost, plus undistributed net realized gains. At June 30, 1988, such undistributed net realized gains amounted to \$223,899,389; consisting of \$223,614,720 in Common Pension Fund A and \$284,669 in Common Pension Fund B.

Investments in the Cash Management Fund are stated at a cost of \$1.00 per unit, which approximates quoted market.

Mortgages are valued at the amount of unpaid principal balance of the loan, adjusted for accretion of discounts which are amortized over the life of the loans.

Purchases and sales of investments are reflected on a trade date basis. Realized gains and losses on sales of investments are determined by the average cost basis and recognized as investment income when the sale occurs. Interest and dividend income on investments is recognized when earned.

Administrative Expenses: The Fund is administered by the State of New Jersey Division of Pensions. All administrative expenses are allocated to the State who is responsible for such cost. The Fund's assets available for paying benefits are not reduced for administrative expenses.

**STATE OF NEW JERSEY
TEACHERS' PENSION AND ANNUITY FUND**

NOTE B—DESCRIPTION OF THE SYSTEM

Organization: The Fund is a single-employer contributory defined benefit plan which was established as of January 1, 1955, under the provisions of N.J.S.A. 18A:66. The Fund is considered a component unit of the State of New Jersey and is included along with other State-administered pension trust funds in the general purpose financial statements of the State.

The Fund's designated purpose is to provide retirement benefits and other benefits to members. Membership in the Fund is mandatory for substantially all teachers or members of the professional staff certified by the State Board of Examiners and employees of the Department of Education that have titles that are unclassified, professional and certified. The Fund's Board of Trustees is responsible for its organization and administration.

Membership in the Fund as of March 31, 1987, the date of the most recent actuarial valuation, was as follows:

Retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits but not yet receiving them	<u>33,079</u>
Active members:	
Vested	69,956
Nonvested	<u>39,312</u>
TOTAL	<u>109,268</u>

Loans Receivable: The Fund provides for member loans up to 50% of their accumulated member contributions. To obtain a loan, a member must have three years of contributions to the members' annuity savings account. Repayment of loan balances is deducted from payroll checks and bears an annual interest rate of 4%. Benefit payments are utilized to repay any outstanding loan balance upon retirement, termination, or death.

Vesting and Benefit Provisions: The vesting and benefit provisions are set by N.J.S.A. 18A:6c. The System provides retirement as well as death and disability benefits. All benefits vest after 10 years of service. Retirement benefits for age and service are available at age 60 and are generally determined to be 1/60 of final average salary for each year of service credit. Final average salary equals the average salary

**STATE OF NEW JERSEY
TEACHERS' PENSION AND ANNUITY FUND**

NOTE B—DESCRIPTION OF THE FUND—Continued

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 or they may elect deferred retirement after achieving 10 years of service 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 3 years of service credit becomes vested for 2% of related interest on the contributions. In the case of death before retirement, members' beneficiaries are entitled to full interest credited to the members' accounts.

Other: According to the retirement code, all obligations of the Fund will be assumed by the State should the Fund terminate.

Information about the agreement, including vesting and benefit provisions is contained in the pamphlet "Teachers' Retirement in New Jersey." Copies of this pamphlet are available from the State of New Jersey Division of Pensions.

NOTE C—PENSION BENEFIT OBLIGATION

The following "pension benefit obligation" is the actuarial present value of credited projected benefits. It is a standardized disclosure measure representing the present value of pension benefits adjusted for the effects of projected salary increases estimated to be payable in the future based on employee service credit to date. This measure is independent of the actuarial funding method used to determine employer contributions to the system discussed in Note D.

The pension benefit obligation was determined as part of the annual actuarial valuation dated March 31, 1987. The liability was determined as of March 31 and projected forward to June 30, 1987 allowing for increases in benefits and variations in the population during the three month period.

