

Dirk Kempthorne, Governor, State of Idaho

**RETIREMENT BOARD**



**Jody B. Olson, Chairman**  
Term expires July 1, 2007



**Pamela I. Ahrens**  
Term expires July 1, 2008



**Jeff Cilek**  
Term expires July 1, 2010



**Clifford T. Hayes**  
Term expires July 1, 2009



**J. Kirk Sullivan**  
Term expires July 1, 2006

**PERSI EXECUTIVE STAFF**

Alan H. Winkle, Executive Director  
Robert M. Maynard, Chief Investment Officer  
John R. Doner, Deputy Director  
James E. Monroe, Financial Officer  
Judy Aitken, Answer Center Manager  
Susan Shaw, Processing Center Manager  
Patrice Perow, Communications Manager  
Carol Boylan, Information Technology Manager  
Diane Berg, Defined Contribution Manager  
Brad Goodsell, Deputy Attorney General

**PROFESSIONAL CONSULTANTS**

Actuary: Milliman, Inc., Seattle, WA

Auditor: Deloitte & Touche LLP, Boise, ID

Medical: VPA, Inc., Calabasas, CA

Investment: Callan Associates, Inc., San Francisco, CA  
 CS Capital Management, Inc., Atlanta, GA  
 GMAC Institutional Advisors, San Francisco, CA  
 Hamilton Lane Advisors LLC, Philadelphia, PA

Legal: Calhoun Law Group, Washington, DC  
 Foster, Pepper & Shefelman PLLC, Seattle, WA

Other: ACS Human Resources & Investor Solutions, Pittsburgh, PA  
 Mellon Transition Management Services, San Francisco, CA

Investment Custodians: Mellon Global Security Services, Pittsburgh, PA  
 Wells Fargo Bank of Idaho, Boise, ID

**Investment Managers:**

Adelante Capital Management LLC, Berkeley, CA Apollo Management, LP, Purchase, NY Baring America Asset Management, Inc., Boston, MA Brandes Investment Partners, LP, San Diego, CA Bridgewater Associates, Inc., Westport, CT Capital Guardian Trust Company, Brea, CA Chisholm Partners, LP, Providence, RI Clearwater Advisors LLC, Boise, ID D.B. Fitzpatrick & Co., Inc., Boise, ID Donald Smith & Co., Inc., New York, NY Fidelity Management Trust Company, Boston, MA Frazier Technology Ventures, LP, Seattle, WA Furman Selz Investors, LP, New York, NY Galen Partners, LP, New York, NY Genesis Asset Managers, Ltd., London Goense Bounds & Partners, LP, Lake Forest, IL Gores Capital Partners, LP, Los Angeles, CA Green Equity Investors, LP, Los Angeles, CA Hamilton Lane Secondary, LLC, Baja Cynwyd, PA Harvest Partners, Inc. LP, New York, NY Highway 12 Venture Fund, LP, Boise, ID Ida-West Energy Fund LLC, Boise, ID Kohlberg & Co., LLC, Mt. Kisko, NY Koll Company, LLC, Newport Beach, CA Koll/PER, LLC, Newport Beach, CA	Littlejohn Fund, LP, Greenwich, CT McCown DeLeeuw & Co., LP, Menlo Park, CA Mellon Capital Management, San Francisco, CA Mondrian Investment Partners, Ltd., London Mountain Pacific Investment Advisers, Inc., Boise, ID Nautic Partners, LLC, Providence, RI Oaktree Capital Management, LLC, Los Angeles, CA Pareto Partners, LLC, London Peregrine Capital Management, Inc., Minneapolis, MN Providence Equity Partners, LP, Providence, RI Prudential Investment Management LLC, Newark, NJ Sanford C. Bernstein & Co., LLC, New York, NY Saugatuck Capital Company, LP, Stamford, CT Societe Generale Asset Management Intl, Ltd., London State Street Global Advisors, Boston, MA T. Rowe Price International, Inc., London T3 Partners, LP, Fort Worth, TX TCW Asset Management Co., Los Angeles, CA Thomas H. Lee Equity Fund, LP, Boston, MA TPG Partners, LP, Fort Worth, TX Tukman Capital Management, Inc., Larkspur, CA W. Capital Partners, LP, New York, NY Western Asset Management Co., Pasadena, CA Zesiger Capital Group LLC, New York, NY
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Specific information about the investment managers can be found on pages 65-66 in the Investment Section of this report.

