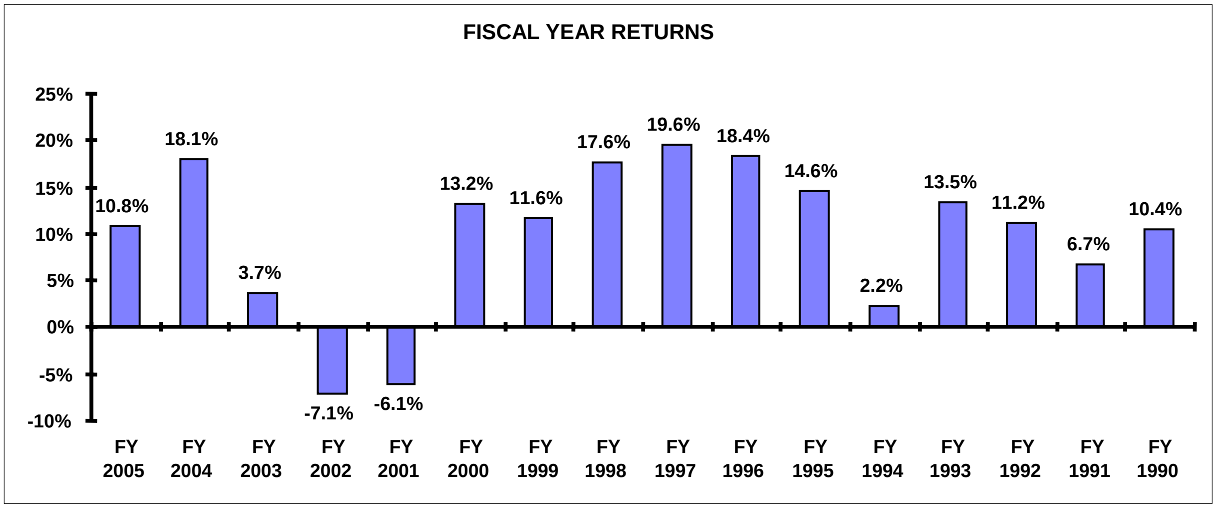
REPORT ON INVESTMENT ACTIVITY

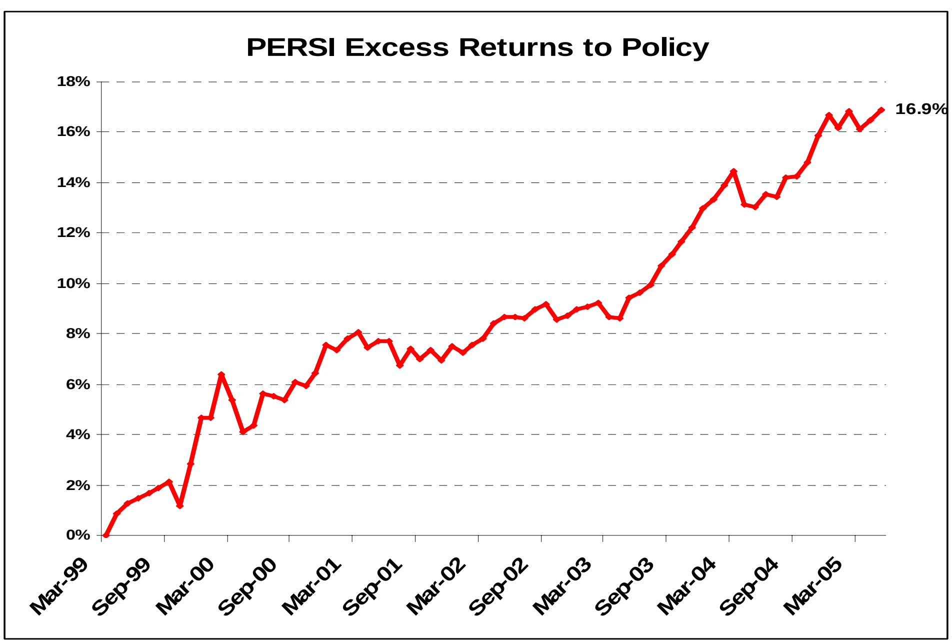
Prepared by Robert M. Maynard, Chief Investment Officer

PERSI had another very good fiscal year. The 2005 fiscal year return of 10.78% was well above the actuarially needed average return of 7.75%. PERSI's peer performance rankings continued to be strong as well, ranking in the top 10% of public funds in the nation for recent years and well above median for almost all time periods.