**STATE OF NEW JERSEY
 TEACHERS' PENSION AND ANNUITY FUND**

NOTE C—PENSION BENEFIT OBLIGATION—Continued

The projected pension benefit obligation as of June 30, 1987 was:

Pension benefit obligations:	
Retirees and beneficiaries currently receiving benefits and terminated employees not yet receiving benefits	\$ 3,406,530,000
Current employees:	
Accumulated employees contributions with interest	1,448,690,000
Employer-financed vested	5,180,980,000
Employer-financed nonvested	486,330,000
	<hr/>
Total pension benefit obligation, including cost-of-living adjustments	<u>\$10,522,530,000</u>
Net assets (fund balance) available for benefits at book value (market value of \$8,800,522,855)	<u>\$ 7,144,923,671</u>
Unfunded pension benefit obligation	<u>\$ 3,377,606,329¹</u>

¹In addition, based on current legislation described below, the actuarially determined unfunded obligation for post-retirement medical premiums was \$2,306,400,000 as of June 30, 1987.

The above pension benefit obligation was calculated based on the actuarial assumptions of a) rate of return on investments of 7¼% compounded annually as compared to 7½% used in the prior year valuation; b) salary increases ranging from 6.58% at age 25 to 2.35% at age 70 which includes inflation, merit and productivity; c) assets valued at cost or amortized cost; and d) 3% increase in benefit provisions and e) mortality, vesting, retirement and withdrawal estimates based on tables furnished by the actuary. The pension benefit obligation decreased by \$406,300,000 due to this change in the actuarial assumptions.

Legislation enacted during the current year required cost-of-living adjustments and health care benefits for retirees to be determined actuarially, as of March 31, 1987, and required the resulting liability to be funded within 40 years. Previously, the State (General Fund) contributed the cost-of-living benefits to the Fund monthly and paid post-retirement medical premiums annually from the Health Benefits Program, both on

**STATE OF NEW JERSEY
TEACHERS' PENSION AND ANNUITY FUND**

NOTE C—PENSION BENEFIT OBLIGATION—Continued

a pay-as-you-go basis. As a result of these amendments, the 1987 actuarially determined contribution by the State was increased by \$168,963,000 based on a funding period of 33 years, commencing with the fiscal 1989 payment, due July 1, 1988. As a result of actuarially funding the cost-of-living benefits, the pension benefit obligation increased \$2,674,400,000 as of June 30, 1987.

In accordance with the March 31, 1987 actuarial valuation and the legislation, the State Treasurer mandated that the fund begin payment of these benefits as of June 1, 1988 and assume the obligation for cost-of-living benefits from April 1, 1987. As a result, the Fund will reimburse the State (General Fund) for the cost-of-living benefits for the period April 1, 1987 to May 31, 1988 in the amount of \$111,586,431, which includes interest at $6\frac{7}{8}\%$. This obligation is shown in the Fund's balance sheet as "Due to the General Fund" at June 30, 1988.

NOTE D—CONTRIBUTION POLICY

The contribution policy is set by N.J.S.A. 18A:66 and requires contributions by active members and the State. Member contribution rates range from 5.05% to 9.09% of salary based on the members' age at date of enrollment. Once members are assigned a rate, it is not normally adjusted.

In accordance with the provisions of Chapter 385, P.L. 1987, contributions of the State consist of a normal contribution and an accrued liability contribution as determined by a qualified actuary. The current year State contributions are based on the 1986 actuarial valuation. The normal contribution includes an amount that is reported to fund noncontributory death benefits.

The Fund's actuary uses the "projected benefit method" to determine normal costs. Beginning in the 1989 plan year, the State will be required to make contributions for qualified retirees towards the payment of cost-of-living adjustments and the costs for medical premiums after retirement. The accrued liability was revalued as of March 31, 1987 by resetting the normal contribution at the entry age level. The revalued unfunded accrued liability for basic allowances as of March 31, 1987, the date of the most recent actuarial valuation, was \$1,071,091,511. This amount is to be funded over a 33-year period commencing July

NOTES TO FINANCIAL STATEMENTS—Continued

**STATE OF NEW JERSEY
TEACHERS' PENSION AND ANNUITY FUND**

NOTE D—CONTRIBUTION POLICY—Continued

1, 1988. Additional accrued liabilities were determined for cost-of-living adjustments and the post retirement medical premiums for qualified retirees in the amount of \$8,510,042,281 and these amounts will be funded over a 33-year period commencing July 1, 1988. For current active members, additional normal contributions will be made for these benefits. The additional normal rates will be recognized over a 30-year period.

Total contributions for the year ended June 30, 1988 were \$494,899,990 (\$359,773,275 from the State and \$135,126,715 from members, or 11.10% and 4.17%, respectively, of annual covered compensation) of which \$331,534,040 represented the recommended normal contribution amount and \$25,435,494 related to the accrued liability funding.

