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INDEPENDENT AUDITORS' REPORT

Retirement Board
Public Employee Retirement System of Idaho
Boise, Idaho

We have audited the accompanying basic financial statements of the Public Employee Retirement System of Idaho (the "System"), a component unit of the State of Idaho, as of June 30, 2005, and for the year then ended, listed in the foregoing table of contents. These basic financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these basic financial statements based on our audit. The prior year summarized comparative information has been derived from the System's 2004 financial statements and, in our report dated November 2, 2004, we expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the basic financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such basic financial statements present fairly, in all material respects, the plan net assets of the pension funds of the System as of June 30, 2005 and the changes in plan net assets of the pension funds for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis and required supplementary information listed in the Table of Contents are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the System's management. We have applied certain limited procedures which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was performed for the purpose of forming an opinion on the basic financial statements of the System taken as a whole. The additional supplementary schedules on pages 50 through 52 are presented for purposes of additional analysis and are not a required part of the basic financial statements of the System. The additional supplementary schedules are also the responsibility of the System's management. Such additional information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects when considered in relation to the basic financial statements taken as a whole. The Introductory Section, Investment Section, Actuarial Section, and Statistical Section listed in the Table of Contents are also presented for purposes of additional analysis and are not a required part of the basic financial statements of the System. Such additional information has not been subjected to the auditing procedures applied in our audit of the basic financial statements and, accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 19, 2005 on our consideration of the System's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

October 19, 2005

MANAGEMENT'S DISCUSSION AND ANALYSIS

Management is pleased to provide this Management's Discussion and Analysis (MD&A) of the financial activities of the Public Employee Retirement System of Idaho (the System or PERSI) as of and for the year ended June 30, 2005. This overview and analysis is designed to focus on current known facts and activities and resulting changes. We encourage readers to consider the information presented here in conjunction with information furnished in the Letter of Transmittal, beginning on page 10 of this report.

The System administers five fiduciary funds. These consist of two defined benefit pension trust funds, the PERSI Base Plan and the Firefighters' Retirement Fund (FRF), and three defined contribution pension trust funds, the PERSI Choice Plan 401(k) and 414(k) and the Sick Leave Insurance Reserve Fund.

Financial Highlights

- Plan net assets for all pension funds administered by the System increased $862 million during the fiscal year 2005. The increase in the defined benefit plans was primarily due to the continuation of favorable investment markets. The increase in the Choice Plan 401(k) was due to new contributions in addition to market gains. Each fund experienced an increase in net assets.

PERSI Base Plan	$ 788,494,640
Firefighters' Retirement Fund	16,814,037
PERSI Choice Plan 414(k)	3,055,242
PERSI Choice Plan 401(k)	35,176,225
Sick Leave Insurance Reserve Fund	18,514,290
Total increase in plan net assets	$ 862,054,434

- Investments for the two defined benefit plans, the PERSI Base Plan and the FRF, are pooled. For the fiscal year ended June 30, 2005, the rate of return net of investment expenses on the pooled investment assets was 10.3% compared with 17.6% for the prior year. All of the plans experienced gains as a result of positive market performance. Net investment income for all of the funds administered by the System for the fiscal year ended June 30, 2005, was $819 million.

Net investment income:	
PERSI Base Plan	$ 769,968,881
Firefighters' Retirement Fund	21,267,341
PERSI Choice Plan 414(k)	5,519,836
PERSI Choice Plan 401(k)	9,629,286
Sick Leave Insurance Reserve Fund	13,089,800
Total net investment income	$ 819,475,144

- As of June 30, 2005 and 2004, the funding ratio (actuarial value of assets divided by actuarial accrued liability) and amortization period (estimated time to payoff unfunded liability) for the unfunded actuarial liability for each of the defined benefit plans were:

	2005 Funding Ratio	Amortization Period	2004 Funding Ratio	Amortization Period
PERSI Base Plan	94.2%	6.2 years	91.7%	7.8 years
Firefighters' Retirement Fund	73.5%	9.0 years	69.5%	10.9 years

For the PERSI Base Plan and the FRF in 2005, contributions and other income of $393.7 million exceeded deductions to net assets of $379.6 million by $14.1 million. This increase in income in addition to investment gains of $791.2 million brought the defined benefits plans' net assets to $8.5 billion. For actuarial calculations, the System's actuary uses market value to determine the actuarial value of assets. For the July 1, 2005, valuation, the actuarial value of assets for the PERSI Base Plan was $8.2 billion. The aggregate actuarial liability for all PERSI Base Plan employers was $8.8 billion. On an actuarial basis, the assets held currently fund 94.2% of this liability.

The System's funding objective is to meet long-term benefit obligations through contributions and investment income and provide a reserve against market fluctuations. The funding ratio listed above gives an indication of how well this objective has been met at a specific point in time. The higher the funding ratio, the better the plan is funded. For more detailed information and history of the funding ratio, see the Schedule of Funding Progress on page 46 of this report. The actuarial funding ratio for the two defined benefit plans improved because investment performance was above the actuarial expected rate. The PERSI Board initiated a systematic increase in the employee and employer contribution rates beginning July 1, 2004, to provide a stable funding base and to bring the amortization period below the statutorily required 25-year period for the Base Plan. Because of these contribution rate increases, and improving investment markets, the amortization period of the unfunded liability has decreased and should continue to do so based on current assumptions. The PERSI Board decided to postpone, for a second year, the July 1, 2005 and 2006, scheduled rate increases.

Using the Annual Financial Report

This discussion and analysis is intended to serve as an introduction to the System's financial statements. The financial section is comprised of four components: (1) fund financial statements, (2) notes to the financial statements, (3) required supplementary information, and (4) other supplementary schedules.

Fund Financial Statements—There are two financial statements presented for the fiduciary funds. The Statement of Plan Net Assets as of June 30, 2005, indicates the net assets available to pay future payments and gives a snapshot at a particular point in time. The Statement of Changes in Plan Net Assets for the year ended June 30, 2005 provides a view of the current year's activity. It details the additions and deductions to the individual funds and supports the change to the prior year's ending net asset value on the Statement of Net Assets. All pension fund statements are presented on a full accrual basis and reflect all trust activities, as incurred.

Notes to Financial Statements—The notes provide additional information essential for a full understanding of the data provided in the fund financial statements. The notes to the financial statements can be found on pages 13–27 of this report.

Required Supplementary Information—The required supplementary information consists of Schedules of Funding Progress and Schedules of Employer Contributions and related notes concerning the funding status for the defined benefit pension trust funds. These schedules provide historical trend information, illustrating the changes in the funded status over time.

Additional Supplementary Schedules—The additional schedules (Schedule of Administrative Expenses and Schedule of Investment Expenses) are presented for additional analysis.

Comparative Financial Statements

Defined Benefit Pension Trust Funds

The PERSI Base Plan and the Firefighters' Retirement Fund are qualified plans under Internal Revenue Code and provide retirement and disability benefits to the employees of affiliated employers. Benefits are funded by member and employer contributions and by earnings on investments. Assets for these plans are pooled for investment purposes.

Defined Benefit Pension Trust Funds Net Assets

	As of June 30, 2005	As of June 30, 2004	$ Change	% Change
Assets:				
Cash and cash equivalents	$ 3,631,830	$ 3,319,118	$ 312,712	9.4 %
Investments sold receivable	819,110,168	712,838,249	106,271,919	14.9 %
Other receivables	40,848,719	37,985,473	2,863,246	7.5 %
Investments—at fair value	8,707,502,568	7,702,033,786	1,005,468,782	13.1 %
Prepaid retiree payroll	27,754,259	24,930,718	2,823,541	11.3 %
Capital assets—net of accumulative depreciation	3,516,630	4,550,368	(1,033,738)	(22.7)%
Total assets	9,602,364,174	8,485,657,712	1,116,706,462	13.2 %
Liabilities:				
Investments purchased payable	1,139,739,452	829,687,740	310,051,712	37.4 %
Benefits and refunds payable	63,069	492,672	(429,603)	(87.2)%
Other liabilities	8,762,883	6,987,207	1,775,676	25.4 %
Total liabilities	1,148,565,404	837,167,619	311,397,785	37.2 %
Net assets available for benefits	$8,453,798,770	$7,648,490,093	$ 805,308,677	10.5 %

The fiscal year ended June 30, 2005, was most notably marked by a continuation in favorable investment markets. Other Liabilities is higher at the end of FY 2005 because of an increase in the amounts owed for investment management services. Growth in asset values and timing of payments can affect the balance of liabilities at the balance sheet date.