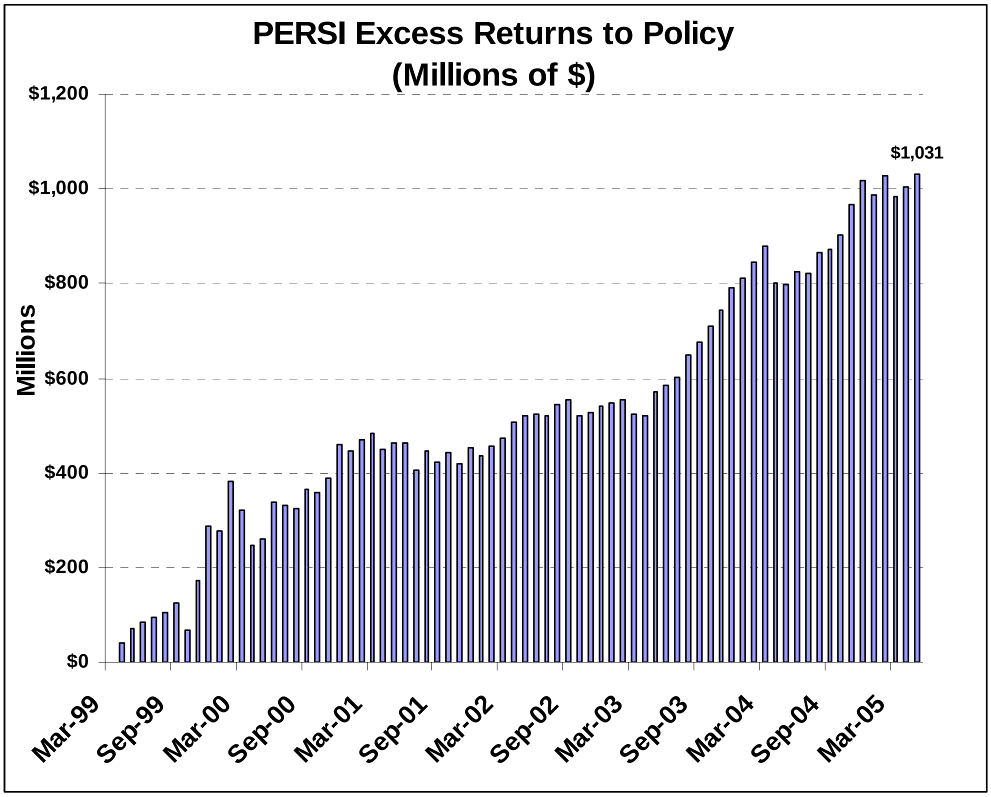


It has been a very good time, particularly in terms of returns relative to peers and to benchmarks. Starting in March1999, including the equity market crash of 2000-2003, and through today, PERSI has been on a very good investment streak. Even with the recession and equity market depression, PERSI is up over 40% cumulatively over that period, has handily exceeded the high points in total value of the boom years ($8.6 billion vs. $7.2 billion in January of 2001), has reached new highs starting in December 2003, and hasn't looked back (at least not yet).

And, compared to simply being passively invested in the market, PERSI has almost doubled its market return from extra efforts. PERSI has added 17% of extra value over the past six years or so:



These excess returns have added over $1 billion of value to the total fund size, as follows:



Similarly, PERSI peer rankings have also been very favorable over both the shorter and longer term. Except for poor relative rankings during the depths of the equity bear market (due to PERSI's higher equity allocations than many public funds), PERSI's peer rankings have been often in the top quartile, and sometimes in the top decile, of public funds nationally. And, for all cumulative time periods, PERSI has done markedly better than its underlying policy would have expected:

RANKINGS IN THE CALLAN PUBLIC FUND UNIVERSE

June 30, 2005

Percentile Rankings over Period

(1 is highest, 100 is lowest)

	QTR	*1Yr*	*2Yrs*	*3Yrs*	*4Yrs*	*5Yrs*	*7Yrs*	*10Yrs*
Return (%)	**2.6**	**10.8**	**14.4**	**10.7**	**6.0**	**3.4**	**5.9**	**9.6**
Policy Return (%)	2.0	8.7	12.2	9.2	4.6	1.9	4.6	8.8
Median Fund (%)	1.9	9.2	11.8	9.1	5.6	3.9	5.5	8.8
PERSI Rank 6	**9**	**9**	**11**	**36**	**62**	**29**	**18**	
Policy Rtn Rank	**41**	**61**	**42**	**48**	**87**	**91**	**88**	**49**

Consequently, despite a strategic policy that would have meant mediocre to poor peer performance for PERSI over the past ten years, both absolutely and relatively (as would be expected given the horrible equity markets of 2000-2003), PERSI has come through what should have been very rough waters with remarkable serenity.

During the last year, PERSI completed its restructuring of the fixed income portfolio, adding an active real return fixed income manager (Bridgewater), and adding two more active bond managers to the line-up (Western and Fidelity). In addition, Peregrine, a large cap growth manager, was added to the domestic equity line-up. The combination of these additions will give a slightly more aggressive cast to the fixed income line-up (to address a likely increase in interest rates over the next few years) and fill in, to a large extent, what had been a marked hole in the equity portfolio compared to the indices (US large cap quality growth stocks).

Almost all parts of PERSI's investment program had good annual and longer-term performance, either absolutely, relative to the markets, or mostly, both. US Equity (including private equity and real estate) returned 9.1% compared to the general equity market return of 8.1% (Russell 3000), global equity (managers who can invest both in the US and internationally) returned 10.6% compared to the world equity index of 10.6% (MSCI World), international equity returned 19.6%, beating the benchmark return of 14.1% (MSCI EAFE), and fixed income returned 8.2% outpacing the general investment grade market gain of 6.8% (Lehman Aggregate). These returns not only beat their individual benchmarks, but also outpaced the performance of PERSI's peers in their general categories. PERSI's domestic equity segment ranked in the top 20th percentile for domestic equity programs by fund sponsors, our international equity efforts ranked in the top 3rd percentile, and we were in the top 8th percentile for the fixed income segment [Callan Asset Class Rankings].

The best performing parts of the PERSI portfolio were emerging markets (46%), Real Estate Investment Trusts (REITs)(34%), private equity (22%), and international equities (20%). The top performing public security accounts were the Bernstein and Genesis emerging markets accounts (48.7% and 42.2%), the Adalente REIT portfolio (33.9%), Mondrian international equity (19.3%), and the Bernstein global equity account (17%). Compared to benchmarks, the greatest outperformance was by Bernstein Emerging Markets (outperforming the index by 12%), Genesis (+6.9%), and Bernstein Global (+6.7%).

At the other end, the worst PERSI return came from Tukman, both in absolute return (-4.6%) and in return relative to its benchmark (underperforming by 10.9%). Tukman invests in a concentrated portfolio of a few (15-20) large cap quality stocks and was badly hurt by corporate accounting and other problems with previously well-thought of companies like AIG and Fannie Mae.

FY 2005 Returns

	Relative to Benchmark FY 2005 (%)	Absolute FY 2005 (%)
Mellon R3000	-0.4	7.6
Tukman Capital Mgmt.	-10.7	-4.6
TCW	-8.9	3.7
D. Smith	-2.7	6.6
Mountain Pacific	-5.0	7.5
Lend Lease	0.3	33.9
Prudential	1.7	15.7
Barings	-3.2	7.1
Bernstein Global	6.7	17.0
Brandes	-0.7	9.6
Capital Guardian	-2.9	7.4
Zesiger Public	3.4	13.7
Mellon EAFE	-0.5	103.6
Rowe Price	-3.2	11.0
Mondrian	5.2	19.3
SGAM	-7.1	7.0
Bernstein Emg.	12.0	46.6
Genesis	6.9	41.1
State Street	0.1	7.6
Barings Fixed	1.1	7.9
DFB MBS	-0.7	5.4
Clearwater	-0.6	5.6
Idaho MTGS.	1.7	7.8
TIPS	4.4	11.2

PERSI's US equity segment returned 9.1%, compared to the general US market return (the Russell 3000) of 8.1%. This was primarily due to the high returns of the REIT portfolio managed by Adelante, with returns of 33.9%, beating the general equity market, although lagging the overall REIT market return of 34.2%. Tukman, as mentioned previously, had a poor year both absolutely (-4.6%) and relative to the S&P 500 (which was up 6.3%). Mountain Pacific although up 7.5%, lagged their benchmark, the Russell 2500, by 5.2%. TCW Domestic, a new equity manager, got off to a poor start with returns of only 3.7%, as did Donald Smith, with returns of only 6.6%. These poor US active manager returns were overcome by the excellent performance of not only the REIT returns from Adalente, but also another good year from private equity (21.8%) and private real estate (12.2%).