# Certificate of Achievement for Excellence in Financial Reporting

Presented to

## Public Employee Retirement System of Idaho

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
June 30, 2004

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



*Nancy L. Ziehl*

President

*Jeffrey R. Emswiler*

Executive Director



Public Pension Coordinating Council  
**Public Pension Standards**  
**2005 AWARD**

Presented to

**Public Employee Retirement System of Idaho**

In recognition of meeting professional standards for  
plan design and administration as  
set forth in the Public Pension Standards.

*Presented by the Public Pension Coordinating Council, a confederation of*

National Association of State Retirement Administrators (NASRA)  
National Conference on Public Employee Retirement Systems (NCPERS)  
National Council on Teacher Retirement (NCTR)

A handwritten signature in black ink that reads "Alan H. Winkle". The signature is written in a cursive, flowing style.

Alan H. Winkle  
Program Administrator

## ORGANIZATIONAL CHART

### Retirement Board

**Alan H. Winkle**  
Executive Director

**John R. Doner**  
Deputy Director

**Brad Goodsell**  
Deputy Attorney General

**Joanne Ax**  
Management Assistant

**Robert M. Maynard**  
Chief Investment Officer

**Richelle Sugiyama**  
Investment Officer

**Rose Marie Sawicki**  
Administrative Assistant 1

**Investment Managers**  
See Investment Section for a list of managers – page 65

**James E. Monroe**  
Financial Officer

**Rhonda Yadon**  
Senior Accountant  
**Cecile McMonigle**  
Portfolio Accountant  
**Tess Myers**  
Administrative Assistant 1

**JoAnne Dieffenbach**  
Financial Technician  
**Sharon Simon**  
Financial Support Technician

**Debbie Buck**  
Employer Services Supervisor  
**Jaimie Hiskey**  
Financial Technician  
**Suzanne Jewell**  
Financial Technician  
**Vacant**  
Office Specialist 1

**Alan Roberts**  
Financial Technician  
**Pam Fowers**  
Financial Technician  
**Barbara Weirick**  
Financial Technician  
**Alice Brown**  
Financial Technician

**Carol Boylan**  
Information Technology Manager

**Kris Colt**  
IT Information System Tech Sr.  
**Nancy Fauver**  
IT Database Analyst

**Joy Fereday**  
IT Programmer Analyst Sr.  
**Stacy Jones**  
IT Program System Specialist

**Ryan Evey**  
IT Programmer Analyst Sr.  
**Stacy Parr**  
Web Developer

**Tim Thuis**  
IT Production Specialist  
**Vacant**  
IT Network Analyst

**Judy Aitken**  
Answer Center Manager

**Roger Bartlett**  
Member Services Rep  
**Kari Caven**  
Member Services Rep  
**Catherine Atchison**  
Member Services Rep

**Vacant**  
Member Services Rep  
**Lisa Conn**  
Member Services Rep  
**Lisa Mabe**  
Member Services Rep

**Kathi Kaufman**  
Customer Service Rep. 2  
**Alicia Harper**  
Customer Service Rep. 2  
**Lynne Yowell**  
Customer Service Rep. 2  
**Karen Miller**  
Customer Service Rep. 2

**Denice Desilet**  
Customer Service Rep. 2  
**Gerry Sjol**  
Customer Service Rep. 2  
**Stacey Hoffman**  
Customer Service Rep. 2  
**Jami Davis**  
Administrative Assistant 1

**Susan Shaw**  
Processing Center Manager

**Penny Walls**  
Member Services Rep.  
**Julisa Adams**  
Member Services Rep.  
**Susan Strouth**  
Member Services Rep.  
**Lynn Duncan**  
Member Services Rep.

**Lenna Strohmeyer**  
Technical Records Spec. 1  
**Kay Prince**  
Technical Records Spec. 1  
**Marian Van Gerpen**  
Technical Records Spec. 1

**Heidi Andrade**  
Technical Records Spec. 1  
**Shasta Luper**  
Technical Records Spec. 1

**Cathy Andrews**  
Imaging Specialist

**Patrice Perow**  
Communications Manager

**Bill Duncan**  
Training Specialist

**Maxine Thomas**  
Training Specialist

**Diane Berg**  
Defined Contribution Manager

**Betsy Griffith**  
Administrative Assistant 1

## **THE SYSTEM**

The Public Employee Retirement System of Idaho (the System) is the administrator of five pension funds 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 Plan 401(k) and 414(k) (PERSI Choice Plans) and the Sick Leave Insurance Reserve Fund.