The annual interest assumption used for valuing the Fund was increased to 6 $\frac{7}{8}$ % in 1987 from 6 $\frac{1}{2}$ % in 1986. This rate differs from that used to compute the standardized measure of the pension benefit obligation discussed in Note C above which was 7 $\frac{1}{4}$ % in 1987 and 7 $\frac{1}{2}$ % in 1986. Other significant assumptions were the same.

The effect on fiscal 1989 contributions due to the changes in actuarial assumptions and benefits funding will be a decrease of \$79,000,000 and an increase of \$168,963,000, respectively (see Note C).

NOTE E—DESCRIPTION OF FUND BALANCES

Members' Annuity Savings Fund and Accumulative Interest:

The Members' Annuity Savings Fund and accumulative interest (ASF) is credited with all contributions made by active members of the Fund. Interest is applied to members' individual accounts at an annual rate established by the State Treasurer which was 6 $\frac{1}{2}$ % for the years ended June 30, 1988 and 1987. After three years of participation, withdrawing members receive interest at an annual rate of 2% of their accumulative contributions with the remaining portion of interest forfeited.

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

STATE OF NEW JERSEY
TEACHERS' PENSION AND ANNUITY FUND

NOTE E—DESCRIPTION OF FUND BALANCES—Continued

Upon death or withdrawal from active service before qualifying for retirement, accumulated contributions plus applicable interest are paid from the Members' Annuity Savings Fund.

Contingent Reserve Fund: The Contingent Reserve Fund is credited with the contributions of the State and other employees. Additionally, interest earnings of the Fund, after crediting the ASF and the Retirement Reserve Fund, as required, are credited to this account.

Upon retirement of a member, the employer contributions necessary to produce the balance of the retirement reserve, are transferred to the Retirement Reserve Fund for subsequent benefit payments.

Each year, the amounts necessary as determined by the actuary for the payment of retirement benefits are transferred from the Contingent Reserve Fund to the Retirement Reserve Fund. In addition, payments for the group insurance made by The Prudential Insurance Company of America to provide noncontributory cash death benefits are made from the Contingent Reserve Fund.

Chapter 385 P.L. 1987 provides that pension adjustment (cost-of-living) benefits and the health care benefits for qualified retirees under Chapter 384 P.L. 1987 shall be paid from the Contingent Reserve Fund.

Retirement Reserve Fund: The Retirement Reserve Fund is the account from which all retirement benefits are paid. Upon retirement of a member, accumulated contributions, together with accumulated regular interest, are transferred to the Retirement Reserve Fund from the ASF. Any reserves needed for the additional retirement benefits are transferred from the Contingent Reserve Fund. Annually, interest as determined by the State Treasurer (6½% in 1988 and 1987) is credited to the Retirement Reserve Fund. Any surplus or deficit developing in the Retirement Reserve Fund shall be adjusted from time to time by transfers to or from the Contingent Reserve Fund upon advice of the actuary. During 1988, a transfer amounting to \$1,274,700,000 was made from the Contingent Reserve Fund to the Retirement Reserve Fund primarily due to the cost-of-living adjustment amendments discussed in Note C.

Special Reserve Fund: The Special Reserve Fund is the fund to which excess interest earnings and net realized gains or losses from the sale of securities are transferred. The maximum limit on the accumulation

**STATE OF NEW JERSEY
 TEACHERS' PENSION AND ANNUITY FUND**

NOTE E—DESCRIPTION OF FUND BALANCES—Continued

of this account is 1% of the book value of the investments of the Fund. Amounts in excess of 1% are credited to the Contingent Reserve Fund, excluding investments allocated to the Contributory Group Insurance Premium Fund which was \$41,697,099 in the Cash Management Fund at June 30, 1988.

Contributory Group Insurance Premium Fund: The Contributory Group Insurance Premium Fund represents the accumulation of member 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 this first year of membership and may cancel the contributory coverage thereafter. The current contribution rate for this coverage is 4/10 of 1% of salary.

NOTE F—INVESTMENTS

The State of New Jersey Division of Investments under the jurisdiction of the State Investment Council, has the investment responsibility for all funds administered by the State of New Jersey Division of Pensions. All investments must conform to standards set by State law.