Global equity managers again had a good year, with overall returns for the segment of 10.6%, exceeding the world equity market returns of 10.4%. Bernstein Global led this group with returns of 17.0%, followed by Zesiger Capital with returns of 14.3%. Lagging the world indices were Brandes (9.6%), Capital Guardian (7.4%), and Barings (7.1%).

The international equity segment once again benefited from the dedicated exposure to emerging markets. Overall, the total international equity segment outperformed EAFE, with returns of 19.6% compared to the index return of 14.1%. This would not have occurred without emerging markets, which returned 44% for the year, with Bernstein Emerging returning 48.7% and Genesis returning 42.2% – both handily outperforming the emerging markets index of 34.9%. Mondrian, with a 19.3% return, was the only active international manager to outperform the EAFE index return of 14.1%. Both SGAM (7.0%) and Rowe Price (10.9%) continued their lagging performance from the previous year.

Fixed income had another excellent year in comparison with the general fixed income market. PERSI's fixed income total return of 8.2% handily beat (in fixed income terms) the general US investment grade market return of 6.8%. Once again, PERSI's large commitment to TIPS drove this relative outperformance, with a return of 11.6%. Barings fixed income outperformed the general market with returns of 7.8%, as did the Idaho Commercial Mortgage program, with returns of 7.9%. Mortgage Backed Securities portfolios managed by DBF (5.2%) and Clearwater (5.6%) both lagged the Lehman Mortgage index returns of 6.2%.

As a result, this last year has continued a run of good absolute and excellent relative performance that began over six years ago. In fact, the concern at the moment is that this stretch of performance may represent a peak, and could be a limit on how good PERSI can be. PERSI is not structured to be a consistent outstanding performer – instead, we are structured to be a median to slightly above median fund. We are set up to hit singles, not home runs. The exceptional stretch of absolute and relative performance may be due to a confluence of luck when most of our particular biases or special leanings all happened to perform well together. Most of those leanings are undertaken for diversification or other reasons (global equity, TIPS, Idaho Mortgages, REITS, etc.), not for "juicing up" our returns. We rely primarily on the markets, not special efforts, for our returns. The exceptional performance of those special efforts, almost all at the same time, is likely to be an occasion that will not be consistently repeated.

First, PERSI has had a long commitment to the concept and practice of global equity management. For asset allocation reasons (among other reasons, including a belief that the equity markets are increasingly global in scope), PERSI has taken a significant portion of its domestic equity commitment and given it to global equity managers, who may then invest that money anywhere in the world. To the extent global equity managers do better than the US equity market, PERSI will perform better than its policy benchmark. And, for some period, that has been the case. Over the five years through last calendar year, for example, the global equity managers collectively outperformed the Russell 3000 by over 30%.

Second, PERSI made a large commitment to REITs in 1999, rather than either the public real estate market or the public equity market. Again, to the extent that REITS outperform the US public equity market, PERSI will do better than its policy benchmarks, and REITS over the past five years have done very well indeed, beating the Russell 3000 by a cumulative amount of 170%.

Third, PERSI has had a long-standing commitment to emerging markets, a commitment PERSI reviewed after the Asian crisis of 1997, and ended up increasing, rather than eliminating. To the extent that emerging markets do better than the international developed markets (represented by the MSCI EAFE index), PERSI will do better than the policy benchmarks. And, over the five years ending last calendar year, the emerging markets have outperformed by more than 60%.

Finally, PERSI placed about one-third of its fixed income investments in TIPS — Treasury Inflation Protected Securities (actually TIIS —Treasury Inflation Indexed Securities) — at a time when the real interest rate on those instruments was 4.2%. This action was done for diversification reasons, namely that it was a pure protection from unexpected inflation and would have very low correlations with equity and other capital market instruments. It has always been expected the TIPS portfolio would, over the long term, underperform the general bond market (not only is one giving up what should be an inflation risk premium from the general Treasury market, but also one is giving up the corporate yield spread). We couldn't have been more wrong — TIPS have handily outperformed the Lehman Aggregate for a consistent period of time, and by more than 25% during the five years ending last calendar year.

Collectively, these four actions account for almost all of the excess return earned by PERSI. Over the five years ending last calendar year, PERSI earned 11.6% over its policy benchmark. All but 1% of this excess amount came from just these four areas.

There is every reason to doubt these four areas will continue to uniformly and consistently add to return. REITs have already had a tremendous run, and appear, at best, fairly valued compared to both the private real estate market and the rest of the public equity market. We have always expected TIPS to underperform the general bond market, and with real interest rates now at 1.5%-2%, it appears that expectation will likely start to occur.

Emerging markets is an area that might still see some outperformance, despite their recent run. For most of the 1990s, and through the Asian crisis of 1997, emerging markets had a prolonged period of underperformance. There may still be some period in this area of continued outperformance.

And, it may be PERSI's global equity managers can continue to outperform the US equity market. They did so even when international was underperforming the US market, and continued when the wind of better international and emerging market equity returns were in their sails. On the other hand, active management rarely has prolonged periods of uninterrupted success, and there was a period in the early to mid 1990s when global equity management was a noticeable drag on overall PERSI relative returns.

Nonetheless, it is nice to know there can be some market circumstances, like the last year and collectively over the past six years, where all the stars can be lined up at once. But the question we have had to face is our posture in light of likely capital market conditions over the upcoming decade. And, in general, after some review, we have decided to generally maintain our current course with only relatively minor expansions of existing activity, and not try and reach aggressively for any additional return through new approaches (such as hedge funds).

