

PUBLIC EMPLOYEES'
RETIREMENT SYSTEM
OF
NEW JERSEY



1987
Annual Report

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**DEPARTMENT OF
THE TREASURY**

FEATHER O'CONNOR
Treasurer

**DIVISION OF
PENSIONS**

DOUGLAS R. FORRESTER
Director

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

20 West Front Street
Trenton, New Jersey 08625

BOARD

ANGELINA SICONOLFI, Chairperson
THOMAS P. BRYAN, State Treasurer Representative
SUZANNA BURIANI-DeSANTIS
JAMES H. BIGGS
JOSEPH W. STAUSS
WILLIAM P. GERVASI
CANDACE L. STRAIGHT
NORMA SAWYER
VINCENT J. McKENNA (Deceased)

JANICE F. NELSON, Secretary

GEORGE B. BUCK
Consulting Actuaries, Inc.

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WILLIAM COLEMAN, M.D.
MURRAY SHEPP, M.D.
DAVID ECKSTEIN, M.D.

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

Dear Sir:

The board of trustees of the Public Employees' Retirement System is pleased to present the Thirty-Third Annual Report in compliance with the provisions of N.J.S.A. 43:15A-21.

Respectfully submitted,

ANGELINA SICONOLFI,
Chairperson

Annual Report

Chapter 188, Laws of 1986 permits Section 414(h) treatment of employees' contributions to the major state-administered retirement systems. This means that such contributions are exempt from federal income tax until withdrawn or utilized in the payment of retirement benefits. This law was approved on December 16, 1986 to become effective on January 1, 1987.

Chapter 51, Laws of 1986 permits members of the Public Employees' Retirement System who became injured while voluntarily performing their regular or assigned duties at their place of employment before or after their scheduled work hours to qualify for accidental disability retirement benefits. This law was approved and became effective July 16, 1986.

Chapter 109, Laws of 1986 prohibits a temporary employee who is employed under the Federal Job Training Partnership Act from joining the retirement system. Furthermore, this law required that any temporary employee who is employed under that federal act and enrolled in the Public Employees' Retirement System on or before September 19, 1986, to have such membership terminated. The members received a refund of the contributions made since being employed under the act. The payment of such accumulated deductions acted as a waiver of any future benefits payable to the employee or his or her beneficiaries from the retirement system. This law was approved and became effective September 19, 1986.

Chapter 139, Laws of 1986 changes the minimum annual salary requirement for enrollment eligibility within the retirement system from the previous \$500 per year to \$1,500 per year. However, any person who was enrolled in the system before the effective date of this law and is being paid between \$500 and \$1,500 per year continued such membership if they informed the Division of Pensions in writing of such intentions by May 5, 1987. This law was approved and became effective November 6, 1987.

Chapter 1, Laws of 1987 provides that members of the retirement system who continue to be employed beyond age 70 will continue to have full life insurance coverage. This law mandates that these members will continue to pay the premiums for their contributory life insurance. In addition, this law provides the opportunity for members of the system to convert their life insurance upon retirement provided that the retiree pays the total cost for such coverage. This law was approved on January 16, 1987 but the over-age-70 continued coverage was retroactive to October 1, 1985.

As a result of the annual election, Regine Brown, Suzanna M.F. Buriani-DeSantis and Gary Saage were elected to three-year terms commencing July 1, 1987. Angelina Siconolfi was re-elected chairperson by the Board effective July 1, 1987.

MEMBERSHIP

A summary of the membership activity for the fiscal year ended June 30, 1987, follows:

36,998—enrollments
 5,069—retirements
 21,465—active accounts terminated through
 separation from employment
 776—deaths before retirement

Comparative data on membership for selected June 30 periods since 1955 follow:

<u>June 30</u>	<u>Active</u>	<u>Retirants and Beneficiaries</u>	<u>Total</u>
1955	34,087	2,649	36,736
1960	50,576	7,116	57,692
1965	68,086	10,445	78,531
1970	113,866	13,298	127,164
1975	171,518	21,682	193,200
1980	205,038	35,185	240,223
1985	236,060	50,939	286,999
1987	218,615	57,092	275,707