The percent change in Investments Sold Receivable and Investments Purchased Payable fluctuates as the volume of trading activity by the System's professional investment managers changes. The cash balance change is due to normal fluctuates in operating cash requirements and the timing of transfers to investment managers. Benefits and Refunds Payable fluctuate based on the demand for and timing of contribution refund payments.

Defined Benefit Pension Trust Funds Changes in Net Assets

	Year Ended June 30, 2005	Year Ended June 30, 2004	$ Change
Additions:			
Employee contributions	$ 145,727,272	$ 131,237,106	$ 14,490,166
Employer contributions	247,842,553	224,336,265	23,506,288
Investment income	791,236,222	1,145,095,702	(353,859,480)
Other additions	149,317	68,284	81,033
Total additions	1,184,955,364	1,500,737,357	(315,781,993)
Deductions:			
Benefits and refunds paid	372,531,093	343,940,999	28,590,094
Administrative expenses	7,115,594	6,991,503	124,091
Total deductions	379,646,687	350,932,502	28,714,185
Changes in net assets available for benefits	$ 805,308,677	$ 1,149,804,855	$ (344,496,178)

The annual amount of Investment Income and Changes in Net Assets Available for Benefits decreased from FY 2004 to FY 2005 because of a slowing of the growth in the investment market. The increase in Benefits and Refunds Paid is a result of increased number of retirees and COLA increase to benefits paid.

Defined Contribution Pension Trust Funds

During FY 2005, the System administered three defined contribution plans. The PERSI Choice Plan, a qualified plan under Internal Revenue Code, consists of a 401(k) plan and a 414(k) plan and provides retirement benefits to members of the Defined Benefit Pension Trust Funds. The Sick Leave Insurance Reserve Fund (the Fund) provides payment of eligible postretirement insurance premiums on behalf of retired state and school employees, based on accumulated unused sick leave at the time of retirement. The Fund’s contributions are financed by state agency and school district employers of the System.

The Choice Plan was created during FY 2001. The 401(k) Plan consists of employee voluntary contributions, rollover contributions, and some employer matching contributions. The 414(k) Plan represents the Gain Sharing allocation made to eligible PERSI members during FY 2001. The assets of this Plan cannot be used to pay the benefits of the 401(k) Plan and vice versa. Beginning with the year ending June 30, 2004, the Sick Leave Insurance Reserve Fund was reclassified from an agency fund to a defined contribution plan with the implementation of GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. For clarity in this presentation, the Sick Leave Insurance Reserve Fund will be reported separately from the PERSI Choice Plan.

Defined Contribution Pension Trust Funds Net Assets

	As of June 30, 2005	As of June 30, 2004	$ Change	% Change
Assets:				
Cash	$ 112,699	$ 115,786	$ (3,087)	(2.7)%
Short-term investments	105,315		105,315	100.0 %
Investments—at fair value	358,955,236	302,399,536	56,555,700	18.7 %
Receivables	2,175,740	2,104,303	71,437	3.4 %
Total assets	361,348,990	304,619,625	56,729,365	18.6 %
Liabilities:				
Other liabilities	19,067	35,459	(16,392)	(46.2)%
Net assets available for benefits	$ 361,329,923	$ 304,584,166	$ 56,745,757	18.6 %

Investments increased from FY 2004 to FY 2005 because of the increase in employee contributions and the continued favorable investment market. Receivables include contributions that are not yet recorded by the recordkeeper at year end and accrued interest and dividends.

Defined Contribution Pension Trust Funds Changes in Net Assets

	Year Ended June 30, 2005	Year Ended June 30, 2004	$ Change	% Change
Additions:				
Employee contributions	$ 21,464,820	$ 17,489,692	$ 3,975,128	22.7 %
Employer contributions	16,270,833	16,726,939	(456,106)	(2.7)%
Investment income	28,238,922	36,160,864	(7,921,942)	(21.9)%
Transfers in	8,275,628	3,318,115	4,957,513	149.4 %
Other additions	10,595	9,410	1,185	12.6 %
Total additions	74,260,798	73,705,020	555,778	0.8 %
Deductions:				
Administrative expenses	53,660		53,660	100.0 %
Benefits and refunds paid	14,003,439	11,384,181	2,619,258	23.0 %
Transfers out	3,457,942	1,976,643	1,481,299	74.9 %
Total deductions	17,515,041	13,360,824	4,154,217	31.1 %
Changes in net assets available for benefits	$ 56,745,757	$ 60,344,196	$ (3,598,439)	(6.0)%

Investment Income decreased from FY 2004 to FY 2005 because of more moderate market growth than the prior year. Transfers In and Out only include rollovers from/to other plans. A large portion of the increase in Transfers In is the result of a PERSI employer's DC plan transfer into the PERSI Choice Plan. Employee Contributions grew due to an increase in the number of employees with salary deferrals. Changes in Employer Contributions vary up or down according to individual employers' desire to match employee contributions.

For FY 2004, the System changed the presentation of the Sick Leave Insurance Reserve Fund from an agency fund to an Other Postemployment Benefit (OPEB) in accordance with a new accounting standard issued by the Governmental Accounting Standards Board in April 2004. Investment Income decreased from FY 2004 to FY 2005 because of more moderate growth in the investment market. Beginning in FY 2005, a fee representing administrative expense is being assessed to the sick leave fund.

Plan Membership

This table reflects PERSI Base Plan and Choice Plan membership at the beginning and end of the fiscal year.

Changes in Plan Membership

	Base Plan			Choice Plan		
	2005	2004	Change	2005	2004	Change
Active participants:	64,391	63,385	1.6 %	44,780	41,836	7.0 %
Actively contributing				8,218	6,778	21.2 %
Vested	40,796	39,999	2.0 %			
Non-vested	23,595	23,386	0.9 %			
Retirees and beneficiaries	27,246	26,043	4.6 %	522	420	24.3 %
Terminated vested	8,460	8,118	4.2 %	8,479	6,388	32.7 %

While the above table reflects changes in active participants, the following table demonstrates the changes in retirees and beneficiaries during the period.

Changes in Retirees and Beneficiaries (Base Plan)

Beginning July 1, 2004	26,043
Retirements	1,935
Death of retiree/beneficiary	(732)
Ending June 30, 2005	27,246

Investment Activities

Long-term asset growth is vital to the Defined Benefit Plans' current and continued financial stability. Therefore, trustees have a fiduciary responsibility to act with prudence and discretion when making plan investment decisions. To assist the Board in this area, a comprehensive formal investment policy is updated periodically. As managers are added, specific detailed investment guidelines are developed, adopted, and become part of that manager's agreement.

Portfolio performance is reviewed monthly by the Board and its consultants. Performance is evaluated individually, by money manager style, and collectively by investment type and for the aggregate portfolio. Investment types include both domestic and international equities, domestic and international fixed income, and real estate.

Economic Factors

PERSI, like any pension fund, has a broad range of opportunities for investment in the open market, as well as many choices for asset allocation and investment managers. For purposes of comparison, the table of Investment Results in the Investment Section of this report indicates various index returns, which are reflective of the market environment available.

As a result of the FY 2002 amortization period calculation being 39.3 years, the Board increased contribution rates 1% per year for three years beginning July 2004. The PERSI Board has postponed, for a second year, the rate increases scheduled for July 1, 2005 and July 1, 2006, due to a significant increase in funded status. These two increases are now scheduled for July 1, 2007 and 2008. The maximum amortization period allowed by state law for the Base Plan is 25 years. PERSI's Base Plan amortization period before any cost of living adjustment (COLA) as of July 1, 2005, is 6.2 years.

During FY 2004, an actuarial study of PERSI experience from July 1, 1999 through June 30, 2003, was done. An experience study is an analysis of economic assumptions and active member demographics. This study resulted in some changes to the economic assumptions and relatively minor changes to the demographic assumptions. Actuarial assumptions are estimates as to the occurrence of future events affecting such things as changes in pension costs, compensation, and rates of investment earnings and are used to measure and budget future costs. The most significant changes in the economic assumptions involved the recommended reduction of the inflation assumption from 4.00% to 3.75% and the general wage increase assumption from 4.75% to 4.50%. To maintain the 4.00% real investment return target derived from our asset allocation, the investment assumption was decreased from 8.00% to 7.75% which matches a trend nationwide. These changed assumptions will not change the actual cost of future benefits but will result in a slight decrease to the funding of the benefits. The effective date of these changes was June 30, 2004. The changes are included in the actuarial valuation dated July 1, 2005.