In reviewing our options, there were a couple of developments that dominated our thinking. First, it was clear the rebound after the recession and equity bear market was going to be over after a year or two — it was not going to be a long, drawn out affair. And, it was also clear the capital markets of the next 20 years were going to be different from the previous 20, if at least for the end of the secular decline of interest rates (and the resulting expansion of PE ratios) that began in the early 1980s. Third, it was clear we should not, and probably could not, rely on our larger macro themes to carry the burden of continued excellent absolute and relative returns.

The question was whether we should attempt to continue, through some extraordinary or new means, the outperformance of the past six years or, alternatively, simply maintain, in general, our current posture and expect our performance to track more with the general markets and our peers over the next three to five years. This, in turn, raised two questions. First, were there any obvious means or avenues to generate excess returns that had a high chance of success? Second, was there any underlying need to generate consistently higher-than-market returns?

As for the ability to find successful overall long-term strategies or investment areas that would give a high probability of generating excess returns, the landscape looks bleak. The flood of liquidity into the global capital markets over the past few years have, in general, arbitraged away most obvious pricing disparities between major investment instruments and strategies. We do not see any new strategy, instruments, or markets (like the TIPS and REITs markets in the late 1990s, or the relatively untested global equity investment approach of the early 1990s) that, at this time, offer clear opportunities.
Nor are we impressed with the recent moves of many institutional investors into more aggressive forms of active management — here, mainly, the hedge fund movement. Collectively for all institutional investors the hedge fund world appears, after fees and costs, to be a negative, not positive or even zero, sum game. Even those entering the area agree that in order to be successful, one had to pick the "top quartile" manager. Entering a field where the basic odds were 3 to 1 against us (could we pick, in advance, those top managers?) does not seem an attractive alternative. Consequently, every avenue

for generating extra market returns comes attached with the equivalent (or greater) risk that we will suffer rather than prosper.

Therefore, the second question becomes more important: namely, do we even need to reach for those extra returns? Like crisis managers or emergency room doctors, the appropriate first inquiry might be, instead, to make sure one avoids doing greater harm before looking toward potential other actions. Here our position is much stronger and bodes very well for the future.

PERSI has been very fortunate to have a legislature and Board that have good actual and intuitive sense of the importance of managing the liability side of the pension fund equation. It has always been a principle of the Board and Legislature that any benefit increases must be paid for by a corresponding increase in contribution rates. By statute, the contribution rate can never go below the independently actuarially calculated "normal cost" — the amount needed to fund current benefits. If, because of investment returns or otherwise, an unfunded liability does develop, the Board must statutorily raise rates at least as much as would be needed to pay off that unfunded liability within 25 years. Cost of Living increases above 1% can only be given after the Board annually determines that they can be paid for, and the Legislature concurs in that annual decision. And, after the "roaring '90s", the extra benefits given were only one-time payments (an extra check to retirees, a short contribution holiday for the employers, and a one-time deposit to active employees in a special 401k-type account), and those benefits were only given after a "one standard deviation" reserve account was provided for — an account that absorbed more than half of the record equity bear market that soon followed. As another example, in partial recognition of potentially tougher capital markets, the Board recently reduced the net discount rate (the needed investment rate of return) from 7.5% to 7.25%.

As a result of this tradition and these actions, our legislature and Board did not fall into the common trap of the late '90s of either lowering contribution rates too much or permanently increasing benefits (or both). We do not have medical benefits to contend with. While PERSI would like to achieve a 5% real return to maintain the discretionary COLA level, simply to keep up with the statutory benefits only needs a 3.5% or so real return. As stated earlier, with a 70/30 equity/debt posture, anything above 4% - 5% real equity returns and 1% - 2% real bond returns would be sufficient to at least meet statutory funding goals (assuming the actuary is not materially off base).

It is, therefore, our current conclusion we do not need to reach for returns, and that general exposure to the capital markets is probably sufficient to at least meet statutory benefits. In recognition of the elimination of the tailwind of declining interest rates and other factors, we have decided to play marginally harder around the edges of the portfolio, and not rely quite so much on outperformance based on a few big exposures that are different from the normal capital market approaches (REITs, TIPS, etc.). It is our hope the parts of the portfolio that have not added to excess return will begin to produce (private equity, private real estate, traditional active management in US and international equity, and more aggressive fixed income management).

But, we are not taking any new big bets, either from an overall portfolio perspective (new asset types or classes), or from aggressive or complicated investment styles (such as hedge funds). We do not see any big opportunities in the current capital markets. As a result, we do not intend to take significant actions to avoid the potential for poor markets as spreads widen to more historic levels, and the individual markets regain the risk premiums that have narrowed over the past few years. Thus, we are more in a "do not do significant greater harm in potential bad times" mode, than in an attempt to take significant actions to actively avoid any harm (big bets on hedge funds, real assets, commodities, or other similar actions). To stretch an analogy, we are positioned to be more of a turtle than a hare.

Overall, we are not trying to duplicate the unexpectedly good relative returns of the past six years, and the absolute returns of the last couple of years. We are not trying to add new macro strategies from the top, nor employ extremely aggressive or complicated active management strategies (like hedge funds) from below. We recognize over the next few years our returns may reflect market returns, and our peer rankings may drop more toward the middle of the pack. But, until markets present clear opportunities for both overall portfolio benefits and potential return enhancement, we will rely on more "grind it out" active management with some increased private components to generate incremental return. But, because our Board and Legislature have managed our liabilities and benefit structure well, we can quite comfortably meet our return needs even with mediocre or slightly worse capital markets over the next decade.

For the numbers presented, the source of the above-disclosed data is the Mellon Trust Services reporting system, which follows AIMR's Performance Presentation Standards.