Retirements by Type and Option July 1, 1986—June 30, 1987

<u>Service</u>	<u>Early</u>	<u>Deferred</u>	<u>Accidental Disability</u>	<u>Ordinary Disability</u>	<u>Veteran</u>	<u>Accidental Death</u>
2,801	232	202	14	184	1,080	3
	<u>Maximum</u>	<u>Option I</u>	<u>Option II</u>	<u>Option III</u>	<u>Option IV</u>	
	2,395	1,140	620	335	23	

Standard Retirement Payroll June 30, 1987

Regular Allowance—57,092 retirants and beneficiaries

Pension Adjustment Act—

Gross Payroll, month of June 1987 \$ 22,625,101

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

<u>June 30</u>	<u>Number</u>	<u>Payroll</u>
1955	2,649	\$ 2,848,923*
1960	7,116	8,876,808*
1965	10,445	16,737,419*
1970	13,298	24,036,226*
1975	21,682	53,518,488*
1980	35,185	144,408,900*
1985	50,939	213,581,142*
1987	57,092	260,460,447*

*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>
694	Cash Lump Sum Reserve	\$36,771,740
4	Monthly Annuities	141,807
	Total active member death claims	
698		\$36,913,547

Retired Members

1,590	Regular Retirants (Death after age 60)—Lump Sum	\$ 3,890,945
29	Disability Retirants (Death before age 60)—Lump Sum	663,940
1,619	Total death claims—retirants	\$ 4,554,885
2,317	Total claims—active and retired members	<u>\$41,468,432</u>

SUMMARY OF CLAIM CHARGES (CASH BASIS)

Noncontributory Plan:

Active Members	698	\$18,954,584
Retirants	<u>1,619</u>	<u>4,554,885</u>
	2,317	\$23,509,469

Contributory Plan:

Active Members	<u>\$17,958,963</u>	<u>\$41,468,432</u>
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Return of Contributions (Cash Basis):

a) 21,465 members withdrew from the system and received a return of the pension contributions totaling	\$32,222,911
b) The survivors of 776 members who died before retirement received a return of the members' contributions totaling	\$ 6,595,893
c) Settlement of inactive accounts	<u>177,404</u>
	38,996,208

Loans:

42,883 members applied for and received loans on their accounts totaling \$71,374,060.

UNCLAIMED ACCOUNTS

Unclaimed accounts, June 30, 1986	\$2,083,956
Memberships discontinued and not settled during 1986-87	\$979,685
Memberships discontinued and settled in 1986-87	<u>145,660</u>
Added in fiscal year 1986-87	<u>1,125,345</u>
	3,209,301
Less:	
Cash settlements during fiscal year	\$174,282
Cash escheat to State Treasurer	0
Transferred to new accounts	<u>66,148</u>
	<u>240,430</u>
BALANCE, JUNE 30, 1987	<u>\$2,968,571</u>

Lists of the new additions during 1986-87 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.

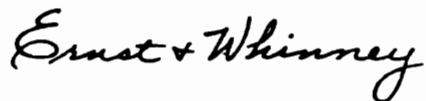
Ernst & Whinney

3131 Princeton Pike
Lawrenceville, New Jersey 08648
609/896-3223

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

We have examined the balance sheets of the State of New Jersey Public Employees' Retirement System as of June 30, 1987 and 1986, and the related statements of revenues, expenses, and changes in fund balances and of changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of the State of New Jersey Public Employees' Retirement System at June 30, 1987 and 1986, and the results of operations and the changes in financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

A handwritten signature in cursive script that reads "Ernst & Whinney". The signature is written in dark ink and is positioned to the right of the main body of text.

Lawrenceville, New Jersey
November 9, 1987

BALANCE SHEET

STATE OF NEW JERSEY PUBLIC EMPLOYEES' RETIREMENT SYSTEM

	June 30,	
	1987	1986
ASSETS		
Investments at cost:		
Bonds (market value of \$161,247,457 in 1987 and \$214,159,007 in 1986)	\$ 175,525,939	\$ 236,873,361
Common Pension Fund A (market value of \$3,565,226,021 in 1987 and \$2,758,855,448 in 1986)	2,198,363,695	1,784,839,817
Common Pension Fund B (market value of \$2,310,541,269 in 1987 and \$2,167,960,699 in 1986)	2,221,577,885	1,959,716,425
Cash Management Fund (market value of \$198,626,165 in 1987 and \$120,252,658 in 1986)	198,626,165	120,252,658
Mortgages (market value of \$705,444,269 in 1987 and \$638,666,269 in 1986)	721,368,751	623,622,207
Total Investments	5,515,462,435	4,725,304,468
Receivables:		
Contributions:		
Members	37,138,287	33,847,796
Employers	108,135,289	122,382,090
Investments:		
Accrued interest	64,689,161	57,629,347
Dividends	20,593,740	18,770,429
Members' loans	99,594,006	100,196,169
Due from Pension Adjustment Fund	4,111,291	3,737,321
Other	1,499,355	7,260,742
Total Receivables	335,761,129	343,823,894
Cash	9,799,771	0
TOTAL ASSETS	\$5,861,023,335	\$5,069,128,362