PUBLIC EMPLOYEE RETIREMENT SYSTEM OF IDAHO

COMBINING STATEMENT OF PLAN NET ASSETS—PENSION FUNDS
AS OF JUNE 30, 2005 WITH SUMMARIZED FINANCIAL INFORMATION AS OF JUNE 30, 2004

	Pension Funds					Totals	
	PERSI Base Plan	Firefighters' Retirement Fund	PERSI Choice Plan 414(k)	PERSI Choice Plan 401(k)	Sick Leave Insurance Reserve Fund	2005	2004
ASSETS							
CASH AND CASH EQUIVALENTS	$ 3,533,837	$ 97,993	$ -	$ 37,622	$ 75,077	$ 3,744,529	$ 3,434,904
INVESTMENTS—At fair value:							
Fixed income investments:							
Domestic	2,052,306,470	56,910,116			72,820,634	2,182,037,220	1,905,420,592
International	55,445,555	1,537,496				56,983,051	59,889,873
Idaho commercial mortgages	252,934,663	7,013,836				259,948,499	259,763,230
Short-term investments	498,263,260	13,816,757		105,315		512,185,332	277,708,503
Real estate	77,196,628	2,140,650				79,337,278	59,687,610
Equity Securities:							
Domestic	3,545,284,156	98,310,139			109,282,253	3,752,876,548	3,482,488,760
International	1,785,482,929	49,511,144				1,834,994,073	1,657,691,373
Private equity	205,646,233	5,702,536				211,348,769	163,073,839
Mutual, collective, unitized funds			56,973,945	119,878,404		176,852,349	138,709,542
Total investments	8,472,559,894	234,942,674	56,973,945	119,983,719	182,102,887	9,066,563,119	8,004,433,322
RECEIVABLES:							
Investments sold	797,093,613	22,016,555				819,110,168	712,838,249
Contributions	4,987,308	29,057		265,826		5,282,191	5,352,594
Interest and dividends	34,869,230	963,124	241,728	374,534		36,448,616	33,456,550
Total receivables	836,950,151	23,008,736	241,728	640,360	-	860,840,975	751,647,393
ASSETS USED IN PLAN OPERATIONS—Net	3,516,630					3,516,630	4,550,368
DUE FROM OTHER FUNDS					1,293,652	1,293,652	1,280,632
RETIREE PAYROLL IN PROCESS	27,754,259					27,754,259	24,930,718
TOTAL ASSETS	$ 9,344,314,771	$ 258,049,403	$ 57,215,673	$ 120,661,701	$ 183,471,616	$ 9,963,713,164	$ 8,790,277,337

(Continued)

PUBLIC EMPLOYEE RETIREMENT SYSTEM OF IDAHO

COMBINING STATEMENT OF PLAN NET ASSETS—PENSION FUNDS
AS OF JUNE 30, 2005 WITH SUMMARIZED FINANCIAL INFORMATION AS OF JUNE 30, 2004

	Pension Funds					Totals	
	PERSI Base Plan	Firefighters' Retirement Fund	PERSI Choice Plan 414(k)	PERSI Choice Plan 401(k)	Sick Leave Insurance Reserve Fund	2005	2004
LIABILITIES AND NET ASSETS							
LIABILITIES:							
Accrued liabilities	$ 7,276,927	$ 192,304	$ -	$ -	$ 19,067	$ 7,488,298	$ 5,742,034
Benefits and refunds payable	63,069					63,069	492,672
Due to other funds	1,293,652					1,293,652	1,280,632
Investments purchased	1,109,104,823	30,634,629				1,139,739,452	829,687,740
Total liabilities	1,117,738,471	30,826,933	-	-	19,067	1,148,584,471	837,203,078
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS (see supplementary schedules of funding progress)	$8,226,576,300	$227,222,470	$57,215,673	$120,661,701	$183,452,549	$8,815,128,693	$7,953,074,259

See notes to financial statements.

(Concluded)

PUBLIC EMPLOYEE RETIREMENT SYSTEM OF IDAHO

COMBINING STATEMENT OF CHANGES IN PLAN NET ASSETS—PENSION FUNDS
FOR THE YEAR ENDED JUNE 30, 2005 WITH SUMMARIZED FINANCIAL INFORMATION FOR YEAR ENDED JUNE 30, 2004

	Pension Funds					Totals	
	PERSI Base Plan	Firefighters' Retirement Fund	PERSI Choice Plan 414(k)	PERSI Choice Plan 401(k)	Sick Leave Insurance Reserve Fund	2005	2004
ADDITIONS:							
Contributions:							
Members	$ 145,638,100	$ 89,172	$ -	$ 21,464,820	$ -	$ 167,192,092	$ 148,726,798
Employers	236,116,938	11,725,615		203,026	16,067,807	264,113,386	241,063,204
Transfers in				8,275,628		8,275,628	3,318,115
Total contributions	381,755,038	11,814,787	-	29,943,474	16,067,807	439,581,106	393,108,117
Investment income:							
Net appreciation in fair value of investments	579,046,289	15,993,861	5,586,185	5,195,696	13,215,894	619,037,925	1,001,322,358
Interest, dividends and other investment income	223,427,569	6,171,301	56,994	4,474,236		234,130,100	208,641,123
Less investment expenses	(32,504,977)	(897,821)	(123,343)	(40,646)	(126,094)	(33,692,881)	(28,706,915)
Total investment income	769,968,881	21,267,341	5,519,836	9,629,286	13,089,800	819,475,144	1,181,256,566
Other—net	149,317				10,595	159,912	77,694
Total additions	1,151,873,236	33,082,128	5,519,836	39,572,760	29,168,202	1,259,216,162	1,574,442,377
DEDUCTIONS:							
Benefits and refunds paid to members and beneficiaries	356,263,002	16,268,091	276,432	3,126,755	10,600,252	386,534,532	355,325,180
Administrative expenses	7,115,594				53,660	7,169,254	6,991,503
Transfers out			2,188,162	1,269,780		3,457,942	1,976,643
Total deductions	363,378,596	16,268,091	2,464,594	4,396,535	10,653,912	397,161,728	364,293,326
INCREASE IN NET ASSETS	788,494,640	16,814,037	3,055,242	35,176,225	18,514,290	862,054,434	1,210,149,051
NET ASSETS HELD IN TRUST:							
Beginning of year	7,438,081,660	210,408,433	54,160,431	85,485,476	164,938,259	7,953,074,259	6,742,925,208
End of year	$ 8,226,576,300	$ 227,222,470	$ 57,215,673	$ 120,661,701	$ 183,452,549	$ 8,815,128,693	$ 7,953,074,259

See notes to financial statements.

PUBLIC EMPLOYEE RETIREMENT SYSTEM OF IDAHO

NOTES TO FINANCIAL STATEMENTS
AS OF AND FOR THE YEAR ENDED JUNE 30, 2005

1. GENERAL DESCRIPTION OF THE FUNDS

General—The Public Employee Retirement System of Idaho (the System or PERSI) is the administrator of five pension plans including two defined benefit retirement plans, the Public Employee Retirement Fund Base Plan (PERSI Base Plan) and the Firefighters' Retirement Fund (FRF); and three defined contribution plans, the Public Employee Retirement Fund Choice Plans 401(k) and 414(k) (PERSI Choice Plan) and the Sick Leave Insurance Reserve Fund.

Reporting Entity—The System is a component unit of the State of Idaho and is included in the State of Idaho Comprehensive Annual Financial Report. The basic financial statements of the System include the financial activities of all of the above funds. A retirement board (the Board), appointed by the Governor and confirmed by the Idaho Senate, manages the System, which includes selecting the funding agents and establishing funding policy.

Defined Benefit Retirement Plans—The PERSI Base Plan and FRF are both cost-sharing, multiple-employer defined benefit retirement plans that provide benefits based on members' years of service, age, and highest average salary. In addition, benefits are provided for disability, death, and survivors of eligible members or beneficiaries.

Statutes governing the PERSI Base Plan are Title 59, Chapter 13. Statutes governing FRF are Title 72, Chapter 14 of Idaho Code.

Members become fully vested in their retirement benefits with five years of credited service (5 months for elected or appointed officials). Members are eligible for retirement benefits upon attainment of the ages specified for their employment classification. The annual service retirement allowance for each month of credited service is 2.0% (2.3% police/firefighters) of the average monthly salary for the highest consecutive 42 months.