Investment Summary as of the Year Ended June 30, 2005

Types of Investment		Market Value		Percent of Total Market Value
Short-term Investments		$512,080,017		5.9%
Fixed Income				
Domestic	2,109,216,586		24.2%	
International	56,983,051		0.7%	
Commercial Mortgages	259,948,499		3.0%	
Total Fixed Income		2,426,148,136		27.9%
Common Stock				
Domestic Equity	3,643,594,295		41.7%	
International Equity	1,834,994,073		21.1%	
Total Common Stock		5,478,588,368		62.9%
Private Equity		211,348,769		2.4%
Real Estate		79,337,278		0.9%
Total Base Plan Investments		$8,707,502,568		100.0%
Other Funds:				
Sick Leave Insurance Reserve Fund		182,102,887		
Choice Plan 414(k)		56,973,945		
Choice Plan 401(k)		119,983,719		
Total Investments in All Funds		$9,066,563,119		

Schedule of Investments by Account (including interest and dividends receivable) as of June 30, 2005

Adelante Capital Management, LLC	$307,054,670
Apollo Management, LP	12,839,944
Baring Asset Management-Global Equity	244,494,623
Baring Asset Management-Global Fixed Income	214,727,729
Bernstein, LLC -Emerging Markets	167,049,937
Bernstein, LLC -Global Equity	179,443,907
Brandes Investment Partners, LP	447,552,142
Brandes International Equity Fund - Choice Plan	4,778,441
Bridgewater Associates	257,988,693
Capital Guardian	257,936,069
Chisholm Management, LP	19,181,303
Clearwater Advisors, LLC	152,574,521
D.B. Fitzpatrick & Co.-Fixed Income	162,984,119
D.B. Fitzpatrick & Co.-Idaho Mortgages	265,470,538
Dodge and Cox Income Fund – Choice Plan	3,467,186
Donald Smith & Co.	168,101,898
Dreyfus Prem Midcap Stock Fund - Choice Plan	2,535,127
Fidelity Management Trust Company	203,166,381
Frazier Technology Ventures II, LP	2,096,809
Furman Selz Investments, LP	13,007,685
Galen Associates, LP	33,635,147
Genesis Asset Managers	200,947,170
Goense Bounds & Partners, LP	3,952,913
Gores Capital Partners, LP	5,455,313
Green Equity Investors IV, LP	4,976,247
Hamilton Lane Secondary Fund, LLC	800,000
Harvest Partners III, LP	11,149,603
Highway 12 Ventures, LP	4,432,530
Ida-West, LLC	3,275,000
Kohlberg & Co., LLC	1,007,151
Koll Partners, LLC	42,803,442
Littlejohn, LP	15,899,337
McCown DeLeeuw & Co. IV, LP	117,287
Mellon Aggregate Bond Index - Choice Plan	1,022,801
Mellon Capital Management-R2000 Small Cap	140,659,494
Mellon Capital Management-S&P 500 Large Cap	1,306,740,632
Mellon Capital Management-Mid Cap Completion	213,126,655
Mellon Capital Management-International Stock Index	317,675,573
Mellon International EAFE Fund - Choice Plan	738,733
Mellon S&P 500 - Choice Plan	5,309,316
Mellon Transition Management Services	246,995
Mellon Wilshire 5000 - Choice Plan	947,176
Mondrian Investment Partners	184,286,188
Mountain Pacific Investment Advisors	286,741,294
Oaktree Capital Management, LLC	14,712,388
Pareto Partners, LLC	3,164,023
Peregrine Capital Management	157,760,578
PERSI Cash in Short-Term Investment Pool	1,715,605
PERSI Choice Plan Contribution Holding Account	105,315
PERSI Choice Plan Loan Fund	1,608,205

(Continued)

Providence Equity Partners, LP	29,167,987
Prudential Investments, LLC	38,079,029
Rowe Price International	221,935,290
Rowe Price Small Cap Fund - Choice Plan	4,353,882
SEI Stable Asset Fund - Choice Plan	7,007,056
Societe Generale Asset Management	214,768,926
State Street Global Advisors-Fixed Income	568,691,989
State Street Global Advisors-TIPS	495,206,776
State Street Global Advisors-Sick Leave Insurance Reserve	182,102,887
T3 Partners, LP	24,487,023
TCW Domestic	159,116,433
Thomas H. Lee, LP	9,186,579
Tukman Capital Management	241,884,103
Vanguard Growth & Income Fund - Choice Plan	6,498,447
W. Capital Partners, LP	5,134,018
Western Asset Management	204,223,125
Zesiger Capital Group, LLC	301,591,238
Zesiger Capital Group-Private Equity	17,483,830
Total Market Value, Including Investment Receivables and Payables	$8,782,382,451
Add: Investments Purchased	1,139,739,452
Less: Investments Sold	(819,110,168)
Less: Interest and Dividends Receivable (Base Plan, FRF, and Total Return Fund)	(36,448,616)
Total Market Value, Net of Investment Receivables and Payables	$9,066,563,119

(Concluded)

Investment Results (Defined Benefit Plans Only)