The Retirement Board consists of five members, each appointed by the Governor to fulfill a 5-year term. The Board meets monthly to conduct System business, usually on the fourth Tuesday of each month at 8:30 a.m. at PERSI's Boise office.

Administrative expenditures consisting of the personnel costs, operating expenditures, and capital outlay necessary to operate the System are limited to those approved and appropriated by the Legislature for that purpose. In fiscal year 2005 (FY05), these costs totaled \$7,115,594 for the defined benefit retirement plans, including \$152,762 in depreciation and \$908,379 in amortization expense, which are not cash expenditures and, therefore, not appropriated. The defined contribution retirement plan investment expenses are not included because they are paid by the plan members.

The majority of the System's 63 staff works in the headquarters office at 607 North 8<sup>th</sup> Street, Boise, Idaho. There are two staff members in the Coeur d' Alene office, and three in the Pocatello office. The Executive Director and investment personnel are exempt positions appointed by the Retirement Board to serve at its pleasure. The Deputy Director is an exempt position serving under the Executive Director. All other staff members serve under statutes and personnel rules governing classified state service.

The System staff oversees the investment of the trust corpus and new contributions with professional investment managers and funding agents. The Retirement Board maintains fiduciary responsibility for investment policy, asset allocation, and the selection of individual investment managers as discussed in the Investment Section.

## **SUMMARY OF PLAN PROVISIONS**

### **DEFINED BENEFIT "BASE PLAN" PROVISIONS**

Note: The items in parentheses are the provisions applicable to members designated as either PERSI firefighters or as PERSI police officer members for retirement purposes.

### **MEMBER CONTRIBUTION RATE**

The employee contribution rate is set by statute at 60% (72%) of the employer rate. As of June 30, 2005, it was 6.23% (7.65%).

### **EMPLOYER CONTRIBUTION RATE**

The employer contribution rate set by the Retirement Board was 10.39% (10.73%) as of June 30, 2005.

### **SERVICE RETIREMENT**

#### ***ELIGIBILITY***

Five years of service and age 65 (60, or between 60 and 65, depending on the ratio of police officer/firefighter service to total credited service).

**AMOUNT OF ALLOWANCE**

For each year of credited service, the monthly service retirement allowance as of June 30, 2005, was 2% (2.3%) of the monthly average salary of the member's highest 42 consecutive months.

**MINIMUM MONTHLY BENEFIT ALLOWANCE**

Until February 28, 2005: for each year of service, the monthly minimum benefit allowance was \$20.25 (\$24.30) to a maximum of the member's accrued benefit. Effective March 1, 2005: the monthly minimum benefit allowance was \$20.96 (\$25.15).

**NORMAL FORM**

Regular retirement allowance for retiree's life only, plus a lump sum death benefit if the retiree dies before allowances are paid, total accumulated employee contributions and interest.

**OPTIONAL FORMS**

Retirees may also choose 50% or 100% contingent annuitant options as well as Social Security "bridge" options. These are actuarial equivalents of the normal form based on the mortality and interest assumptions adopted by the Retirement Board. The allowance is payable for the life of the retiree and designated contingent annuitant.

**EARLY RETIREMENT**

**ELIGIBILITY**

Five years of service and age 55 (50, or between 50 and 55, depending on the ratio of police officer/firefighter service to total credited service).

**AMOUNT OF ALLOWANCE**

Unreduced accrued service retirement allowance if age plus service, upon separation from employment, total 90 (80, or between 80 and 90, depending on the ratio of police officer/firefighter service to total credited service); otherwise, the accrued service retirement allowance is reduced 3% for each of the first 5 years by which the early retirement date precedes the date the member would be eligible to receive the unreduced benefit, and by 5.75% for each additional year to a maximum of a second 5 years. The unreduced benefit entitlement may be either at the service retirement eligibility date or the date eligible for the rule of 90(80).