State agencies, school districts, cities, counties, highway districts, water and sewer districts, and other political subdivisions contribute to the System. As of June 30, 2005, the number of participating employer units in the PERSI Base Plan was:

Cities	143
School districts	135
Highway and water districts	121
State subdivisions	98
Counties	40
Other	147
	684

As of June 30, 2005, the number of benefit recipients and members in the System consisted of the following:

Members, retirees and beneficiaries currently receiving benefits during the fiscal year and terminated employees entitled to benefits but not yet receiving them:	
Members:	
Active	64,391
Terminated and vested	8,460
Retirees and beneficiaries	27,246

FRF has 22 participating employer units all consisting of fire departments participating in the PERSI Base Plan. As of June 30, 2005, there were 20 active members and 599 retired members or beneficiaries collecting benefits from FRF. The FRF covers a closed group of firefighters who were hired before October 1, 1980, and who receive benefits in addition to those provided under the Base Plan. The cost of these additional benefits is paid by FRF member and employer contributions and receipts from a fire insurance premium tax.

The benefit payments for the PERSI Base Plan and FRF are calculated using a benefit formula adopted by the Idaho Legislature. The Base Plan is required to provide a 1% minimum cost of living increase per year provided the Consumer Price Index increases 1% or more. The Retirement Board has the authority to provide higher PERSI Base Plan cost of living increases to a maximum of the Consumer Price Index movement or 6%, whichever is less; however, any amount above the 1% minimum is subject to review by the Idaho Legislature. The cost of living increase for the FRF is based on the increase in the statewide average firefighter's wage.

The PERSI Base Plan and FRF benefits are funded by contributions from members and employers and earnings from investments. Additional FRF funding is obtained from receipts from a state fire insurance premium tax. Member and employer contributions are paid as a percentage of applicable member compensation. PERSI Base Plan member contribution rates are defined, by state law, as a percentage of the employer contribution rate. FRF member contribution rates are fixed by state law. Employer contribution rates are recommended by periodic actuarial valuations and are subject to the approval of the Retirement Board and limitations set forth in state statute. Valuations are based on actuarial assumptions, the benefit formulas, and employee groups of the System. Costs of administering the fund are financed through the contributions and investment earnings of the System.

Upon termination of employment, accumulated member contributions plus interest, accrued at 17.51% January 1, 2005 through June 30, 2005 (3.22% July 1, 2004 to December 31, 2004) compounded monthly per annum, are refundable. Withdrawal of such accumulated contributions results in forfeiture of the member's accrued benefit; however, state law does include provisions for reinstatement of forfeited service upon repayment of the accumulated contributions plus interest.

Defined Contribution Retirement Plans—The PERSI Choice Plans and the Sick Leave Insurance Reserve Fund are defined contribution retirement plans. The statute governing the Choice Plans is Idaho Code Title 59, Chapter 13. The statutes governing the Sick Leave Insurance Reserve Fund are Idaho Code, Sections 67-5339, 33-1216, 59-1365, and 33-1228.

The PERSI Choice Plans are defined contribution pension plans made up of a qualified 401(k) plan and a 414(k) plan. The assets of the two plans within the Choice Plan are commingled for investment and recordkeeping purposes. Participants direct their investment mix without restriction and may elect to change their salary deferral every pay period. The 401(k) portion of the Choice Plan is open to all active PERSI Base Plan members and was established February 1, 2001. On May 1, 2001, this Plan became open to voluntary employer matching contributions at rates determined by the employers. Beginning in January 2002, employees could make tax-deferred contributions up to 100% of their gross salary less deductions and subject to the IRS annual contribution limit. The 414(k) portion of the Choice Plan was established for Gain Sharing allocations from the PERSI Base Plan. The Gain Sharing amount (if any) is based on funding levels in the Base Plan. Eligibility for Gain Sharing requires twelve months of active PERSI Base Plan membership as defined in Idaho statutes and PERSI rules. On February 1, 2001, all eligible Base Plan members who were active as of June 30, 2000, and eligible to receive Gain Sharing contributions, received an allocation.

The System has entered into a contract with Mellon Human Resources & Investor Solutions (MHR&IS) for plan recordkeeping services. MHR&IS was acquired by Affiliated Computer Services, Inc. (ACS) in May 2005. The plan offers eleven investment options, which are mutual or collective funds. The plans include the PERSI Total Return Fund (PERSI TRF), seven equity funds, two fixed income funds, and a stable value fund. Participants may allocate their assets in 1% increments among these options; however, if no allocation preference is indicated, a default investment election to the PERSI TRF is made. The PERSI TRF is a unitized fund comprised of investment accounts of the PERSI Base Plan.

The PERSI Choice Plan has 684 employer units eligible to have participating employees. As of June 30, 2005, there were 47,626 participants with balances in the Choice Plan. Some of these participants are in both the 414(k) Plan and the 401(k) Plan. As of June 30, 2005, the Choice Plan 414(k) had 42,578 participants, and the Choice Plan 401(k) had 10,707. The administrative expenses of the PERSI Choice Plan, most of which are paid to MHR&IS, are funded by the PERSI Base Plan.

For the Sick Leave Insurance Reserve Fund, school districts and state agencies in Idaho provide payment of eligible postretirement insurance premiums on behalf of former employees based on unused accumulated sick leave at their retirement date. Employers are responsible for any unfunded benefit obligations. The System administers these funds on behalf of the employers, who fund the program by remitting a percentage of payroll to the System to cover future insurance premiums. Other PERSI employers may participate in the fund on a pay as you go basis.

School District Employees—For school district employees, the unused sick leave amount available for benefit is based on one-half of their eligible sick leave balance and rate of compensation at retirement.

State Employees—State employees are limited to the number of allowable hours of sick leave they may use as part of the unused sick leave program as follows:

Credited Hours of State Service	Maximum Allowable Sick Leave Hours
0–10,400 (0–5 years)	420
10,401–20,800 (5–10 years)	480
20,801–31,200 (10–15 years)	540
31,201+ (15 years or more)	600

Members may use one-half of sick leave hours accrued up to the allowable maximum multiplied by their rate of compensation at retirement.

The rate for state agency and school district contributions was .65% and 1.15% of covered salary at June 30, 2005, respectively. Rules have been adopted to increase the contribution rate for school district employers to amortize the unfunded liability and to allocate higher costs to school districts that have a greater liability in the system.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting—The System's basic financial statements are prepared utilizing the accrual basis of accounting. Employee and employer contributions are recognized as additions to net assets when due and receivable, pursuant to formal commitments and statutory or contractual requirements, investment income is recognized when earned, and benefit payments and refunds and other expenses are recorded when the benefits are due and payable in accordance with the plans' terms. The pension funds are accounted for on a flow of economic resources measurement focus. The System adheres to Statement No. 25 of the Governmental Accounting Standards Board ("GASB No. 25"), *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans* and to GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans.*

Investments—The System's investments are presented at fair value. Purchases and sales are recorded at the trade date. Investments of the PERSI Base Plan, FRF, and the PERSI TRF (an option of the PERSI Choice Plan) are pooled for investment purposes.

The Board utilizes and directs individual fund managers to provide whatever investment management and custodial functions the Board has determined best achieves the System's investment objectives. Each fund manager is generally granted full discretion in making investment decisions, within asset allocation policy, portfolio investment policy, specific investment guidelines and other special restrictions set by the Board. The Board monitors overall investment performance and periodically evaluates the performance of each fund manager. The Board in its administration of the System and management of the investment program is guided by the Idaho Uniform Prudent Investor Act, Sections 68-501 through 68-514 of the Idaho Code and of fiduciary responsibilities in the Idaho Code, Section 59-1301, and is empowered in its sole discretion to limit, control, and designate the types and amounts of investments. The Board has adopted investment policy including policy related to deposit and investment risks identified in GASB Statement No. 40.

The fair value of investments is based on published market prices and quotations from major investment brokers, when available. Mortgages have been valued on the basis of their future principal and interest payments discounted at prevailing interest rates for similar instruments of matching duration. The fair value of real estate investments is based on industry practice. For recent acquisitions, cost closely approximates fair value. The fair value of longer term real estate holdings is estimated based on the System's consultants and independent appraisals. Short-term investments are reported at market value, when published market prices and quotations are available, or at cost plus accrued interest, which approximate market value. The fair values of private equity limited partnership investments by their nature have no readily ascertainable market prices. Similar to real estate, cost closely approximates fair value for recent acquisitions. Thereafter, the fair values of limited partnership funds are based on the valuations as presented by the general partner, approved by the funds' advisory committee, and reviewed by managements' consultants. Generally, the companies within a fund are valued by the general partner, taking into account many factors such as the purchase price, estimated liquidation value, significant events like initial public offerings, bankruptcies, and additional rounds of financing, and other relevant factors. Because of the lack of published market prices for these investments, the estimated fair values may differ significantly from the values that would have been used had a ready market for the investments existed. Although these differences could be material to the individual company values, private equity represents less than 2.5% of total investments.