MANAGERS	TOTAL MKT VAL (MILLIONS)	% OF TOTAL FUND	Investment Performance for Periods Ending FISCAL	1 YR	3 YRS *	5 YRS *
U.S. EQUITY						
MELLON CAPITAL MANAGEMENT MID CAP	$213.1	2.5%	16.9%	16.9%	15.7%	(1.5)%
MELLON CAPITAL MANAGEMENT R2000 SM CAP	140.7	1.6	9.7	9.7	12.6	6.4
MELLON CAPTIAL MANAGEMENT S&P 500 LC	1,306.7	15.3	6.5	6.5	8.3	(2.3)
MOUNTAIN PACIFIC	286.7	3.3	7.5	7.5	8.8	10.8
TUKMAN CAPITAL MANAGEMENT	241.9	2.8	(4.6)	(4.6)	2.2	2.6
TCW ASSET MANAGEMENT	159.1	1.9	3.7	3.7		
DONALD SMITH & CO	168.1	2.0	6.6	6.6		
PEREGRINE CAPITAL MANAGEMENT**	157.8	1.8				
TOTAL U.S. PUBLICLY TRADED EQUITY	$2,674.1	31.2%	5.9%	5.9%	8.3%	(1.5)%
BENCHMARK – Russell 3000			8.1%	8.1%	9.5%	(1.4)%
PRIVATE EQUITY						
IDA-WEST	$3.3	0.0%	16.5%	16.5%	39.0%	33.2%
GALEN III	33.6	0.4	(7.2)	(7.2)	1.0	(6.3)
HARVEST PARTNERS	11.1	0.1	26.7	26.7	(6.0)	3.7
FURMAN SELZ INVESTORS	13.0	0.2	47.8	47.8	37.0	17.8
MCCOWN DE LEEUW & CO	0.1	0.0	10.7	10.7	0.1	(12.2)
PROVIDENCE EQ PARTNERS	29.2	0.3	50.4	50.4	56.8	12.5
CHISOLM PARTNERS	19.2	0.2	8.2	8.2	(3.6)	(10.3)
LITTLEJOHN II	15.9	0.2	167.4	167.4	17.5	12.3
OAKTREE CAPITAL MANAGEMENT	14.7	0.2	19.1	19.1	18.9	4.4
GOENSE BOUNDS & PARTNERS	4.0	0.0	22.5	22.5	71.3	34.3
HIGHWAY 12 VENTURE	4.4	0.1	(0.6)	(0.6)	(14.3)	
T3 PARTNERS II	24.5	0.3	22.8	22.8	812.6	
THOMAS H. LEE EQ	9.2	0.1	25.4	25.4	(3.0)	
APOLLO MANAGEMENT	12.8	0.2	68.9	68.9	36.5	
ZESIGER CAPITAL GROUP	17.5	0.2	(5.5)	(5.5)	(12.6)	
GREEN EQUITY IV	5.0	0.1	56.1	56.1		
GORES CAPITAL PARTNERS	5.5	0.1	(23.8)	(23.8)		
W CAP PARTNERS	5.1	0.1	(10.1)	(10.1)		
FRAZIER TECHNOLOGY VENTURES II	2.1	0.0	(16.9)	(16.9)		
KOHLBERG & CO**	1.0	0.0				
HAMILTON LANE SECONDARY**	0.8	0.0				
TOTAL PRIVATE EQUITY	$232.0	2.8%	21.8%	21.8%	9.7%	0.0%
REAL ESTATE						
KOLL PARTNERS	$42.8	0.5%	6.0%	6.0%		
ADELANTE CAPITAL MANAGEMENT[1]	307.1	3.6	33.9	33.9	23.7%	22.0%
PRUDENTIAL INVESTMENT MANAGEMENT	38.1	0.4	15.7	15.7	12.1	10.3
TOTAL R/E MANAGERS	$388.0	4.5%	29.4%	29.4%	21.4%	19.8%
BENCHMARK - NCREIF			18.0%	18.0%	12.1%	10.6%
TOTAL U.S. EQUITY	$3,294.1	38.4%	9.1%	9.1%	9.6%	0.0%
BENCHMARK – Russell 3000			8.1%	8.1%	9.5%	(1.4)%
GLOBAL EQUITY						
BARING ASSET MANAGEMENT	$244.5	2.9%	7.1%	7.1%	9.3%	(7.0)%
BRANDES INVESTMENT PARTNERS	447.6	5.2	9.6	9.6	15.2	11.7
CAPITAL GUARDIAN	257.9	3.0	7.4	7.4	11.5	
ZESIGER CAPITAL GROUP	301.6	3.5	14.3	14.3	18.8	3.5
BERNSTEIN GLOBAL	179.4	2.1	17.0	17.0		
TOTAL GLOBAL EQUITY	$1,431.0	16.7%	10.6%	10.6%	13.2%	2.7%
TOTAL U.S./GLOBAL EQUITY	$4,725.1	55.1%	9.6%	9.6%	10.7%	0.8%
BENCHMARK – Russell 3000			8.1%	8.1%	9.5%	(1.4)%

(Continued)

Investment Results (Defined Benefit Plans only)

MANAGERS	TOTAL MKT VAL (MILLIONS)	% OF TOTAL FUND	Investment Performance for Periods Ending FISCAL	1 YR	3 YRS *	5 YRS *
INTERNATIONAL EQUITY						
GENESIS ASSET MANAGERS	$200.9	2.3%	42.2%	42.2%	30.0%	15.3%
MELLON CAPITAL MGMT INTL STK INDX	317.7	3.7	13.5	13.5	12.0	(0.4)
ROWE PRICE INTERNATIONAL	221.9	2.6	10.9	10.9	9.0	(2.3)
SOCIETE GENERALE ASSET MANAGEMENT	214.8	2.5	7.0	7.0	9.7	(4.9)
MONDRIAN INVESTMENT PARTNERS[2]	184.3	2.2	19.3	19.3		
BERNSTEIN EMERGING	167.0	2.0	48.7	48.7		
TOTAL INTERNATIONAL EQUITY	$1,306.6	15.3%	19.6%	19.6%	14.4%	0.6%
TOTAL INT'L EQUITY (HEDGED)[3]	$1,309.8	15.3%	19.5%	19.5%	13.9%	0.5%
BENCHMARK – EAFE Index Net			14.1%	14.1%	12.5%	(0.2)%
TOTAL EQUITY	$6,034.9	70.4%	11.7%	11.7%	11.5%	0.8%
BENCHMARK – Russell 3000			8.1%	8.1%	9.5%	(1.4)%
U.S. FIXED INCOME						
D.B. FITZPATRICK & CO	$163.0	1.9%	5.2%	5.2%	4.5%	6.8%
D.B. FITZPATRICK & CO-IDAHO MTGS	265.5	3.1	7.9	7.9	6.0	8.3
STATE ST GLOBAL ADVISORS	568.7	6.6	7.3	7.3	6.4	7.7
STATE ST GLOBAL ADVISORS-TIPS	495.2	5.8	11.6	11.6	10.8	11.0
CLEARWATER ADVISORS-TBA	152.6	1.8	5.6	5.6	4.6	
TOTAL U.S. FIXED INCOME	$1,645.0	19.2%	8.5%	8.5%	7.8%	9.0%
GLOBAL FIXED INCOME						
BARING ASSET MANAGEMENT	$214.7	2.5%	7.8%	7.8%	6.8%	7.8%
FIDELITY MANAGEMENT**	203.2	2.4				
BRIDGEWATER ASSOCIATES**	258.0	3.0				
WESTERN ASSET MANAGEMENT**	204.2	2.4				
TOTAL GLOBAL FIXED INCOME	$880.1	10.3%	7.8%	7.8%	5.9%	6.8%
TOTAL FIXED INCOME	$2,525.1	29.5%	8.2%	8.2%	7.4%	8.5%
BENCHMARK – LB Aggregate			6.8%	6.8%	5.8%	7.4%
OTHER						
UNALLOCATED CASH	$1.7	0.0%	5.0%	5.0%	5.4%	5.8%
MELLON TRANSITION MANAGEMENT SERVICES	0.2	0.0	31.4	31.4		
COMBINED TOTAL	$8,561.9	100.0%	10.8%	10.8%	10.7%	3.4%
BENCHMARK – 55% Russell 3000 30% Lehman Aggregate 15% MSCI EAFE Index			8.7%	8.7%	9.2%	1.2%
Add: Mutual Fund Holdings in 401(K) Plan	$38.4					
Sick Leave Fixed Income Investments	72.8					
Sick Leave Equity Securities	109.3					
Investments Purchased	1,139.7					
Less: Interest and Dividends Receivable	(36.4)					
Investments Sold	(819.1)					
Total Pension Fund Investments Net of Receivables	$ 9,066.6					