	June 30,	
	1987	1986
LIABILITIES AND FUND BALANCES		
Liabilities:		
Retirement benefits payable	\$ 22,595,449	\$ 20,628,414
Death benefits payable	2,533,458	1,918,367
Cash overdraft	0	5,078,484
Accounts payable and accrued expenses	12,648,648	11,251,454
Total Liabilities	37,777,555	38,876,719
Fund Balances:		
Members' annuity savings fund and accumulative interest	1,440,319,050	1,295,060,376
Contingent reserve fund	2,384,942,253	1,959,452,380
Retirement reserve fund	1,907,372,343	1,696,652,943
Special reserve fund	54,816,127	46,974,028
Contributory group insurance premium reserve fund	35,796,007	32,111,916
Other fund	0	0
Total Fund Balances	5,823,245,780	5,030,251,643
TOTAL LIABILITIES AND FUND BALANCES	\$5,861,023,335	\$5,069,128,362

See notes to financial statements.

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN FUND BALANCES

STATE OF NEW JERSEY PUBLIC EMPLOYEES' RETIREMENT SYSTEM

	Fund Balances						Totals	
	Members' Annuity Savings Fund and Accumulative Interest	Contingent Reserve Fund	Retirement Reserve Fund	Special Reserve Fund	Contributory Group Insurance Premium Reserve Fund	Other Fund		
							Year Ended June 30, 1987	1986
REVENUES								
Contributions:								
Members	\$ 182,131,022				\$22,905,893	\$ 110,385	\$ 205,147,300	\$ 184,511,198
Employers		\$ 296,480,787					296,480,787	277,292,387
Investment revenue	75,734,945	194,973,207	\$ 111,498,154	\$236,839,294	3,014,929		622,060,529	413,674,435
Pension Adjustment Fund						51,660,869	51,660,869	49,708,338
Other			218,514			170,020	388,534	510,682
TOTAL REVENUES	257,865,967	491,453,994	111,716,668	236,839,294	25,920,822	51,941,274	1,175,738,019	925,697,040
EXPENSES								
Benefit payments			216,983,863				216,983,863	196,568,346
Withdrawals	29,767,617						29,767,617	30,182,733
Noncontributory group insurance death benefits		26,348,897					26,348,897	28,946,313
Pension Adjustment Fund						51,878,180	51,878,180	49,780,719
Transfers to other funds	12,871,376	21,453,917					34,325,293	4,085,312
Other			205,379		22,236,731	997,922	23,440,032	15,793,964
TOTAL EXPENSES	42,638,993	47,802,814	217,189,242	0	22,236,731	52,876,102	382,743,882	325,357,387
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES	215,226,974	443,651,180	(105,472,574)	236,839,294	3,684,091	(934,828)	792,994,137	600,339,653

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

STATE OF NEW JERSEY PUBLIC EMPLOYEES' RETIREMENT SYSTEM

	Fund Balances						Totals	
	Members' Annuity Savings Fund and Accumulative Interest	Contingent Reserve Fund	Retirement Reserve Fund	Special Reserve Fund	Contributory Group Insurance Premium Reserve Fund	Other Fund	Year Ended 1987	June 30, 1986
Transfers between reserves for:								
Retirements by members	(69,207,429)	(229,296,313)	298,503,742				0	0
Other	(760,871)	211,135,006	17,688,232	(228,997,195)		934,828	0	0
FUND BALANCES AT BEGINNING OF YEAR	<u>1,295,060,376</u>	<u>1,959,452,380</u>	<u>1,696,652,943</u>	<u>46,974,028</u>	<u>32,111,916</u>	<u>0</u>	<u>5,030,251,643</u>	<u>4,429,911,990</u>
FUND BALANCES AT END OF YEAR	<u>\$1,440,319,050</u>	<u>\$2,384,942,253</u>	<u>\$1,907,372,343</u>	<u>\$ 54,816,127</u>	<u>\$35,796,007</u>	<u>\$ 0</u>	<u>\$5,823,245,780</u>	<u>\$5,030,251,643</u>

See notes to financial statements.

