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STATE OF NEW JERSEY
TEACHERS' PENSION AND
ANNUITY FUND



1987
Annual Report

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**DEPARTMENT OF
THE TREASURY**

FEATHER O'CONNOR
Treasurer

**DIVISION OF
PENSIONS**

DOUGLAS R. FORRESTER
Director

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

20 West Front Street
Trenton, New Jersey 08625

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MURRAY SHEPP, M.D.

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-Eighth Annual Report in compliance with the provisions of N.J.S.A. 18A:66-59.

Respectfully submitted,

DOLORES MARSH,

Chairperson

**Addendum
Teachers' Pension and Annuity
Fund
1987 Annual Report**

After this annual report went to press, it was noted that the total number of active members in the pension fund was incorrect (see page 4).

The correct number of **active** members, as of June 30, 1987, was **111,846** (not 102,430). This increased the **total** membership to **142,807** (not 133,391).

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 This means that such contributions are exempt from federal income tax until withdrawn or utilized in the payment of retirement benefits.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 22, Laws of 1987 eliminates the full time requirement for enrollment eligibility for teachers in the Teachers' Pension and Annuity Fund. This law was approved and became effective June 3, 1986.

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 97, Laws of 1987 changes the calculation from average of the three highest years of salary to the last year's salary for qualified military veterans members of the Teachers' Pension and Annuity Fund who have attained age 60 with at least 35 years of accrued aggregate creditable service. This law was approved and became effective on April 14, 1987.

MEMBERSHIP

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

7,656—enrollments
1,944—retirements
3,710—active accounts terminated through
separation from employment
175—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

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

<u>Service</u>	<u>Early</u>	<u>Deferred</u>	<u>Ordinary Disability</u>	<u>Accidental Disability</u>	<u>Veteran</u>	<u>Accidental Death</u>
791	357	134	70	3	180	0
	<u>Maximum</u>	<u>Option I</u>	<u>Option II</u>	<u>Option III</u>	<u>Option IV</u>	
	845	323	207	137	23	

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Standard Retirement Payroll, June 30, 1987

Regular Allowances—30,961 retirants and beneficiaries	\$19,496,310
Pension Adjustment Act—	7,107,548
Gross Payroll, month of June 1987	\$26,603,858

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*

*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>
162	Cash Lump Sum	\$17,132,742
0	Reserve—Monthly Annuities	0
162	Total active member death claims	\$17,132,742

RETIRED MEMBERS

912	Regular Retirants (Death after age 60)— Lump Sum	\$ 5,338,760
16	Disability Retirants (Death before age 60)— Lump Sum	594,548
928	Total death claims—retirants	\$ 5,933,308
1090	Total claims—active and retired members	\$23,066,050

Summary of Claim Charges (Cash Basis)

NONCONTRIBUTORY PLAN:

Active Members	162	\$7,598,213	
Retirants	928	<u>3,223,259</u>	\$10,821,472

CONTRIBUTORY PLAN:

Active Members	151	\$ 9,534,529	
Retirants	<u>643</u>	<u>2,710,049</u>	<u>12,244,578</u>
			\$23,066,050

Return of Contributions:

a) 3,710 members withdrew from the fund and received a return of their pension contributions with interest totaling	\$6,577,333
b) The survivors of 175 members, who died before retirement, received a return of the member's contribution with interest totaling	3,144,393
c) Settlement of expired accounts	<u>231,205</u>
Total	\$9,952,931

Loans:

22,191 members applied for and received loans on their accounts totaling \$65,858,550.

UNCLAIMED ACCOUNTS

Unclaimed accounts, June 30, 1986	\$1,357,021
Memberships discontinued and not settled during 1986-87	\$834,698
Memberships discontinued and settled in 1986-87	<u>246,818</u>
Added in fiscal year	<u>1,081,516</u>
	\$2,438,537

Less:

Cash settlements during fiscal year	\$231,205
Cash escheat to State Treasurer	0
Transferred to new accounts	<u>175,431</u>
BALANCE, JUNE 30, 1987	\$2,031,901

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
Teachers' Pension and Annuity Fund

We have examined the balance sheet of the State of New Jersey Teachers' Pension and Annuity Fund 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 examination was 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 Teachers' Pension and Annuity Fund 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.