The System purchases forward contracts for certain international investments and United States of America agency-guaranteed collateralized mortgage obligations for the purpose of enhancing liquidity, reducing transaction or other costs, or partially hedging an existing exposure. The System does not incur any costs for forward contracts until the settlement date. Future potential obligations for the forward contracts are not recognized until the contract expiration date.

Use of Estimates—The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of net assets and liabilities, disclosure of contingent liabilities, and the actuarial present value of accumulated plan benefits at the date of the financial statements. Actual results could differ from those estimates. The System utilizes various investment instruments. Investment securities, in general, are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the financial statements.

Assets Used in Plan Operations—These assets represent buildings, equipment, and computer software development costs used by the System and are recorded at cost. Depreciation and amortization are provided on the straight-line method over the estimated useful lives of the assets. The estimated useful life for buildings is 30 years. The estimated useful life of the computer software development costs is five years. The particular type of equipment purchased in May 2005, but not put into service until FY 2006 has a 3-year useful life.

"Totals"—The summarized financial information as of and for the year ended June 30, 2004, presented in the "Totals" column on the accompanying basic financial statements, does not present consolidated financial information and is not necessary for a fair presentation of the basic financial statements but is presented only to facilitate financial analysis and for comparison purposes.

New Accounting Standards—In March 2003, the GASB issued Statement No. 40, Deposit and Investment Risk Disclosures. Statement No. 40 amends GASB Statement No. 3, Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements. The objective of this Statement is to update the custodial credit risk disclosure requirements of GASB Statement No. 3 and to establish more comprehensive disclosure requirements addressing other common risks of the deposits and investments of state and local governments. The System has implemented this Statement for the fiscal year ended June 30, 2005.

3. DEPOSITS AND INVESTMENTS

A. Deposits

Cash and cash equivalents are deposited with various financial institutions and are carried at cost plus accrued interest. Cash balances represent operating cash accounts held by various banks and on deposit with the State Treasurer. Cash held by the State Treasurer is held in the System's name and is fully insured or collateralized with securities held by the State Treasurer or by its agent in the State Treasurer's name. Cash deposits in bank accounts for operations are covered by federal depository insurance up to $100,000. The System does not have a policy for custodial credit risk related to operating cash on deposit at local financial institutions.

Cash and Cash Equivalents:	
Held by the State Treasurer	$ 2,598,976
FDIC insured	203,075
Uninsured and uncollateralized	942,478
Total	$ 3,744,529

B. Investments

Investments of the pension trust funds are reported at fair market value. See note 2 for more details. The Board of Trustees maintains a formal Statement of Investment Policy, which addresses governing provisions and additional guidelines for the investment process. In fulfilling its responsibilities, the Board of Trustees has contracted with investment managers, a master global custodian, and a cash manager. Manager contracts include specific guidelines regarding the PERSI investments under management. For the year ended June 30, 2005, Mellon Global Securities Services was the global custodian for the majority of the investments of the combined PERSI Base Plan, FRF, and PERSI Choice Plan.

Investments at fair value as of June 30, 2005:

Domestic fixed income	$ 2,109,216,586
Co-mingled domestic fixed income (Sick Leave Insurance Reserve Fund)	72,820,634
Short-term investments	498,180,340
Idaho commercial mortgages	259,948,499
Total domestic fixed income securities	2,940,166,059
International fixed income	56,983,051
Total fixed income securities	2,997,149,110
Domestic equities	3,643,594,295
International equities	1,834,994,073
Short-term investments	14,004,992
Real estate	79,337,278
Private equity	211,348,769
Mutual funds (PERSI Choice Plan)	176,852,349
Co-mingled equity fund (Sick Leave Insurance Reserve Fund)	109,282,253
Total investments	$ 9,066,563,119

***Derivatives*—**Derivatives are financial obligations whose value is derived from underlying debt or equity securities, commodities, or currencies. They are designed, among other things, to help investors protect themselves against the risk of price changes. In accordance with its investment policy, the System, through its external investment managers, holds investments in futures, options, swaps, repurchase agreements, and forward foreign currency contracts. Only a few selected managers are permitted to use derivatives. In every case, the types of derivatives used and limits on their use are defined in manager contracts and are monitored on an ongoing basis.

Futures contracts are contracts for delayed delivery or receipt of securities in which the seller agrees to make delivery and the buyer agrees to take delivery at a specified future date, of a specified instrument, at a specified price. Market risk arises due to market price and interest rate fluctuations that may result in a decrease in the fair value of futures contracts. Futures contracts are traded on organized exchanges and require initial margin in the form of cash or marketable securities. Daily, the net change in the futures contract value is settled in cash with the exchanges. Holders of futures contracts look to the exchange for performance under the contract. Accordingly, the credit risk due to the nonperformance of counterparties to futures contracts is minimal. At June 30, 2005, the System had futures contracts with a fair value of $100,264 that are included in Fixed Income Investments. Cash equivalents and short-term investments in amounts necessary to settle the futures contracts were held in the portfolio so that no leverage was employed, in accordance with the System's Statement of Investment Policy. At June 30, 2005, the System had the following futures contracts exposure:

	Value covered by contract
Cash and cash equivalents-eurodollar	$147,128
U.S. Treasury bond futures	24,500
U.S. Treasury note futures	1,719

Option contracts are contractual agreements giving the purchaser the right, but not the obligation, to purchase or sell a financial instrument at a specified price within a specified time. The option's price is usually a small percentage of the underlying asset's value. Options strategies used by the System are designed to provide exposures to positive market moves and limit exposures to interest rate and currency fluctuations. At June 30, 2005, the System had option contracts payable with a fair value of $535,744 that is included in liabilities reported as Investments Purchased. At June 30, 2005, the System had the following options contracts exposure:

	Value covered by contract
Cash and cash equivalents purchased call options	$130,798
Cash and cash equivalents purchased put options	13,663
Fixed income purchased call options	24,500
Fixed income purchased put options	1,794
Fixed income written call options	607,045
Fixed income written put options	99,453

Swap agreements are derivative transactions whereby two parties agree to "swap" cash flows over a period of time. Each cash flow can be derived from any market index defined in the swap agreement that is based on a notional value which never actually changes hands. The indexes that determine the amount of cash exchanged can be as simple a fixed interest rate or a variable interest rate like the current prime rate, or as complex as algebraic formulas that combine, enhance, or diminish any number of other market indexes. The System does not anticipate additional significant market risk from swap arrangements. At June 30, 2005, the System had swap agreements with a fair value of $90,941 that are included in International Fixed Income Investments.

Repurchase agreements are short-term securities used to finance trading. A broker/dealer who offers a repurchase agreement borrows money by selling securities and simultaneously agreeing to buy them back at a higher price at a later time. The dealer invests the money paid for the securities, hoping to get a higher return than he owes on his obligation to repurchase the securities. Repurchase agreements are commonly called “repos,” and they function in a way similar to a secured loan with the securities serving as collateral. All sales of investments under repurchase agreements are for fixed terms. The credit exposure at year-end under repurchase agreements was $62,108,362 that is included in Short-term Investments.

Forward Foreign Currency Exchange Contracts are carried at fair value by the System. The System has entered into foreign exchange contracts to purchase or sell currency at various dates in the future at a specific price. Some of the System’s international and real estate investment managers use forward contracts to hedge the exposure of investments to fluctuations in foreign currency. Forward foreign exchange contracts are negotiated between two counterparties. The System could sell the forward contract at a loss, or if it were to continue to hold the contract, the System may make a termination payment to the counterparty to cancel its obligation under the contract and then buy the currency on the open market. The System could also incur a loss if its counterparties failed to perform pursuant to the terms of their contractual obligations. Controls are established by the System and the investment managers to monitor the creditworthiness of the counterparties. The System’s investment managers seek to control this risk through counterparty credit evaluations and approvals, counterparty credit limits, and exposure monitoring procedures. As of June 30, 2005, the System had sold forward currency contracts with a fair value of $809,001,906 and had bought forward currency contracts with a fair value of $809,107,799. Purchases of forward currency contracts are liabilities reported as Investments Purchased, and sales of forward currency contracts are receivables reported as Investments Sold. Unrealized losses of $105,892 at June 30, 2005 were recognized, which represents the loss which would occur from executing these forward foreign currency contracts at June 30, 2005.