**FORMS**

Regular retirement allowance; contingent annuitant allowances for the life of the retiree and a designated contingent annuitant; Social Security level income option for the life of the retiree only or for the life of the retiree and designated survivor.

**DISABILITY RETIREMENT**

**ELIGIBILITY**

Active members must have 5 years of service, be unable to perform work of *any* kind, and be expected to remain disabled for life. They are eligible from first day on the job if the disability is due to occupational causes.

**AMOUNT OF ALLOWANCE**

Projected service retirement allowance based on the highest 42 consecutive month average salary at the time of disability. The benefit is calculated using the accrued service at the time of disability plus the service which would have accrued through service retirement age had the disability not occurred. If a member has less than 360 months of service as of the date he is eligible for disability retirement, he will be given credit for the months of service he would have earned from the date of disability to the date he would have reached Service Retirement Age (65 for general members/62 for police and firefighters) had he not become disabled (360 months of credited service maximum). In other words, PERSI will give members up to 30 years of credit or to Service Retirement Age, whichever comes first. Monthly allowance is payable after all

## **Introductory Section**

temporary compensation ceases and is offset by the amount payable as income benefit under worker's compensation law, except when offset by Social Security.

### ***NORMAL FORM***

Regular retirement allowance to normal service retirement age when retirement benefit changes to service retirement allowance with its optional forms available.

## **DEATH BENEFITS**

### ***AFTER RETIREMENT***

Under the normal form of the retirement allowance, a Social Security adjustment option, or a disability retirement, the balance, if any, of the member's accumulated contributions and interest at retirement over all payments received is paid to the beneficiary in a lump sum. In the case of a disability retirement, the beneficiary may waive the lump sum if the retiree is married so that the spouse will receive a lifetime monthly allowance, or the beneficiary may take a lump-sum payment of two times the amount in the member's account at the time of disability retirement minus any amount paid. Under the contingent annuitant options, the designated annuitant receives a lifetime monthly benefit following the member's death. If the survivor dies before the balance of the member's accumulated contributions and interest has been paid, the balance will be paid to the beneficiary in a lump sum. If the member's designated contingent annuitant predeceases him/her, the member's allowance will be recalculated to a single life payment.

### ***BEFORE RETIREMENT***

- 1 Non-vested Members: Beneficiary receives a lump sum payment of the member's accumulated contributions plus interest.
  
- 2 Vested Members:
  - a Beneficiary receives a lump sum payment of two times the member's accumulated contributions plus interest.
  - b If the member is married, and the spouse is the sole beneficiary, the spouse may select a lump sum payment or a lifetime monthly benefit.
  - c If the member is married, but the spouse is not the sole beneficiary, the beneficiary may waive the lump sum, in which case, a lifetime monthly benefit is available to the surviving spouse.
  
- 3 A \$100,000 death benefit for duty-related deaths for police officers/firefighters became effective July 1, 2003.

## **SEPARATION BENEFIT**

Accumulated member contributions with regular interest is payable upon becoming an inactive member separated from eligible employment. The Regular Interest Rate in effect for FY05 was 3.22% per year compounded monthly from July 1, 2004 through December 31, 2004, and 17.51% from January 1, 2005 through June 30, 2005.

## **POSTRETIREMENT ADJUSTMENTS**

An annual postretirement adjustment based on and limited by a cost-of-living factor reflecting the changes in the Consumer Price Index (CPI) is effective in March each year. If the CPI change from August of the previous year to August of the second previous year is 1% or more, a 1% mandatory adjustment is made. The Board may authorize additional discretionary adjustments based on the CPI increase (up to a total maximum annual COLA of 6% or the CPI rate, whichever is lower) if it determines that the System can do so and still maintain an appropriately funded position as required by Idaho Code Section 59-1355(1). Adjustments in excess of the 1% authorized by the Board must be reported to the Legislature. If the Legislature has not acted by the 45<sup>th</sup> day of the legislative session, the COLA becomes effective March 1 of each year.



## **Introductory Section**

The Board is also authorized to award postretirement adjustments for prior years in which the actual amount of adjustment was less than the CPI for those years. If the CPI change is downward, in no event will any benefit be reduced below its initial amount.

The COLA authorized and implemented March 1, 2005, was 2.7% plus a retro COLA of 0.8%.