Ernst & Whinney

Lawrenceville, New Jersey
November 9, 1987

BALANCE SHEET

STATE OF NEW JERSEY TEACHERS' PENSION AND ANNUITY FUND

	June 30,	
	1987	1986
ASSETS		
Investments, at cost:		
Bonds (market value of \$290,278,891 in 1987 and \$420,779,971 in 1986)	\$ 318,790,164	\$ 473,676,934
Common Pension Fund A (market value of \$4,383,464,727 in 1987 and \$3,364,320,066 in 1986)	2,719,701,263	2,180,568,787
Common Pension Fund B (market value of \$2,494,195,157 in 1987 and \$2,272,145,367 in 1986)	2,449,785,848	2,098,438,199
Cash Management Fund (market value of \$153,128,400 in 1987 and \$229,964,007 in 1986)	153,128,400	229,964,007
Mortgages (market value of \$891,849,642 in 1987 and \$694,898,364 in 1986)	915,518,862	681,028,200
Total Investments	6,556,924,537	5,663,676,127
Receivables:		
Contributions:		
Members	34,179,000	27,936,667
Employers	132,849	116,629
Investments:		
Accrued interest	73,023,211	63,875,023
Dividends	25,329,253	22,860,868
Members' loans	115,183,148	122,093,884
Due from Pension Adjustment Fund	6,725,800	6,385,283
Other	10,359,862	15,252,855
Total Receivables	264,933,123	258,521,209
TOTAL ASSETS	\$6,821,857,660	\$5,922,197,336

June 30,
1987 1986

LIABILITIES AND FUND BALANCES

Liabilities:

Retirement benefits payable	\$ 26,605,673	\$ 24,870,279
Death benefits payable	3,027,450	528,022
Cash overdraft	3,636,377	8,767,566
Accounts payable and accrued expenses	1,027,119	2,302,420
Total Liabilities	34,296,619	36,468,287

Fund Balances:

Members' annuity savings fund and accumulative interest	1,448,688,767	1,309,879,299
Contingent reserve fund	3,095,578,322	2,594,575,391
Retirement reserve fund	2,131,945,998	1,877,546,038
Special reserve fund	65,229,124	56,313,917
Contributory group insurance premium fund	46,118,830	47,414,404
Other fund	0	0
Total Fund Balances	6,787,561,041	5,885,729,049

TOTAL LIABILITIES AND FUND BALANCES

\$6,821,857,660	\$5,922,197,336
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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, 1987	1986
REVENUES								
Contributions:								
Members	\$ 126,885,089				\$11,541,768	\$ 16,043	\$ 138,442,900	\$ 121,267,549
Employers		\$ 321,389,604	\$ 170,672				321,560,276	299,499,600
Investment revenue	78,477,121	233,268,679	126,270,819	\$278,820,330	4,318,332		721,155,281	470,317,749
Pension Adjustment Fund						84,566,784	84,566,784	83,440,047
Other			210,189			250,288	460,477	583,222
TOTAL REVENUES	<u>205,362,210</u>	<u>554,658,283</u>	<u>126,651,680</u>	<u>278,820,330</u>	<u>15,860,100</u>	<u>84,833,115</u>	<u>1,266,185,718</u>	<u>975,108,167</u>
EXPENSES								
Benefit payments			238,230,268				238,230,268	215,598,008
Withdrawals	11,198,343						11,198,343	11,872,745
Noncontributory group insurance death benefits		11,745,440					11,745,440	11,742,508
Pension Adjustment Fund						84,813,593	84,813,593	83,570,725
Other	0	129,341	198,991	0	17,155,674	882,076	18,366,082	10,506,939
TOTAL EXPENSES	<u>11,198,343</u>	<u>11,874,781</u>	<u>238,429,259</u>	<u>0</u>	<u>17,155,674</u>	<u>85,695,669</u>	<u>364,353,726</u>	<u>333,290,925</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES	194,163,867	542,783,502	(111,777,579)	278,820,330	(1,295,574)	(862,554)	901,831,992	641,817,242

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 June 30, 1987	Year Ended June 30, 1986
Transfers between funds:								
Retirements	(54,521,506)	(247,257,592)	301,779,098	0	0	0	0	0
Other	(832,893)	205,477,021	64,398,441	(269,905,123)	0	862,554	0	0
Fund balances at beginning of year	1,309,879,299	2,594,575,391	1,877,546,038	56,313,917	47,414,404	0	5,885,729,049	5,243,911,807
FUND BALANCES AT END 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

See notes to financial statements.