A summary of investment securities as of June 30, 1988 and the approximate market values follows:

	<u>Amortized Cost</u>	<u>Market Value</u>
	(In 000's)	
Bonds:		
U.S. and municipal government bonds	\$ 24,843	\$ 24,680
Industrial bonds	28,409	26,736
Telephone bonds	35,906	32,313
Gas, electric, and water bonds	116,276	104,849
Finance companies—senior debt	6,998	6,816
Railroad equipment obligations	1,470	1,402
Other	<u>28,214</u>	<u>26,925</u>
	242,116	223,721

NOTES TO FINANCIAL STATEMENTS—Continued

**STATE OF NEW JERSEY
TEACHERS' PENSION AND ANNUITY FUND**

NOTE F—INVESTMENTS—Continued

Mortgages	1,047,842	1,031,726
Common Pension Fund A	3,081,637	3,917,534
Common Pension Fund B	2,906,164	2,901,308
State of New Jersey Cash Management Fund	257,211	257,211
TOTAL	<u>\$7,534,970</u>	<u>\$8,331,500</u>

Investments in excess of 5% of net assets are:

	June 30	
	<u>1988</u>	<u>1987</u>
	(In 000's)	
Common Pension Fund A	\$3,081,637	\$2,719,701
Common Pension Fund B	2,906,164	2,449,786

NOTE G—INCOME TAX STATUS

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

NOTE H—HISTORICAL TREND INFORMATION

Historical trend information designed to provide information about the System's progress made in accumulating sufficient assets to pay benefits when due is presented on pages 29 and 30.

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ACTUARIAL EVALUATION

The information given below is taken from the valuation of March 31, 1987, showing the system's contributions (assets) and present and contingent benefits (liabilities) as of that date.

ASSETS

Present assets of fund creditable to:

Retirement Reserve Fund:

Credited to fund	\$2,028,057,744	
Add accrued interest creditable	94,592,047	
Add reserve transferable from Contingent Reserve Fund	<u>1,274,702,023</u>	
Total		\$ 3,397,351,814

Pension Fund:

Credited to fund	\$ 1,994,921	
Add accrued interest creditable	<u>111,067</u>	
Add reserve transferable from Contingent Reserve Fund	4,031,918	
Total		6,137,906

Annuity Savings Fund:

Credited to fund	\$1,342,605,408	
Add accrued interest creditable	<u>58,857,841</u>	
Total		1,401,463,249

Contingent Reserve Fund:

Credited to fund	\$2,624,422,773	
Add accrued interest creditable	123,302,817	
Add excess interest earnings creditable	263,823,687	
Deduct reserve transferable to Retirement Reserve Fund	<u>1,274,702</u>	
Deduct reserve transferable to Pension Fund	4,031,918	
Total		\$ 1,732,815,336

Special Reserve Fund:

Credited to fund	\$ 275,408,432	
Add accrued interest creditable	<u>52,274,503</u>	
Deduct excess interest earnings transferable	263,823,687	
Contributory Group Insurance Premium Fund	47,047,895	

Total Present Assets

\$ 6,648,675,4-

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Present value of prospective contributions to members to be made to Annuity Savings Fund	\$ 1,271,997,738	
Present value of prospective contributions of members to be made to Annuity Savings Fund		\$ 1,271,997,738
Present value of prospective contributions to the Pension Fund and the Contingent Reserve Fund including payments due July 1, 1987:		
Normal contributions		
Basic allowances with cost-of-living adjustments	\$5,470,265,735	
Accrued liability contributions		
Basic allowances with cost-of-living adjustments	2,446,130,229	7,916,395,964
Present value of prospective contributions to the Post Retirement Medical Fund:		
Normal contributions	\$3,800,909,520	
Accrued liability contributions	541,187,355	4,342,096,875
Total Prospective Assets		\$13,530,490,577
TOTAL ASSETS		\$20,179,166,025
LIABILITIES		
Present value of benefits payable on account of beneficiaries now drawing allowances from the Retirement Reserve Fund:		
Service and early service benefits	\$3,222,686,221	
Disability benefits	104,117,195	
Benefits to dependent beneficiaries	70,548,398	\$ 3,397,351,814
Present value of benefits payable on account of beneficiaries now drawing allowances from the Pension Fund:		
Service and early service benefits	\$ 5,725,507	
Disability benefits	21,517	
Benefits to dependent beneficiaries	390,882	6,137,906
Present value of benefits to be paid by contributions to the Annuity Savings Fund and the Contingent Reserve Fund:		
Service retirement allowances including early retirement and vesting of benefits	\$8,698,345,291	
Ordinary disability retirement allowances	179,754,717	