Mortgage-Backed Securities—These investments are based on the cash flows from interest and principal payments on the underlying mortgages. As a result, they are sensitive to prepayments, which are likely to occur in declining interest rate environments, thereby reducing the value of the securities. Details regarding interest rate risk for these investments are included in the Interest Rate Risk section below.

TIPS—Treasury Inflation Protected Securities (TIPS) are fixed income securities issued by the U.S. Treasury that pay a fixed coupon rate plus an adjustment for subsequent inflation. At June 30, 2005, the System had invested in TIPS with a fair value of $701,714,595.

C. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to the System. The System’s investment policies require each portfolio to maintain a reasonable risk level relative to its benchmark. As of June 30, 2005, the System’s fixed income assets that are not government guaranteed represented 57% of the fixed income portfolio. The System’s fixed income assets are shown with current credit ratings below.

Credit quality of fixed income securities at fair value:

Credit Quality S&P Rating Level	Domestic	International	Total
Agency (A-1+)	$ 1,216,509	$ -	$ 1,216,509
AAA	616,512,139	25,897,848	642,409,987
AA	50,070,878	5,802,060	55,872,938
A	173,078,732		173,078,732
BBB	108,743,478	4,881,125	113,624,603
BB	20,051,859	88,747	20,140,606
B	14,162,932		14,162,932
CCC	10,012,965		10,012,965
Not rated	353,430,059	76,153,878	429,583,937
Total credit risk fixed income securities	1,347,279,551	112,823,658	1,460,103,209
U.S. government	1,108,400,197		1,108,400,197
Pooled investments	169,606,648		169,606,648
Total fixed income securities investments	2,625,286,396	112,823,658	2,738,110,054
Reconciling Items From Report to Investments on Net Asset Statement			
401(k) Total Return Fund	(43,091,899)	(941,244)	(44,033,143)
USD denominated international	108,206,571	(108,206,571)	
Preferred/convertibles	(10,668,137)	(4,396,478)	(15,064,615)
International short sale liability		57,484,955	57,484,955
Idaho commercial mortgages	259,948,499		259,948,499
Other	484,629	218,731	703,360
Total	$ 2,940,166,059	$ 56,983,051	$ 2,997,149,110

As a matter of practice, there are no strict limitations for credit risk exposures within the portfolio. Each portfolio is managed in accordance with operational guidelines that are specific as to expected portfolio characteristics that usually, but not always, include credit quality and exposure levels. Per the System’s policy, these characteristics are established and monitored within each portfolio, with variances reported by the manager.

D. Custodial Credit Risk

Custodial credit risk is the risk that in the event of a financial institution or bank failure, the System would not be able to recover the value of their deposits and investments that are in the possession of an outside party. The System mitigates custodial credit risk by requiring in policy, to the extent possible, that investments be clearly marked as to PERSI ownership and be registered in the System’s name. All securities are required to be delivered to a third party institution mutually agreed upon by the bank and the System.

The System’s short-term investments are created through daily sweeps of excess cash by the System’s custodian, cash manager, and a few selected investment managers into short-term investment funds. Clearwater Advisors, LLC is the System’s cash manager and invests the bulk of the System’s cash in short-term instruments. Clearwater Advisors manages approximately 70% of the System’s short-term investments. Of the short-term investments at June 30, 2005, $14,004,992 were held by various counterparties not in the System’s name and were neither insured nor registered. The remainder of the pooled short-term investment funds is invested in bank-maintained collective investment funds except collective vehicles held and managed by individual investment managers.

E. Concentration of Credit Risk

Concentration of credit risk is the risk of loss that may be attributed to the magnitude of a government's investment in a single issuer. The System's operational guidelines for investments in any corporate entity are stated in each individual manager's specific portfolio guideline.

In line with policy, the System does not have any investments from a single issuer (excluding explicitly guaranteed governments) that represent more than 5% of the System's net assets.

F. Interest Rate Risk

Market or interest rate risk is the greatest risk faced by an investor in the debt securities market. The price of a debt security typically moves in the opposite direction of the change in interest rates. Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. This risk is managed within the portfolio using the effective duration methodology. The methodology takes into account optionality on bonds and scales the risk of price changes on bonds depending upon the degree of change in rates and the slope of the yield curve. All of the System's fixed income portfolios are managed in accordance with operational guidelines which include an expected range of interest rate risk in the portfolio. Per the System's policy, these characteristics are establish and monitored within each portfolio, with variances reported by the manager. The reporting of effective duration found in the tables below quantifies the interest rate risk of the System's fixed income assets.

Effective duration of domestic fixed income assets by security type:

Investment	Fair Value	Effective Duration in years
Asset-backed securities	$ 17,307,304	1.83
Asset-backed securities	390,607	N/A
Commercial paper	49,124,911	0.12
Commercial paper	219,583,466	N/A
Corporate bonds	390,512,201	4.62
Corporate bonds	908,999	N/A
Fixed income derivatives	(533,151)	N/A
Government agencies	123,505,885	3.3
Government bonds	408,906,167	5.43
Government mortgage-backed securities	446,127,615	2.31
Pooled investments	169,606,648	N/A
Preferred stock	2,503,408	2.22
Preferred stock	8,164,730	N/A
Private placements	24,244,829	3.63
Private placements	1,109,821	N/A
Repurchase agreements	62,108,362	N/A
TIPS	701,714,595	7.73
Total fixed income securities—domestic	2,625,286,397	
Reconciling items:		
401(k) Total Return Fund adjustment	(43,091,899)	
Idaho commercial mortgages	259,948,499	
USD denominated international securities	108,206,571	
Preferred/convertible stock	(10,668,137)	
Other	484,629	
Total	$ 2,940,166,060	

Effective duration of international fixed income assets by security type:

Investment	Fair Value	Effective Duration in years
Commercial paper	$ 13,818,694	0.03
Commercial paper	21,822,090	N/A
Corporate bonds	63,697,070	3.35
Corporate bonds	100,132	N/A
Government bonds	13,385,672	4.74
Total fixed income securities—international	112,823,658	
Reconciling items:		
401(k) Total Return Fund adjustment	(941,244)	
USD denominated international securities	(108,206,571)	
Preferred/convertible stock	(4,396,478)	
Short sale liability	57,484,955	
Other	218,731	
Total	$ 56,983,051	

G. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely impact the fair value of an investment. The System's currency risk exposures, or exchange rate risk, primarily reside within the international equity investment holdings. The System expects these managers to maintain adequately diversified portfolios to limit foreign currency and security risk. Per the System's policy, individual manager guidelines outline at a minimum ranges of currency exposure which are monitored within each portfolio. Managers are required to report variances to the System. Foreign currency risk arises due to foreign exchange rate fluctuations. Currency gains and losses will result from these fluctuations. The System's exposure to foreign currency risk expressed in U.S. dollars as of June 30, 2005, is highlighted in the table on the following page.

Currency exposures:

Currency	Short-term Investments	Equities	Fixed Income	USD Equivalent Fair Value
Australian Dollar	$ 125,710	$ 50,041,673	$ 1,072,475	$ 51,239,858
Botswana Pula		1,450,764		1,450,764
Brazil Real	961,091	23,326,677		24,287,768
British Pound Sterling	(991,086)	310,704,197	(43,217,762)	266,495,349
Canadian Dollar	296,521	13,086,437	14,245,780	27,628,738
Czech Koruna	7,910			7,910
Danish Krone	429	14,477,458		14,477,887
Egyptian Pound	482,128	11,683,379		12,165,507
Euro	1,026,916	556,683,103	(5,614,043)	552,095,976
Hong Kong Dollar	186,457	61,467,279		61,653,736
Hungarian Forint	47,502	6,763,138		6,810,640
Indonesian Rupian	624,739	33,495,396		34,120,135
Israeli Shekel	485,398	8,602,289		9,087,687
Japanese Yen	5,443,298	338,693,613		344,136,911
Malaysian Ringgit	87,994	10,776,490		10,864,484
Mexican New Peso	4,518	15,836,310	21,484,236	37,325,064
New Taiwan Dollar	764,087	39,253,528		40,017,615
New Turkish Lira	264,410	21,634,901		21,899,311
New Zealand Dollar	76,460	4,171,770		4,248,230
Norwegian Krone	14,630	4,783,021		4,797,651
Philippines Peso	18,703	5,732,007		5,750,710
Polish Zloty	12		6,257,328	6,257,340
South African Rand	131,167	50,008,314		50,139,481
Singapore Dollar	648,133	23,758,667	6,083,536	30,490,336
South Korean Won	58,729	104,658,602		104,717,331
Swedish Krona	409,661	15,382,247		15,791,908
Swiss Franc	101,102	99,653,605		99,754,707
Thailand Baht	149,894	38,822,728		38,972,622
Zimbabwe Dollar		373,401		373,401
Total securities subject to foreign currency risk	$ 11,426,513	$ 1,865,320,994	$ 311,550	1,877,059,057
Reconciling Items:				
401(k) Total Return Fund				(31,456,702)
Short sale liability				57,484,955
Reverse repurchase liability				2,228,703
Other				94,318
Total				$ 1,905,410,331