Governor  
Dirk Kempthorne

Retirement Board  
Jody B. Olson,  
Chairman  
Pamela I. Ahrens  
Jeff Cilek  
Clifford T. Hayes  
J. Kirk Sullivan

Executive Director  
Alan H. Winkle

**BOISE**  
Mailing Address  
P.O. Box 83720  
Boise, ID 83720-0078

Office Address  
607 North 8th Street  
Boise, ID 83702-5518

208-334-3365  
1-800-451-8228  
FAX 208-334-3805

**POCATELLO**  
Mailing Address  
P.O. Box 1058  
Pocatello, ID 83204

Office Address  
850 East Center, Ste.  
"D"  
Pocatello, ID 83201

208-236-6225  
1-800-762-8228  
FAX 208-236-6159

**COEUR D' ALENE**  
Mailing & Office  
Address  
2005 Ironwood Pkwy.  
Coeur d' Alene, ID  
83814

208-769-1474

November 30, 2005

Dear Governor Dirk Kempthorne, Legislators, and Members of the Retirement System:

We are pleased to present to you the Public Employee Retirement System of Idaho (the System) comprehensive annual financial report, for the fiscal year ended June 30, 2005 (FY 2005). This financial report is a historical perspective of benefits, services, and fiscal activities of the System. Included is a summary of our actuarial valuations, an independent auditors' report, an investment summary, and a statistical section.

Generally accepted accounting principles require management to provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement the MD&A and should be read in conjunction with it. The System's MD&A can be found immediately following the independent auditors' report.

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to PERSI for its comprehensive annual financial report for the fiscal year ended June 30, 2004. This was the 14<sup>th</sup> consecutive year PERSI has achieved this prestigious award. To be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe that our current comprehensive annual financial report continues to meet the Certificate of Achievement Program's requirements, and we are submitting it to GFOA to determine its eligibility for another certificate.

#### REPORT STRUCTURE

This FY 2005 comprehensive annual financial report has five sections:

Introductory Section contains this letter of transmittal plus an overview of the fund.

Financial Section contains the independent auditors' report, management's discussion and analysis, the financial statements, and supplementary data.

Investment Section contains the funds' investment performance, strategy, and guidelines.

Actuarial Section contains the consulting actuary's certification letter and a summary of the results of the actuarial valuations and related data.

Statistical Section contains tables of significant data.

This Letter of Transmittal is intended to serve as an overview of the System and to "transmit" information on the topics that follow.

## **PLAN HISTORY**

The Public Employment Retirement System of Idaho (PERSI) was created by the Thirty-seventh Legislature, Regular Session of 1963 with funding effective July 1, 1965. It is a tax qualified, defined benefit system to which both the member and the employer contribute. Participation in the System is mandatory for eligible state and school district employees and available to other public employers and their employees on a contractual basis.

When the Teachers Retirement System of Idaho was abolished, members of that system were integrated into PERSI, and all other eligible school district employees became PERSI members effective July 1, 1967.

Legislative amendments since 1965 have made it possible for municipal police officer retirement funds to merge with the System, and two of the five police officer systems have since merged. The other three are being phased out, and police officers hired since 1969 have become PERSI members.

Legislation in 1979 mandated the Firefighters' Retirement Fund be administered by PERSI effective October 1, 1980. Paid firefighters who were members of the original system retained their original benefit entitlement, while paid firefighters hired after October 1, 1980, were entitled to PERSI benefits. An actuarial valuation of the firefighter member benefit entitlement is conducted every year, separate from the annual PERSI valuation.

In January 2001, PERSI implemented a "Gain Sharing" program as a way to distribute \$155 million in excess investment earnings back to our active members, retirees, and employer members. Retirees received their gain sharing as a "13<sup>th</sup> check." Employers received their share as a contribution "holiday." Some 53,000 eligible active members received their portion as deposits into newly created defined contribution (DC) accounts. This new plan, called the PERSI "Choice" Plan, supplemented PERSI's traditional Defined Benefit (DB) "Base" Plan. It allowed employees for the first time to actively participate in saving for their retirement.

The Choice Plan is somewhat unique in the public sector. PERSI obtained permission from the Internal Revenue Service to expand a grandfathered State 401(k) to our members statewide. While some public employees were familiar with 457 or 403(b) plans, a 401(k) was something new to them. Many of our members had never had the opportunity to make such pre-tax voluntary contributions.