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Accidental disability retirement allowances	14,915,560	
Ordinary death benefits	432,696,444	
Accidental death benefits	5,973,831	
Return of members' contributions upon withdrawal before retirement	<u>236,910,478</u>	\$12,286,531,535
Cost-of-Living Adjustments	2,817,935,214	
Present value of medical premiums to be paid by contributions to the Post Retirement Medical Fund	4,342,096,875	
Group insurance benefits to be paid from Contributory Group Insurance Premium Fund	47,047,895	
TOTAL LIABILITIES		<u>\$20,179,166,025</u>

LEVEL OF FUNDING

With respect to the funding of the system, the following is an excerpt from page 34 of the actuarial valuation as of March 31, 1987.

In conjunction with the current valuation, the level of funding of the fund as measured by the ratio of valuation assets to projected accrued liabilities under the traditional approach is:

A. Projected Accrued Liabilities	\$12,967,470,000
B. Valuation Assets	\$ 6,648,675,448
C. Funding Level B ÷ A	51.3%

The projected accrued liabilities are calculated using the valuation interest rate (6⁷/₈ percent) and salary scales. Valuation assets are based on book value as reported in the Fund's financial statements. The calculations are made as of the valuation date (March 31).

The retirement system believes that misleading inferences concerning the system's funding status may result from a comparison of the actuarial present value of accumulated system's benefits with the fair value of net assets available for system benefits. This is because the system's assets have been accumulated by making contributions equal to the current year's costs determined on an ongoing basis, while the determination of the actuarial present value of accumulated system benefits required by FASB #35 and 36 has been made using methods and assumptions which are not the same as those used to determine the pension costs for the current year. For example, the required method for determining the actuarial present value of accumulated system benefits fails to take into consideration future wage and salary increases which have been considered by the Actuary and the retirement system in determining the costs of the system. Furthermore, the fair value of net assets for system benefits will fluctuate, which may create erroneous impressions with respect to the long term progress on funding the retirement system. The retirement system is concerned that, from an ongoing perspective, the financial statements pursuant to FASB #35 and 36 materially overstate the funded status of the system and can lead employers, on one hand, to believe that a cutback in appropriation for funding may be proper, while likewise leading employee organizations to recommend benefit liberalizations to be financed as a result of what appears to be a near-surplus financial position.

CONTRIBUTORY INSURANCE

The board of trustees is authorized by law to purchase a group life insurance policy to provide for the benefits which are to be met by contributions by members. The statute requires the board to establish rates so that the contributions made by or on behalf of all covered members in the aggregate shall be sufficient to provide for the cost of the benefits payable to eligible active and retired members.

In the administration of the program certain accounts derived from employee contributions have been left on deposit with the carrier for specific reasons. A brief description of each deposit account is noted below:

1. **Dividend Accumulation**—This is an account established by the board of trustees, as policyholder, into which dividends arising from the active life experience are deposited. Such funds could be used to forestall rate increases and used to reduce rates.

2. **Special Reserve**—This money is used to stabilize experience.

3. **Insurance Continuance Fund**—*This money is to prefund the cost of insurance on retired lives. Any dividends arising from the retired life experience are deposited here.

4. **Advance Premium**—Returned premiums are deposited in this account when the Special Reserve contains funds in excess of its contractual limit. Such money could be used to delimit rate increases or reduce rates.

The Dividend Accumulation and the Advance Premium Accounts earned interest at the rate of 10.0 percent per annum during the policy year.