STATEMENT OF CHANGES IN FINANCIAL POSITION

STATE OF NEW JERSEY TEACHERS' PENSION AND ANNUITY FUND

	Year Ended June 30,	
	1987	1986
SOURCES OF FINANCIAL RESOURCES		
Excess of revenues over expenses	\$ 901,831,992	\$ 641,817,242
Items not requiring (providing) financial resources:		
Accretion and amortization—net	(3,229,916)	(2,848,700)
Net (gain) loss on sales and maturities of long-term investments	(8,148,518)	30,174,174
Net realized gain on Common Pension Funds A and B	(270,671,812)	(79,951,952)
	<u>619,781,746</u>	<u>589,190,764</u>
Proceeds from sales and maturities of long-term investments	670,439,614	617,162,474
Decrease in Cash Management Fund	76,835,607	130,306,127
Decrease (increase) in members' loans	6,910,736	(12,128,822)
Decrease (increase) in other receivables	4,552,476	(2,587,972)
Increase (decrease) in death benefits payable	2,499,428	(184,568)
Increase in retirement benefits payable	<u>1,735,394</u>	<u>2,059,986</u>
TOTAL SOURCES OF FINANCIAL RESOURCES	1,382,755,001	1,323,817,989
USES OF FINANCIAL RESOURCES		
Purchases of long-term investments	1,358,473,385	1,326,467,648
Increase in contribution receivables	6,258,553	684,208
Increase in accrued investment income	11,616,573	5,382,190
Decrease (increase) in accounts payable and accrued expenses	<u>1,275,301</u>	<u>(1,708,879)</u>
TOTAL USES OF FINANCIAL RESOURCES	<u>1,377,623,812</u>	<u>1,330,825,167</u>
INCREASE (DECREASE) IN CASH	5,131,189	(7,007,178)
CASH OVERDRAFT, beginning of year	(8,767,566)	(1,760,388)
CASH OVERDRAFT, end of year	<u>(\$ 3,636,377)</u>	<u>(\$ 8,767,566)</u>

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

STATE OF NEW JERSEY TEACHERS' PENSION AND ANNUITY FUND

June 30, 1987

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.

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, 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, 1987, such undistributed net realized gains amounted to \$264,150,241; consisting of \$260,639,036 in Common Pension Fund A and \$3,511,205 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 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 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.

NOTES TO FINANCIAL STATEMENTS—Continued

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

NOTE B—DESCRIPTION OF THE FUND

Organization: The Fund is a contributory defined benefit plan which was established as of January 1, 1955, under the provisions of N.J.S.A. 18A:66. 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.

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

In accordance with the provisions of Chapter 121, P.L. 1971, contributions of the State consist of a normal contribution and an accrued liability contribution. The State pays over a period of 40 years commencing with July 1, 1971 to liquidate the unfunded liability accrued on the basis of services rendered prior to July 1, 1970 by all members, except veterans who were employed as teachers on January 1, 1955. In addition, an annual contribution, payable over a thirty-year period, is to be made by each employer, having teachers on January 1, 1955 who were veterans, to liquidate the unfunded liability accrued on the basis of services rendered prior to January 1, 1955 which was satisfied in 1987.

The normal contribution is based upon an annual actuarial valuation computed as a percentage of the total compensation of all active members. The normal contribution rate for the year ended June 30, 1987 (payable July 1, 1986) is 11.43% based upon the March 31, 1985 actuarial valuation which is comparable to the prior-year rate of 11.39%. The normal contribution includes an amount that is required to fund noncontributory death benefits.

Actuarial Valuation: The contribution policy requires the State to make a normal contribution and a past service contribution as determined by a qualified actuary. The Fund'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, utilizing the present method of funding, the unfunded actuarial liability of the State for prior service to be \$328,127,733. This amount is to be funded in approximately 23 years.

NOTES TO FINANCIAL STATEMENTS—Continued

STATE OF NEW JERSEY TEACHERS' PENSION AND ANNUITY FUND

NOTE B—DESCRIPTION OF THE FUND—Continued

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 6.58% at age 25 to 2.35% at age 70; (c) assets valued at cost or amortized cost; and (d) mortality, vesting, retirement age, and withdrawal estimates based on tables furnished by the actuary.

No material actuarial assumptions were changed during the year.

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.

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 Fund. The cost-of-living increases are funded 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 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.

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

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 Fund. 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, 1986 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.

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

NOTES TO FINANCIAL STATEMENTS—Continued

STATE OF NEW JERSEY TEACHERS' PENSION AND ANNUITY FUND

NOTE C—DESCRIPTION OF FUND BALANCES—Continued

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 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 \$34,012,125 in the Cash Management Fund at June 30, 1987.