*Rates of Return are annualized
[1] Formerly Lend Lease Rosen
[2] Formerly Delaware International
[3] Includes Pareto Partners currency overlay account
** Accounts open less than one year

Prepared using a time-weighted rate of return in accordance with AIMR's Performance Presentation Standards.

(Concluded)

Schedule of Investment Income for the Last Six Years

Year	Interest	Dividends	Gains & Losses*	Total
2000	153,008,941	71,583,903	629,687,058	854,279,902
2001	165,528,342	63,318,176	(669,263,570)	(440,417,052)
2002	120,190,309	68,412,290	(663,804,822)	(475,202,223)
2003	107,626,722	82,726,663	47,095,088	237,448,473
2004	105,106,092	99,565,950	1,005,291,439	1,209,963,481
2005	108,964,781	121,363,908	622,839,336	853,168,025

*Includes realized and unrealized gains and losses and other investment income

List of Largest Assets Held

Largest Bond Holdings (by Market Value) June 30, 2005

	Par	Bonds		Market Value
1	$216,807,619	U.S. TREASURY INFLATION INDEX BD	3.875% 04/15/2029 DD 04/15/99	$304,716,387
2	261,240,065	U.S. TREASURY INFLATION INDEX NT	4.250% 01/15/2010 DD 01/15/00	293,976,580
3	38,960,000	U.S. TREASURY NOTES	4.000% 06/15/2009 DD 06/15/04	39,380,028
4	35,000,000	COMMIT TO PUR FHLMC GOLD SFM	5.000% 08/01/2035 DD 08/01/05	34,923,420
5	34,000,000	COMMIT TO PUR FNMA SF MTG	5.500% 08/01/2035 DD 08/01/05	34,403,750
6	18,304,703	U.S. TREASURY INFLATION INDEX BD	3.375% 04/15/2032 DD 10/15/01	24,900,839
7	22,000,000	COMMIT TO PUR FNMA SF MTG	6.500% 08/01/2035 DD 08/01/05	22,749,364
8	21,000,000	COMMIT TO PUR FNMA SF MTG	6.000% 08/01/2020 DD 08/01/05	21,689,052
9	20,700,000	COMMIT TO PUR GNMA SF MTG	5.500% 08/15/2035 DD 08/01/05	21,107,542
10	19,920,000	DEUTSCHE AUSGLEICHBANK EMT NTS	5.875% 05-FEB-2008 USD1000	20,856,240

Largest Stock Holdings (by Market Value) June 30, 2005

	Shares	Stock	Market Value
1	2,048,475	GENERAL ELECTRIC CO.	$ 70,979,659
2	2,519,517	MICROSOFT CORP.	62,584,802
3	868,508	EXXON MOBIL CORP.	49,913,155
4	1,743,441	PFIZER, INC.	48,084,103
5	924,710	WALMART STORES, INC.	44,571,022
6	932,250	CITIGROUP, INC.	43,097,918
7	631,818	WELLS FARGO & CO.	38,907,352
8	480,500	VORNADO REALTY TRUST	38,632,200
9	593,191	JOHNSON & JOHNSON	38,557,415
10	499,237	IBM CORP.	37,043,385

A complete list of portfolio holdings is available upon request.

Schedules of Fees and Commissions for the Year Ended June 30, 2005

Investment Fees	Average Assets Under Management	Fees	Basis Points
Investment Manager Fees:			
Equity Managers	$6,144,616,918	$18,932,149	31
Fixed Income Managers	1,986,247,812	1,557,038	8
Private Equity Managers	206,135,252	3,774,502	183
Real Estate Managers	340,190,089	3,703,706	109
Total Investment Manager Fees	$8,677,190,071	27,967,394	32
Other Investment Service Fees:			
Custodian/Record Keeping Fees		4,108,133	
Investment Consultant Fees		736,934	
Legal Fees		319,087	
Actuary/Audit Service Fees		271,250	
Total Investment Service Fees		5,435,078	6
Total Defined Benefit Plans Fees		$33,402,798	38
Total Defined Contribution Plans Fees		290,083	
Total Fees		$33,692,881	

Broker Commissions	Base Commission	Total Shares	Commission per Share
LEHMAN BROS INTL, LONDON	$ 456,540	16,909,833	0.02700
LEHMAN BROS INC, NEW YORK	217,287	6,161,748	0.03526
GOLDMAN SACHS & CO, NEW YORK	214,491	9,091,360	0.02359
JEFFERIES & CO INC, NEW YORK	193,667	3,984,679	0.04860
CREDIT SUISSE (EUROPE), LONDON	154,962	3,108,530	0.04985
CITIGROUP GBL MKTS/SALOMON, NEW YORK	140,982	37,467,510	0.00376
MERRILL LYNCH PIERCE FENNER SMITH INC, NEW YORK	123,674	4,072,216	0.03037
CITIGROUP GBL MKTS INC, NEW YORK	119,479	4,450,358	0.02685
SALOMON BROS INTL LTD, LONDON	107,238	4,432,569	0.02419
MORGAN STANLEY & CO INTL, LONDON	103,863	4,516,114	0.02300
CREDIT SUISSE, NEW YORK	101,349	3,102,502	0.03267
BANC OF AMERICA SECS LLC, CHARLOTTE	96,629	2,976,551	0.03246
UBS SECURITIES LLC, STAMFORD	94,520	5,845,825	0.01617
CANTOR FITZGERALD & CO INC, NEW YORK	92,354	2,807,039	0.03290
DEUTSCHE BANC ALEX BROWN INC, NEW YORK	86,484	3,527,349	0.02452
MORGAN STANLEY & CO INC, NEW YORK	85,063	4,196,159	0.02027
MERRILL LYNCH PIERCE FENNER, WILMINGTON	77,060	43,787,207	0.00176
UBS WARBURG ASIA LTD, HONG KONG	76,345	18,645,447	0.00409
CITATION GROUP, NEW YORK	74,565	2,521,515	0.02957
BERNSTEIN SANFORD C & CO, NEW YORK	73,684	1,770,087	0.04163
GOLDMAN SACHS INTL, LONDON	66,958	2,682,963	0.02496
PERSHING SECURITIES LTD, LONDON	66,886	2,617,232	0.02556
DEUTSCHE BK AG (INTL EQUITIES), LONDON	65,576	2,545,993	0.02576
OTHER BROKERS UNDER $60,000	2,112,905	1,937,373,646	0.00109
Total Broker Commissions	$5,002,561	2,128,594,432	0.00235