FUNDS ON DEPOSIT

	Balance <u>6/30/88</u>	Balance <u>6/30/87</u>
Dividend Accumulation	\$3,732,326	\$4,328,056
Special Reserve	—	—
Insurance Continuance	0	0
Advance Premium	0	5,816,097

**REPORT OF INDEPENDENT AUDITORS ON
REQUIRED SUPPLEMENTARY INFORMATION**

Board of Trustees
State of New Jersey
Teachers' Pension and Annuity Fund

The analysis of funding progress and revenues by source and expenses by type of the State of New Jersey Teachers' Pension and Annuity Fund are not required parts of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Ernst & Whinney

October 28, 1988

**REQUIRED SUPPLEMENTARY INFORMATION
ANALYSIS OF FUNDING PROGRESS**

(In Millions)

**STATE OF NEW JERSEY
TEACHERS' PENSION AND ANNUITY FUND**

Information from the most recent actuarial valuation for the fiscal year end:

Fiscal Year	(1)	(2)	(3)	(4)	(5)	(6)
	Net Assets Available For Benefits	Pension Benefit Obligation	Percentage Funded (1) ÷ (2)	Unfunded Pension Benefit Obligation (2) - (1)	Annual Covered Payroll	Unfunded Pension Obligation As A Percentage Of Covered Payroll (4) ÷ (5)
1986	\$5,003.3	\$ 5,174.8	97.3%	\$ 141.5	\$2,763.9	5.1%
1987	5,840.4	6,831.0	85.5%	990.6	3,011.7	32.8%
1988	7,144.9	10,522.5	67.9%	3,377.6	3,241.9	104.2%

Analysis of the dollar amounts of net assets available for benefits, pension benefit obligation, and unfunded pension benefit obligation in isolation can be misleading. Expressing the net assets available for benefits as a percentage of the pension benefit obligation provides one indication of the Fund's funding status on a going-concern basis. Analysis of this percentage over time indicates whether the Fund is becoming financially stronger or weaker. Generally, the greater this percentage, the stronger the Fund. Trends in unfunded pension benefit obligation and annual covered payroll are both affected by inflation. Expressing the unfunded pension benefit obligation as a percentage of annual covered payroll approximately adjusts for the effects of inflation and aids analysis of the Fund's progress made in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the stronger the Fund.

Information for the seven years prior to the year ended June 30, 1986 is unavailable.

**REQUIRED SUPPLEMENTARY INFORMATION
REVENUES BY SOURCE AND EXPENSES BY TYPE**

**STATE OF NEW JERSEY
TEACHERS' PENSION AND ANNUITY FUND**

Plan Fiscal Year	REVENUES BY SOURCE				
	Member Contributions	Employer Contributions	Percentage Of Annual Covered Compensation	Investment Income	Total
1979	\$ 69,387,194	\$142,226,397	8.13%	\$162,264,924	\$ 373,878,515
1980	70,291,610	155,713,024	8.39	192,891,718	418,896,352
1981	76,059,228	151,175,004	7.68	229,950,979	457,185,211
1982	79,281,519	205,247,825	9.76	285,534,902	570,064,246
1983	85,755,631	235,805,262	10.52	299,442,076	621,002,969
1984	91,170,531	253,395,280	10.54	346,760,249	691,326,060
1985	98,561,518	280,652,017	10.97	397,087,025	776,300,560
1986	110,656,183	299,499,600	10.84	466,831,691	876,987,474
1987	126,885,089	321,560,276	10.68	716,836,949	1,165,282,314
1988	135,126,715	359,773,275	11.10	722,967,594	1,217,867,584

Plan Fiscal Year	EXPENSES BY TYPE				
	Benefits		Withdrawals	Transfers To Other Retirement Systems	Total
Retirement	Other				
1979	\$121,637,418	\$ 41,619	\$10,154,872	\$232,803	\$132,066,712
1980	130,249,617	0	12,285,753	152,986	142,688,356
1981	140,422,656	0	12,490,103	109,987	153,022,746
1982	152,207,949	0	11,819,619	730,413	164,757,981
1983	162,925,554	0	9,440,484	81,261	172,447,299
1984	178,051,923	8,525,832	10,376,442	82,792	197,036,989
1985	196,536,957	12,850,904	10,710,202	44,005	220,142,068
1986	215,594,634	11,742,508	10,345,403	56,592	237,739,137
1987	238,359,609	11,745,440	10,539,838	658,505	261,303,392
1988	265,731,642	14,723,615	8,523,828	686,187	289,665,272

Contributions were made in accordance with actuarially determined contribution requirements.

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Teachers' Pension and Annuity Fund

State of New Jersey

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