## **SERVICES PROVIDED**

The ability of the System to serve both employee and employer members at the local level through the Boise, Pocatello, and Coeur d' Alene offices remains a key factor for efficient administration. The merging of other retirement systems with PERSI, plus statutory amendments over the years, have produced both multiple and diverse member benefit entitlements and administrative requirements. These can best be analyzed and explained to the members through personal contact with knowledgeable System staff members.

In its 40<sup>th</sup> year of operation, the System continued a wide range of services to both employee and employer members. Members may visit the PERSI website, call, e-mail, or visit one of the three offices for personal information and assistance regarding credited service, account balances, eligibility, benefit options and amounts, and other retirement matters.

Members receive advance notice of service retirement qualification and are provided with estimates of monthly allowances. They also receive information regarding the availability of alternate forms of retirement payments. Retirement applications are processed in a timely fashion, and monthly payments are made promptly. Direct deposit of benefit payments is available to retired members as is withholding for income tax, medical insurance, or other purposes.

## **Introductory Section**

System retirees are provided notices whenever their net benefit amount changes. This notice gives retirees a list of their itemized deductions from their gross benefit.

Separation and death benefits are paid in an orderly manner and as rapidly as possible. In some instances payments are expedited to avoid placing a financial hardship on a member. Employee contributions and earned interest are posted to individual member accounts each month, and an annual statement is provided to each member confirming their average monthly salary, credited service, contributions, and earned interest. In addition, a report of benefits accrued to date is provided along with an estimate of benefits projected ahead to various retirement ages.

The staff of employer units responsible for reporting and handling retirement transactions and activities is provided regular training and assistance through monthly newsletters and personal contact by field service personnel as needed. Employer records and reporting procedures are reviewed each year for accuracy and compliance with statutory provisions.

Upon request, public employers interested in affiliation with the System are counseled and provided with information regarding employee benefits, cost, and procedures associated with joining. Conversely, employers considering withdrawal are provided information and employee benefit projections to enable them to make an informed decision.

Pre-retirement and financial planning workshops, offered on a regular basis throughout the State, cover financial planning, budgeting, investment basics, Social Security, and System benefits.

### **EMPLOYEE AND EMPLOYER MEMBERSHIP**

During FY 2005, the number of active PERSI members increased from 63,385 to 64,391. The number of retired members or annuitants receiving monthly allowances increased from 26,043 to 27,246. The number of inactive members who have not been paid a separation benefit increased from 18,837 to 20,028. Of these inactive members, 8,460 have achieved vested eligibility. Total membership in PERSI increased from 108,265 to 111,665 during the fiscal year. There are currently 684 public employers in Idaho who are PERSI members. Participating employers are listed in the Statistical Section of this report.

### **MANAGEMENT RESPONSIBILITY**

The System's management is responsible for the complete and fair presentation of the data and the accompanying disclosures in this report. The financial statements and supplemental schedules included in this report have been prepared in accordance with generally accepted accounting principles for governmental accounting and reporting as pronounced or adopted by the Governmental Accounting Standards Board.

### **INDEPENDENT AUDIT**

The System is audited annually, and for the fiscal year ended June 30, 2005, the audit was conducted by Deloitte & Touche LLP, an independent firm of Certified Public Accountants. Refer to the Independent Auditors' Report for the opinion.

### **INTERNAL ACCOUNTING CONTROL**

As an agency of the State of Idaho, the System's administrative expenses are subject to the State's budget controls. Management is responsible for maintaining a system of internal accounting control designed to provide reasonable assurance transactions are executed in accordance with management's general or specific authorization and are recorded as needed to maintain accountability for assets to permit preparation of financial statements. An internal control procedure has been established, and a budget report is prepared for the Board. We believe the internal controls in effect during FY 2005 adequately safeguard the assets and provide reasonable assurance regarding the proper recording of financial transactions.

**FINANCIAL HIGHLIGHTS**

Collection of employer and employee contributions, as well as income and gains from investments, provides the reserves necessary to finance retirement benefits. These income sources totaled \$1,259,216,162 for all pension funds during the fiscal year ended June 30, 2005.