STATEMENTS OF CHANGES IN FINANCIAL POSITION

STATE OF NEW JERSEY PUBLIC EMPLOYEES' RETIREMENT SYSTEM

	Year Ended June 30,	
	1987	1986
SOURCES OF FINANCIAL RESOURCES		
Excess of revenues over expenses	\$ 792,994,137	\$ 600,339,653
Items not requiring (providing) financial resources:		
Accretion and amortization—net	(2,901,543)	(2,606,564)
Net (gain) loss on sales and maturities of long-term investments	(18,068,522)	15,288,294
Net realized gain on Common Pension Funds A and B	(218,770,772)	(66,200,202)
	<u>553,253,300</u>	<u>546,821,181</u>
Proceeds from sales and maturities of long-term investments	525,974,764	493,125,936
Decrease in contributions receivable	10,956,310	6,909,929
Increase in retirement benefits payable	1,967,035	2,042,584
Decrease (increase) in other receivables	5,387,417	(2,931,769)
Decrease (increase) in member loans	602,163	(13,611,786)
Increase in death benefits payable	615,091	1,918,367
Increase in accounts payable and accrued expenses	1,397,194	1,832,604
Total sources of financial resources	<u>1,100,153,274</u>	<u>1,036,107,046</u>
USES OF FINANCIAL RESOURCES		
Purchases of long-term investments	998,018,387	1,102,356,860
Increase (decrease) in Cash Management Fund	78,373,507	(62,492,727)
Increase in accrued investment income	8,883,125	4,163,428
Total uses of financial resources	<u>1,085,275,019</u>	<u>1,044,027,561</u>
NET INCREASE (DECREASE) IN CASH	14,878,255	(7,920,515)
CASH (OVERDRAFT), beginning of year	(5,078,484)	2,842,031
CASH (OVERDRAFT), end of year	<u>\$ 9,799,771</u>	<u>(\$ 5,078,484)</u>

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

STATE OF NEW JERSEY PUBLIC EMPLOYEES' RETIREMENT SYSTEM

June 30, 1987

NOTE A—SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Public Employees' Retirement System (System) are prepared on the accrual basis of accounting and conform to generally accepted accounting principles.

Valuation of Investments: Bonds with fixed maturities are reported at cost as of the settlement date, 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 represent commingled funds in which the State of New Jersey Pension Trust Funds are the sole participants. These investments are valued at cost plus undistributed realized net gains of \$215,239,561; consisting of \$211,986,895 in Common Pension Fund A and \$3,252,666 in Common Pension Fund B at June 30, 1987.

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 in the Common Pension Funds are reflected on a trade date basis and on a settlement date basis for all other investments. Realized gains and losses on sales of investments are determined by the average cost basis and recognized as investment income when sale occurs. Interest and dividend income on investments is recognized when earned.

Administrative Expenses: The system is administered by the State of New Jersey Division of Pensions. All administrative expenses are allocated to the State and State-related (local governmental agencies) employers and they are responsible for such cost. The System's assets available for paying benefits are not reduced for administrative expenses.

NOTE B—DESCRIPTION OF THE FUND

Organization: The system is a contributory defined benefit plan which was established as of January 1, 1955, under the provision of

NOTES TO FINANCIAL STATEMENTS—Continued

N.J.S.A. 43:15A. The System's designated purpose is to provide retirement benefits and other benefits to its members. Membership in the system is mandatory for substantially all full-time employees of the State 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 or local jurisdiction. The System's Board of Trustees is responsible for its organization and administration.

Contributions: The contribution policy is set by N.J.S.A. 43:15A and requires contributions by active members, employers, and the State. Member contribution rates range from 4.96% to 9.91% 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 57, P.L. 1970, the contributions required of employers and the state are based upon an annual actuarial valuation, as a percentage of future compensation of members which will support the pension and death benefits payable by employers. For the year ended June 30, 1987, the amounts required from State-related employers ranged from 6.87% to 8.52% and State contributions ranged from 8.76% to 9.02% of active payroll. The State appropriation for the year ended June 30, 1987, paid July 1, 1986, is based on 1985 actuarial valuations and the State-related employer contributions are accrued on June 30, 1987, based on the most recent 1986 actuarial valuation.