4. ASSETS USED IN PLAN OPERATIONS

Assets used in plan operations at June 30, 2005, consist of the following:

Buildings and improvements	$ 5,449,460
Less: accumulated depreciation	(2,527,232)
	2,922,228
Computer software development	6,331,360
Less: accumulated amortization	(5,743,765)
	587,595
Equipment	6,807
Less: accumulated depreciation	
	6,807
Total assets used in plan operations	$ 3,516,630

For the year ended June 30, 2005, depreciation expense on the buildings and improvements was $152,762, and amortization expense on the computer software development costs was $908,379. The equipment was purchased in May 05, but not put into service until FY06. The depreciation and amortization costs are included in administrative expenses.

5. CONTRIBUTIONS

The System's funding policy for the PERSI Base Plan and FRF is determined by the Board within limitations, as defined by Idaho law. The funding policy provides for periodic employer contributions at actuarially determined rates that, expressed as percentages of annual covered payroll, are adequate to accumulate sufficient assets to pay benefits when due. Level percentages of payroll employer contribution rates are determined using the Entry Age Actuarial Cost Method for the PERSI Base Plan and a modified aggregate funding method for FRF. Under the Entry Age Actuarial Cost Method, the actuarial present value of the projected benefits of each individual included in the actuarial valuation is allocated on a level basis over the earnings of the individual between entry age and assumed exit age. FRF amortizes the difference between the value of the FRF benefits not provided by the Base Plan and the FRF assets over the earnings of all firefighters. The PERSI Base Plan amortizes any unfunded actuarial accrued liability based on a level percentage of payroll. FRF amortizes any unfunded liability based on a level dollar amount. The maximum amortization period for the Base Plan permitted under Section 59-1322, Idaho Code, is 25 years. The maximum amortization period for FRF permitted under Section 59-1394, Idaho Code, is 50 years. The payroll for employees covered by the PERSI Base Plan and FRF was approximately $2,176,000,000 and $43,000,000, respectively.

Actuarial valuations of the PERSI Base Plan and FRF are performed annually. The last valuations were performed as of July 1, 2005.

Normal cost is 14.03% of covered payroll and the amount available to amortize the unfunded actuarial liability is 4.79% of covered payroll for the PERSI Base Plan. There is no normal cost associated with FRF, and all contributions to FRF are available to pay benefits and reduce the unfunded actuarial liability. Police and Fire employers' contribution rates increased 1/10% effective July 1, 2003, as a result of a new death benefit. The PERSI Board also approved a contribution rate increase of 1% per year for 3 years beginning July 1, 2004, for a total increase of 3% split between employers and employees. The rate increases scheduled to begin July 1, 2005 and July 1, 2006, were postponed for two years.

The contribution rates for the year ended June 30, 2005, and subsequent years through June 30, 2008, are as follows:

Optional retirement plan employees of higher education:

Colleges and universities	3.03 %
Junior colleges	3.83 %

	Active Members		Employers	
	General/ Teacher	Fire/ Police	General/ Teacher	Fire/ Police
Current contribution rate effective July 1, 2004	6.23 %	7.65 %	10.39 %	10.73 %
Increase effective July 1, 2005 and 2006	Postponed for two years			
Next planned rate increases:				
Increase effective July 1, 2007	0.37 %	0.44 %	0.61 %	0.61 %
Rate July 1, 2007	6.60 %	8.09 %	11.00 %	11.34 %
Increase effective July 1, 2008	0.37 %	0.44 %	0.61 %	0.61 %
Rate July 1, 2008	6.97 %	8.53 %	11.61 %	11.95 %

FRF employer and employee contribution rates for firefighters hired before October 1, 1980, are 25.89% and 3.80%, respectively, in addition to the PERSI Police and Fire rates shown above. The employer contribution rate for firefighters hired after October 1, 1980, is 17.24%, in addition to the PERSI Police and Fire rate shown above. FRF employer rates increased along with the PERSI Base Plan rates in FY 2005, and are scheduled to increase in 2007 and 2008.

6. PENSION PLAN PARTICIPATION

The System participates as an employer in the PERSI Base Plan, a cost sharing multiple-employer public retirement system, which was created by the Idaho State Legislature. It is a defined benefit plan requiring that both the member and the employer contribute. The Plan provides benefits based on members' years of service, age, and compensation. In addition, benefits are provided for disability, death, and survivors of eligible members or beneficiaries. The authority to establish and amend benefit provisions is established in Idaho Code. Designed as a mandatory system for eligible state and school district employees, the legislation provides for other political subdivisions to participate by contractual agreement with the System. Financial reports for the Plan are available from the System upon request.

After five years of credited service, members become fully vested in retirement benefits earned to date. Members are eligible for retirement benefits upon attainment of the ages specified for their employment classification. For each month of credited service, the annual service retirement allowance is 2.0% (2.3% police/firefighter) of the average monthly salary for the highest consecutive 42 months.

The contribution requirements of the System and its employees are established and may be amended by the PERSI Board of Trustees. For the year ended June 30, 2005, the required contribution rate was 6.23% for general members and 7.65% for police/fighters. The employer rate as a percentage of covered payroll was 10.39% for general members and 10.73% for police/fighter members. PERSI contributions required and paid were $392,003, $361,053, and $341,595 for the three years ended June 30, 2005, 2004, and 2003 respectively.

7. COMMITMENTS

The accrual basis of accounting provides that expenses include only amounts associated with goods and services received and liabilities include only the unpaid amounts associated with such expenses. Accordingly, the System had committed approximately $653,400 in outstanding purchase orders and purchase commitments to fund ongoing administrative projects for the System. These amounts are not reported in the basic financial statements at June 30, 2005.

The System had private equity commitments as of June 30, 2005, of $518,447,933, of which $307,975,041 of funding had been provided, leaving an unfunded commitment of $210,472,892 at fiscal year end. The System also had a private real estate commitment as of June 30, 2005 for an amount of $168,000,000. Funding of $42,326,952 had been provided by the end of FY 2005, leaving an unfunded commitment of $125,673,048.

* * * * * *

REQUIRED SUPPLEMENTARY INFORMATION

PUBLIC EMPLOYEE RETIREMENT SYSTEM OF IDAHO

SCHEDULES OF FUNDING PROGRESS—PUBLIC EMPLOYEE RETIREMENT FUND AND FIREFIGHTERS' RETIREMENT FUND FISCAL YEARS 2000–2005 (Dollars in millions)

PERSI

Actuarial Valuation Date	(1) Actuarial Value of Assets	(2) Actuarial Accrued Liability (AAL) (a.)	(3) PV of Future ORP Contributions	(4) Unfunded AAL (UAAL) (2) - (1) - (3) (b.)	(5) Funded Ratios (1) : [(2) - (3)] (c.)	(6) Annual Covered Payroll (d.)	(7) UAAL as a Percentage of Covered Payroll (4) : (6)
July 1, 2000	$ 7,032.9	$ 6,105.1	$ 70.5	$ (998.3)	116.5 %	$ 1,827.2	(54.6)%
July 1, 2001	6,492.8	6,751.3	72.2	186.3	97.2	1,975.3	9.4
July 1, 2002	6,062.1	7,209.5	71.7	1,075.7	84.9	2,047.1	52.5
July 1, 2003	6,297.8	7,578.8	66.4	1,214.6	83.8	2,057.7	59.0
July 1, 2004	7,420.2	8,154.8	63.5	671.1	91.7	2,115.4	31.7
July 1, 2005	8,208.8	8,778.7	61.3	508.6	94.2	2,208.7	23.0

(a.) Actuarial present value of benefits less actuarial present value of future normal costs based on entry age actuarial cost method.