**ADDITIONS:**

Contributions	\$ 439,581,106
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**INVESTMENT INCOME:**

Net Appreciation in Fair Value of Investments	619,037,925
Interest, Dividends and Other Investment Income	234,130,100
Less: Investment Expenses	<u>(33,692,881)</u>
Net Investment Income	819,475,144

**OTHER INCOME**

159,912

Total Additions	<u>\$ 1,259,216,162</u>
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The payment of benefits is the primary expense of a retirement system. The payments, together with the expenses to administer the Plan, constitute the total expenses of the System. Expenses for FY 2005 are as follows:

**DEDUCTIONS:**

Benefits and Refunds	\$ 386,534,532
Administrative Expenses	7,169,254
Transfers Out	<u>3,457,942</u>

Total Deductions	<u>\$ 397,161,728</u>
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Contributions and expenses continue to increase at a predictable rate.

**ACTUARIAL PRESENT VALUE OF FUTURE BENEFITS**

Future benefits include all benefits estimated to be payable to plan members (retirees and beneficiaries, terminated employees entitled to benefits but not yet receiving them, and current active members) as a result of their service through the valuation date and their expected future salary. The actuarial present value of future benefits as of the valuation date is the present value of the cost to finance benefits payable in the future, discounted to reflect the expected effects of the time value (present value) of money and the probabilities of payment. Simply put, it is the amount that would have to be invested on the valuation date so the amount invested plus investment earnings will provide sufficient assets to pay total future benefits when due.

The actuarial present value was calculated as part of an actuarial valuation at July 1, 2005. Significant actuarial assumptions used include: an investment return rate of present and future assets of 7.75% compounded annually, (7.25% plus 0.50% for expenses); projected salary increases of 4.50% per year compounded annually, attributable to general wage increases; additional projected salary increases attributable to seniority/merit, up to 7.00% per year, depending on service and employee classification, and; 1.00% per year attributable to postretirement benefit increases.

## Introductory Section

At June 30, 2005, the unfunded actuarial liability on a current contribution basis was as follows:

### Unfunded Actuarial Liability on Current Contribution Basis (in millions):

	Valuation Date: July 1, 2005
	Benefit Date: July 1, 2005
A. Actuarial Present Value of All Future Benefits for Contributing Members, Former Contributing Members and Their Survivors	\$ 11,746.2
B. Actuarial Present Value of Total Future Normal Costs for Present Members	2,967.5
C. Actuarial Liability [A - B]	8,778.7
D. ORP Contributions	61.3
E. Actuarial Liability Funded by PERSI Contributions [C-D]	8,717.4
F. Actuarial Value of Assets Available for Benefits	8,208.8*
G. Unfunded Actuarial Liability (funding excess) [E-F]	\$ 508.6
H. Amortization Period on Valuation Date, Based on Contribution Rate Established as of Benefit Date	6.2 Years
I. Funded Ratio [F/E]	94.2%**

\* The total available assets are \$8,453.8 million, but are reduced by \$245.0 million for assets used in plan operations and funds earmarked to provide excess benefits to former members of the Firefighters' Retirement Fund and the Idaho Falls Police Retirement Fund.

\*\* The Funded Ratio of 94.2% includes the effects of the 1% mandatory COLA but not the additional discretionary COLA calculated at 1.7%. The discretionary COLA decreases the ratio to 93.2%.

### ECONOMIC CONSIDERATIONS

The System operates within a dynamic economic environment, as do all investment funds. The objective of the Retirement Board is to minimize the effect of these external influences, where possible, by diversifying among a broad range of asset classes and investment management styles, both domestically and internationally. Such diversification, combined with prudent management by experienced investment professionals, increases the probability the earnings objective will be achieved. The return for fiscal year 2005 was 10.24% net of expenses.

PERSI is funded on a sound actuarial basis, which protects future benefits for participants. Over the long-term, the Plan's assets should achieve their expected returns. However, short-term shortfalls in earnings targets could occur in unfavorable economic environments and/or unfavorable actuarial experience. As of June 30, 2005 the fund had an amortization period of 6.2 years.

### INVESTMENT STRATEGY AND POLICIES

The Retirement Board utilizes and directs funding agents to provide whatever investment management and custodial functions best achieve the System's investment objectives. The Board establishes asset allocation policy, diversification guidelines, custodial functions including safe-guarding of investments,

and other investment restrictions. Each money manager is generally granted full discretion in making investment decisions within their guidelines. The Board, staff, and consultants monitor and evaluate investment results. The Board, in its administration of this System and management of the investment program, is guided by the fiduciary standards in Section 59-1301 of the Idaho Code and the Idaho Uniform Prudent Investor Act, in Sections 68-501 through 68-514 of the Idaho Code and is empowered in its sole discretion to limit, control, and designate the types, kinds, and amounts of investments. Current year investment information and return can be found in the Investment Section of this report.