The normal contribution includes an amount that is required to fund noncontributory death benefits.

Actuarial Valuation: The contribution policy requires State-related employers and the State to make a normal contribution and a past service contribution as determined by a qualified actuary. The System's actuary uses the "projected benefit method" to determine normal costs. As of March 31, 1986, the date of the most recent actuarial report, the actuary computed that, utilizing the present method of funding, the unfunded actuarial liability of the employers and the State for prior service was \$199,080,070. This amount is to be funded in approximately 26 years.

Significant assumptions underlying the actuarial computations include: (a) assumed rate of return on investments of 6-1/2%; (b) assumed rate of salary increases ranging from 8.39% at age 25 to 2.86% at age 69; (c) assets valued at cost or amortized cost; and (d) mortality, vesting, retirement age, and withdrawal estimates based on tables furnished by the actuary.

NOTES TO FINANCIAL STATEMENTS—Continued

No material actuarial assumptions were changed during the year.

Loans Receivable: The System provides for member loans up to 50% of their accumulated member contributions. To obtain a loan, a member must make three years of contributions to the member's 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.

Pension Adjustment Program: Pursuant to N.J.S.A. 43:3B in 1958, eligible retirants 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 percent factor as developed and results in the dollar amount of the adjustment payable. Retired members become eligible for pension adjustment benefits after 24 months of retirement. These cost-of-living increases are not payable by the System. The cost-of-living increases are made from the State of New Jersey Pension Adjustment Fund which is funded on a "pay as you go" basis by State appropriation.

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

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

NOTE C—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 System. Interest is applied to members' individual accounts at an annual rate established by the State Treasurer which was 6-1/2% for the years ended June 30, 1987 and 1986. After three years of participation, withdrawing members receive interest at an annual rate of 2% of their accumulative contribution 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 benefit payments.

NOTES TO FINANCIAL STATEMENTS—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 employers. Additionally interest earnings, 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.

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 additional reserves needed for the retirement benefits are transferred from the Contingent Reserve Fund. Annually, interest as determined by the State Treasurer (6.5% for 1987 and 1986) 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.

Special Reserve Fund: The Special Reserve Fund is the fund to which any excess interest earnings and gains from sale and maturity of investments are transferred and against which any losses from the sale of securities are charged. The maximum limit on the accumulation of this account is 1% of the book value of the investments allocated to the System, excluding cash management fund investments allocated to the Contributory Group Insurance Premium Fund which amounted to \$33,849,748 at June 30, 1987. Amounts in excess of 1% are credited to the Contingent Reserve Fund.

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.

NOTES TO FINANCIAL STATEMENTS—Continued

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 6/10 of 1% of salary.

NOTE D—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, 1987 and the approximate market values follows:

	<u>Book Value</u>	<u>Market Value</u>
	(in 000's)	
Bonds:		
U.S. and Municipal		
Government bonds	\$ 5,877	\$ 5,811
Industrial bonds	45,885	41,914
Telephone bonds	27,976	24,981
Gas, electric, and		
water bonds	69,547	63,532
Finance companies—		
senior debt	4,691	4,490
Railroad equipment		
obligations	734	706
Other	20,816	19,814
Subtotal	<u>175,526</u>	<u>161,248</u>
Mortgages	721,369	705,444
Common Pension Fund A	2,198,364	3,565,226
Common Pension Fund B	2,221,578	2,310,541
State of New Jersey Cash		
Management Fund	<u>198,626</u>	<u>198,626</u>
TOTAL	<u><u>\$5,515,463</u></u>	<u><u>\$6,941,085</u></u>

NOTES TO FINANCIAL STATEMENTS—Continued

NOTE D—INVESTMENTS—Continued

A State law enacted on August 27, 1985 requires the Division of Investments to divest of all securities or other obligations of any company engaged in business in or with the Republic of South Africa by August 27, 1988. At June 30, 1987, the System is a 35% and 37% participant in the two State Common Pension Funds with applicable investments aggregating a cost of \$600 million and \$250 million, respectively. At June 30, 1986, the System had comparable participation in the two Common Pension Funds and was also a participant in the State of New Jersey Cash Management Fund with applicable investments aggregating a cost of \$1.5 billion, \$696 million, and \$326 million, respectively. The market value of these investments at June 30, 1987 and 1986 equals or exceeds the applicable cost basis.