(b.) Actuarial accrued liabilities less actuarial value of assets and present value of future ORP contributions. Amounts reported in this table do not include the value of the discretionary COLA or Gain Sharing allocations granted after the valuation date. If negative, amount is referred to as a funding reserve.

(c.) Funded Ratio is the ratio of the actuarial value of assets over the actuarial accrued liabilities less the present value of future ORP contributions.

(d.) Covered Payroll includes compensation paid to all active employees on which contributions are calculated.

FRF

Actuarial Valuation Date	(1) Actuarial Market Value of Assets	(2) Actuarial Accrued Liability (AAL)	(3) Unfunded AAL (UAAL) (2) - (1)	(4) Funded Ratios (1) : (2)	(5) Annual Covered Payroll (e.)	(6) UAAL as a Percentage of Covered Payroll (3) : (5)
July 1, 2000	$ 217.8	$ 293.4	$ 75.6	74.2 %	$ 30.8	245.5 %
July 1, 2001	200.4	316.2	115.8	63.4	32.9	352.0
July 1, 2002	181.5	300.3	118.8	60.4	34.4	345.3
July 1, 2003	182.7	310.7	128.0	58.8	37.0	345.9
July 1, 2004	210.4	302.6	92.2	69.5	39.8	231.7
July 1, 2005	227.2	309.1	81.9	73.5	42.2	194.1

(e.) Annual covered payroll includes compensation paid to all active firefighters hired prior to October 1, 1980. Annual Covered Payroll differs from Active Member Valuation Payroll, which is an annualized compensation of only those members who were active on the actuarial valuation date.

PUBLIC EMPLOYEE RETIREMENT SYSTEM OF IDAHO

SCHEDULES OF EMPLOYER CONTRIBUTIONS—PUBLIC EMPLOYEE
RETIREMENT FUND AND FIREFIGHTERS' RETIREMENT FUND
FISCAL YEARS 2000—2005 (Dollars in millions)

	PERSI Employer Contributions			FRF Employer Contributions (c.)		
Year Ended June 30	Total Employer Contributions (Statutory) (a.)	Annual Required Contribution (ARC) (b.)	Percentage Contributions	Total Employer Contributions	Annual Required Contribution	Percentage Contributions
2000	$ 182.9	$ 155.7	117.5 %	$ 8.7	$ 8.6	100.4 %
2001	197.9	152.2	130.0	9.2	6.3	147.3
2002	205.5	155.1	132.5	9.6	9.3	102.2
2003	206.7	188.3	110.0	10.1	9.5	107.1
2004	212.6	218.8	97.0	11.7	10.2	114.9
2005	236.2	236.7	100.0	11.7	7.2	162.3

(a.) For 2001, this includes $77,690,500 of gain sharing credits. Actual cash contributions were $120,220,992.

(b.) For PERSI employers, the Annual Required Contribution (ARC) is equal to the normal cost rate plus a 25-year amortization of any Unfunded Actuarial Accrued Liability or minus a 25-year amortization of any Funding Reserve amount. The ARC determined as of the valuation date is applicable for employers' fiscal years commencing October 1, of the calendar year following the valuation date. For Optional Retirement Plan (ORP) employers, the ARC is equal to 3.03% of salaries of university members in the ORP until 2015 and 3.83% of salaries of junior college members in the ORP until 2011.

PUBLIC EMPLOYEE RETIREMENT SYSTEM OF IDAHO

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
YEAR ENDED JUNE 30, 2005

1. ACTUARIAL INFORMATION

The information presented in the required supplementary information was prepared for GASB disclosure purposes and may differ from the funding determination as of the dates indicated. Additional information as of the latest actuarial valuation for GASB purposes is as follows:

	PERSI	**FRF**
Valuation date	July 1, 2005	July 1, 2005
Actuarial cost method	Entry age actuarial cost	Entry age actuarial cos
Amortization method	Level percentage of projected payroll—open	Level dollar amount—closed
Remaining amortization period	25 years	31 years
Asset valuation method	Market value	Market value
Actuarial assumptions:		
Investment rate of return	7.75 %	7.75 %
Projected salary increases—	5.0 % – 11.5 %	4.50 %
Includes salary inflation	4.50 %	4.50 %
Postretirement benefit increase	1.00 %	4.50 %
Implied price inflation rate	3.75 %	3.75 %

ADDITIONAL SUPPLEMENTARY SCHEDULES

PUBLIC EMPLOYEE RETIREMENT SYSTEM OF IDAHO

SCHEDULE OF INVESTMENT EXPENSES
FOR THE YEAR ENDED JUNE 30, 2005

INVESTMENT AND RELATED SERVICES:	
Adelante Capital (formerly Lend Lease Rosen)	$ 2,287,677
Apollo Management	142,560
Baring Asset Management, Inc.	1,359,486
Sanford C. Bernstein	2,164,006
Bloomberg, LP	54,963
Brandes Investment Partners, LP	1,750,142
Bridgewater Associates	417,398
Callan Associates	238,525
Capital Guardian Trust Company	1,155,848
Chadwick, Saylor & Co., Inc.	181,779
Chisholm Partners, LP	406,362
Choice Plan Managers	163,989
Clearwater Advisors, LLC	369,817
D.B. Fitzpatrick & Co., Inc.	1,532,708
Donald Smith & Company	1,291,362
Fidelity Management Trust Company	306,627
Frazier Technology Ventures	84,377
Furman Selz Investments	8,954
Galen Associates	635,967
Genesis Asset Managers, Ltd.	1,495,139
Goense Bounds & Partners, LP	146,680
Gores Capital Partners	(16,829)
Green Equity Investors	204,078
Hamilton Lane Advisors, Inc.	263,805
Highway 12	207,793
Kohlberg & Co., LLC	204,348
Littlejohn & Company	231,558
Mellon Capital Management	627,842
Mellon Trust	2,663,549
Mondrian Investment Partners	644,163
Mountain Pacific Investment Advisors, Inc.	878,031
Navis Partners, LP	182,891
Pareto Partners	824,396
Peregrine Capital	630,249
Providence Investments	394,094
Prudential Investments	367,441
R.V. Kuhns & Associates	(3,562)
Rowe Price International, Inc.	979,733
Societe Generale	1,061,443
State Street Global Advisors	354,602
T3 Partners II, LP	419,155
TCW Asset Management	972,989
Thomas H. Lee	40,133

(Continued)

PUBLIC EMPLOYEE RETIREMENT SYSTEM OF IDAHO

SCHEDULE OF INVESTMENT EXPENSES
YEAR ENDED JUNE 30, 2005

INVESTMENT AND RELATED SERVICES (Continued):	
Tukman Capital Management, Inc.	$ 1,351,188
W. Capital Partners	298,800
Wells Fargo Bank	65,800
Western Asset Management	244,893
Zesiger Capital Group	1,383,691
	31,670,640
CONSULTING SERVICES:	
Calhoun Law Group	5,525
CT Corporation	327
Deloitte & Touche LLP	59,350
Joseph L. Wyatt	425
Mellon Human Resources & Investor Solutions	1,378,783
Morrison & Foerster	1,000
Foster, Pepper, Shefelman PLLC	313,235
Milliman, Inc.	263,596
	2,022,241
	$ 33,692,881

(Concluded)

PUBLIC EMPLOYEE RETIREMENT SYSTEM OF IDAHO

SCHEDULE OF ADMINISTRATIVE EXPENSES
FOR THE YEAR ENDED JUNE 30, 2005

	PERSI Base Plan
PORTFOLIO-RELATED EXPENSES:	
Personnel expenses	$ 404,358
Operating expenses	137,946
Capital outlay	2,894
	545,198
OTHER ADMINISTRATIVE EXPENSES:	
Personnel expenses	2,823,473
Operating expenses	2,595,284
Capital outlay	90,498
Building depreciation expense	152,762
Software amortization expense	908,379
	6,570,396
SICK LEAVE-RELATED EXPENSES—Administrative operating expenses	53,660
	$7,169,254

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INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED UPON AN AUDIT PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Retirement Board of
Public Employee Retirement System of Idaho
Boise, Idaho

We have audited the financial statements of the Public Employee Retirement System of Idaho (the "System") as of and for the year ended June 30, 2005, and have issued our report thereon dated October 19, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the System's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Retirement Board and management and is not intended to be and should not be used by anyone other than these specified parties.

October 19, 2005