## FUNDING STATUS

The funding objective of PERSI is to accumulate sufficient assets to ensure funds will be available to meet current and future benefit obligations to participants on a timely basis. If the level of funding is high, the ratio of assets to the actuarial accrued liability is also greater, which means better investment income potential. Each year an independent actuary engaged by PERSI calculates the amount of the annual contribution the plans must make to fully meet their obligations to retired employees. As of June 30, 2005, the PERSI Base Plan has succeeded in funding 94.2% of the present value of the projected benefits earned by employees. The remaining unfunded amount is being systematically funded over 6.2 years as part of the annual required contribution calculated by the actuary. The closed Firemen's Retirement Fund remains an actuarially funded plan. For GASB reporting purposes, the Notes to Required Supplemental Schedules on page 48 provides detailed information on each plan's remaining amortization period. The actuarial method for calculating accrued liability for both plans is Entry Age Normal with the objective of maintaining employer contributions approximately level as a percent of member payroll. For a more in-depth discussion of PERSI's funding, see Management's Discussion and Analysis and the Actuarial Section of this report.

## MAJOR INITIATIVE

In 2003, PERSI initiated a major multi-year Business Process Reengineering project to improve and enhance its customer service delivery system to meet the growing demands for services from an aging membership. By restructuring the organization, the agency is better positioned to meet the increasing needs of its members and employers well into the future. To ensure success, PERSI contracted MAXIMUS, Inc. to serve as an objective third-party to look at and provide expert advice on the restructuring. MAXIMUS, Inc. facilitated the documentation of current processes, and then identified the how the ideal organization should look and how its services and processes should be delivered in the future. This process was Business Process Reengineering.

Three primary customer operating areas emerged from the reengineering process: the PERSI Answer Center, the PERSI Processing Center, and the Employer Service Center. Rounding out PERSI operations are Administration, Choice Plan, Information Technology, Communications, and Portfolio/Investments.

- **PERSI ANSWER CENTER (PAC):** To improve its already exemplary customer service without compromising the "personal touch" for which it is known, PERSI created a contact center with the goal of answering questions and/or responding to inquiries without transferring or passing callers around, and without asking members to call back. PERSI committed substantial financial resources for the PAC staff to receive the training necessary to ensure success, knowing there would be a return on investment through a better educated staff and more satisfied members.
- **PERSI PROCESSING CENTER (PPC):** PERSI formed a center dedicated to providing consistent and accurate forms, applications, and information request processing not otherwise completed by PAC. As part of the PPC effort, PERSI is identifying workflow solutions for several critical, high-volume business processes including retirement application processing, service credit determinations, and the review of disability, divorce, and separation paperwork. By integrating technical solutions — including digital imaging and

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automated workflow — with new business processes, PERSI expects to reduce operating costs, improve overall efficiency, and enhance customer service.

- **EMPLOYER SERVICE CENTER (ESC):** To provide internal efficiencies and simplify employer service delivery, PERSI launched a centralized service team dedicated to employers. We have combined the best technology and integrated processes to ensure employers receive quick, accurate, and timely responses to questions and have resources readily available to help resolve problems. This effort is being implemented as a multi-phased project, starting with the processing of transmittals on a first-in/first-out basis. This has been followed with dedicated phone numbers so employers can call directly into the ESC, bypassing the receptionist. The ESC goal of streamlined, effective customer service is consistent with PERSI's overall operating philosophy.

### **ACKNOWLEDGMENTS**

This financial report of the Public Employee Retirement System of Idaho was prepared by staff under the leadership of the Retirement Board. It is intended to provide complete and reliable information as a basis for making management decisions, as a means of determining compliance with legal provisions, and as a method of determining responsible stewardship for the assets contributed by the members and their employers.

This report is being sent to the Governor, State Legislators, and other interested parties.

Respectfully submitted,

Jody B. Olson, Chairman

Alan H. Winkle, Executive Director

James E. Monroe, Financial Officer