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 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>Amortized Cost</u>	<u>Market Value</u>
	(in 000s)	
Bonds:		
U.S. and Municipal Government bonds	\$ 9,525	\$ 9,458
Industrial bonds	83,790	76,469
Telephone bonds	51,913	46,236
Gas, electric, and water bonds	125,731	112,053
Finance companies—senior debt	13,299	12,819
Railroad equipment obligations	1,470	1,414
Other	33,062	31,830
	<u>318,790</u>	<u>290,279</u>

NOTES TO FINANCIAL STATEMENTS—Continued

STATE OF NEW JERSEY

TEACHERS' PENSION AND ANNUITY FUND

NOTE D—INVESTMENTS—Continued

	Amortized Cost	Market Value
	(in 000s)	
Mortgages	\$ 915,519	\$ 891,850
Common Pension Fund A	2,719,701	4,383,465
Common Pension Fund B	2,449,786	2,494,195
State of New Jersey Cash Management Fund	153,128	153,128
TOTAL	\$6,556,924	\$8,212,917

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 Fund is a 44% and 40% 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 Fund 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 \$1,663,764,000 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 \$768,255,000. The effect on the market value of the remaining securities held at June 30, 1987 was immaterial.

Retirement benefits payable to the 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 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 fund creditable to:

Retirement Reserve Fund:

Credited to fund	\$1,786,930,988
Add accrued interest creditable	82,300,594
Add reserve transferable from Contingent Reserve Fund	65,286,843
Minimum Pension Fund	2,531

Total

\$1,934,520,956

Pension Fund:

Credited to fund	\$ 2,409,931
Add accrued interest creditable	20,083

Total

2,430,014

Annuity Savings Fund:

Credited to fund	\$1,205,709,391
Add accrued interest creditable	50,613,649

Total

1,256,323,040

Contingent Reserve Fund:

Credited to fund	\$2,188,627,544
Add accrued interest creditable	102,898,322
Add excess interest earnings creditable	36,296,036
Deduct reserve transferable to Retirement Reserve Fund	65,286,843

Total

\$2,262,535,059

Special Reserve Fund:

Credited to fund	\$ 11,907,143
Add excess interest earnings creditable	41,245,435
Realized Gains and Losses Fund	220,462,165

Total Present Assets

53,152,578

\$ 5,729,423,812

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

\$1,240,357,025

Present value of prospective
accrued liability contributions to
be made by state allocable to
Pension Fund on account of
non-veteran present entrants
including payment due July 1,
1986

\$2,181,702

Present value of prospective
contributions to Contingent
Reserve Fund on account of
non-veterans new entrants and
all veterans including payments
due July 1, 1986

To be made by state:

Normal contributions	\$4,096,871,890
Accrued liability contributions	322,960,599

To be made by employers on
account of veterans in service
January 1, 1955

2,985,432

4,422,817,921

Total Prospective Assets
TOTAL ASSETS

\$ 5,665,356,648
\$11,394,780,460

LIABILITIES

**Present value of benefits payable on
account of beneficiaries now drawing
allowances from the Retirement Reserve Fund:**

Service and early service benefits	\$1,830,778,373	
Disability benefits	61,352,729	
Benefits to dependent beneficiaries	42,389,854	\$ 1,934,520,956

**Present value of benefits payable on
account of beneficiaries now drawing
allowances from the Pension Fund:**

Service and early service benefits	\$ 2,324,327	
Disability benefits	7,752	
Benefits to dependent beneficiaries	142,273	2,474,352

**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	\$8,603,143,459	
Ordinary disability retirement allowances	177,622,594	
Accidental disability retirement allowances	14,871,520	
Ordinary death benefits	423,451,245	
Accidental death benefits	5,840,569	
Return of members' contributions upon withdrawal before retirement	232,855,765	\$ 9,457,785,152
TOTAL LIABILITIES		<u>\$11,394,780,460</u>

LEVEL OF FUNDING

With respect to the funding of the system, the following is an excerpt from page 29 of the actuarial valuation as of March 31, 1986.

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	\$7,252,971,900
B. Valuation Assets	\$5,729,423,812
C. Funding Level $B \div A$	79.0%

The projected accrued liabilities are calculated using the valuation interest rate (6½ 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

	<u>Balance</u> <u>6/30/87</u>	<u>Balance</u> <u>6/30/86</u>
Dividend Accumulation	\$4,328,056	\$8,109,996
Special Reserve	—	—
Insurance Continuance	0	983,191
Advance Premium	5,816,097	4,391,045

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Teachers' Pension and Annuity Fund

State of New Jersey

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