NOTE E—INCOME TAX STATUS

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

NOTE F—SUBSEQUENT EVENT

At June 30, 1987, the Fund had approximately \$1,366,862,000 of net unrealized appreciation (market value in excess of carrying value) on its share of equity securities in Common Pension Fund A. During October 1987, the stock market experienced unprecedented volatility and decline in value. As of October 31, 1987, the net unrealized appreciation on the Fund's share of equity securities that were in Common Pension Fund A at June 30, 1987 decreased to \$638,103,000. The effect on the market value of the remaining securities held at June 30, 1987 was immaterial.

Retirement benefits payable to plan participants are set by state formulas which are not affected by the market value of pension fund assets. Furthermore, management believes the current decline in the market value will not have an adverse effect on future contributions as actuarial valuations are based on the carrying value of investments.

ACTUARIAL EVALUATION

The information given below is taken from the valuation of March 31, 1986, showing the system's contributions (assets) and present and contingent benefits (liabilities) as of that date.

ASSETS

Present assets of system creditable to:

Retirement Reserve Fund:

Credited to fund	\$1,584,841,871	
Add accrued interest creditable	74,777,905	
Add reserve transferable from		
Contingent Reserve Fund	18,908,652	\$1,678,528,428

Annuity Savings Fund:

Credited to fund	\$1,198,940,463	
Add accrued interest creditable	44,582,341	1,243,522,804

Contingent Reserve Fund:

Credited to fund	\$1,644,812,801	
Add accrued interest creditable	75,091,520	
Add excess interest earnings		
creditable	54,769,358	
Deduct reserve transferable		
to Retirement Reserve Fund	18,908,652	1,936,465,330
Realized gains or losses	180,700,303	

Special Reserve Fund:

Credited to fund	\$ 22,119,098	
Add excess interest earnings		
creditable	21,829,358	43,948,456
Total Present Assets		\$4,902,465,018

Present value of prospective contributions of members to be made to Annuity Savings Fund

\$1,511,712,040

Present value of prospective contributions payable by the state and local employers to the Contingent Reserve Fund as follows:

Future normal contributions	2,910,819,951	
Future accrued		
liability contributions	199,080,070	
Total Prospective Assets		4,621,612,061

TOTAL ASSETS

\$9,524,077,079

LIABILITIES

Present value of benefits payable on account of beneficiaries or their dependents now drawing allowance from the Retirement Reserve Fund			\$1,678,528,428
Present value of benefits payable from contributions to the Annuity Savings Fund and the Contingent Reserve Funds:			
Service retirement allowance including early retirement and vesting benefits	\$6,175,652,140		
Ordinary disability retirement allowances	319,940,794		
Accidental disability retirement allowances	80,854,458		
Ordinary death benefits	703,658,830		
Accidental death benefits	7,574,951		
Return of members' contributions upon withdrawal before retirement	557,867,478	7,845,548,651	
<u>TOTAL LIABILITIES</u>			<u><u>\$9,524,077,079</u></u>

LEVEL OF FUNDING

With respect to the funding of the system, the following is an excerpt from page 31 of the actuarial valuation as of March 31, 1986.

In conjunction with the current valuation, the level of funding of the system, as measured by the ratio of valuation assets to projected liabilities, has been determined under the traditional approach to be:

	<u>State</u>	<u>Local Employers</u>
A. Projected Accrued Liabilities	\$2,294,010,000	\$3,326,118,000
B. Valuation Assets	1,808,981,912	3,093,483,106
C. Funding Level		
B ÷ A	78.9%	93.0%

The projected accrued liabilities are calculated using the valuation interest rate 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 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 of contributions for the purpose of maintaining the Contributory Group Insurance Premium Fund at a level sufficient to meet the obligations of the fund for the cost of insurance.

In the administration of the program certain amounts 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. **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.

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

The Dividend Accumulation account earned interest at the rate of 10.0 percent during the policy year. The Special Reserve earned interest at the rate of 10.0 percent for the portion of the reserve held on July 1, 1982 and interest at the rate of 11.0 percent on the balance.

FUNDS ON DEPOSIT

	Balance 6/30/87	Balance 6/30/86
Dividend Accumulation	\$ 0	\$3,133,094
Advance Premium	0	294,833
Special Reserve	691,766	983,757

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