A complete list of broker commissions is available from PERSI. PERSI does not require that investment managers use specific brokers.

STATEMENT OF INVESTMENT POLICY AND GUIDELINES

I. Introduction

The Retirement Board of the Public Employee Retirement System of Idaho (“the Board”)(“the System”) hereby establishes its Statement of Investment Policy for the investment of the trust funds (“the Trust”) in accord with Idaho Code Chapter 13, Title 59.

II. Statutory Requirements

The investment of the Trust will be in accord with all applicable laws of the State of Idaho.

A. Sole Interest of Beneficiaries

Investments will be solely in the interest of the participants and beneficiaries and for the exclusive purpose of providing benefits to the participants and their beneficiaries and defraying reasonable expenses of administration.

B. Prudent Investments

Investments will be made with the judgment and care under the circumstances then prevailing, which people of prudence, discretion and intelligence exercise in the management of their own affairs, not in regard to speculation but in regard to the permanent disposition of their funds, considering the probable outcome as well as the probable safety of their capital. Investments will be diversified so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly prudent not to do so.

C. Fiduciary Duties

The Board and its agents, including staff, consultants, and investment managers, will discharge their duties with respect to the fund solely in the interest of the members and retired employees, and with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims.

III. Investment Goals

A. General Objective

1. Purpose

The purpose of the investment of Trust assets is to provide funds to meet the obligations of the Public Employee Retirement System of Idaho (PERSI) while incurring the appropriate amount of risk consistent with attaining that goal. The Board will invest the assets of the Trust so as to meet the projected obligations of the System, and will reduce risk through diversification of the assets of the Trust.

2. Considerations

In determining the returns needed by the system, the acceptable risk levels, and the allowable investments, the Board will consider:

* The effect of particular investments on the total portfolio,
* The purpose of the plan,
* The diversification of the portfolio,
* Liquidity needs and the current return relative to the anticipated cash flow requirements, and
* The projected return of the portfolio as it relates to the funding objectives of the plan.

B. Specific PERSI return and risk objectives

1. Investment Returns

(a) Actuarial Assumptions

In projecting obligations and the returns needed to meet those obligations, the Board will consider studies performed by actuaries hired by the Board. The actuary uses an investment return assumption of 7.75% before fees and expenses in balancing projected obligations, projected contributions, and projected returns on assets. Assuming all of the actuarial assumptions are accurate, this 7.75% return will suffice to: (1) assure the payment of statutorily required benefits, which includes a 1% Cost of Living Adjustment (COLA); and (2) maintain the reduction of the level of the unfunded liability (if any) on the scheduled amortization (one year at a time). The assumed 7.75% return will not be sufficient to fund either discretionary COLAs (2-6%), retroactive COLAs, accelerate the amortization of the unfunded liability, build a stabilization reserve, or allow for gain-sharing distributions.

(b) Inflation and Salary Assumptions

This 7.75% rate assumes an inflation rate of 3.75% and an annual general state salary growth of 4.50%. To the extent that either inflation or salary growth are higher or lower than these rates, then the investment returns needed will also be higher or lower than the assumed 7.75%, although not on a 1:1 ratio. Consequently, the investment returns actually needed by the system do not have a nominal rate which can be determined with precision in advance -- the 7.75% rate currently used by the actuary is only a general midpoint accurate over long (15-20) year periods and is only as accurate as are the inflation and salary assumptions.

(c) Relation to Funding Policy

As set out in the Board's funding policy, to the extent investment markets allow, it is the desire of the Board to provide discretionary COLAs, accelerate the amortization of any unfunded liability, and provide for gain-sharing. It is also the goal of the Board to maintain a reasonable amortization of any unfunded liability, and not to exceed the 25 year amortization period set by statute. Therefore, it is the goal of the Board to set an expected rate of return above the actuarially assumed return so that (1) discretionary COLAs will have a reasonable chance of being consistently funded and (2) the scheduled amortization of any unfunded liability is not unreasonably jeopardized. Returns above that amount will be used to build a stabilization reserve and to distribute to the System participants through gain-sharing.

(d) Periodic Specific Return Goals

Because of the inflation sensitivity of both the returns needed by the system and the size of annual COLAs, an exact target return (either real or nominal) cannot be set in advance. Nonetheless, under most reasonable actuarial assumptions, PERSI has a relatively stable real return goal of between 4.75% - 5.25% if consistent funding of discretionary COLAs and providing for gain sharing is included as an objective. Consequently, specific return goals for upcoming periods will be set out in the strategic asset allocations periodically adopted by the Board.

2. Investment Risk and Strategic Asset Allocations

(a) Diversification Among Asset Classes

In controlling the risk level that is appropriate for the Trust, the Board will diversify the assets of the Trust among various asset classes as the Board may from time to time adopt as appropriate asset classes. The specific asset classes to be used will be set in conjunction with the strategic asset allocation adopted from time to time by the Board.

(b) Review of Asset Classes and Asset Allocation

In setting strategic allocations, the Board will focus on assuring that the expected long-term returns will meet expected long-term obligations with the appropriate level of risk sufficient to meet those objectives. The Board will at least once every four years determine the appropriate asset classes for the investment of Trust assets and conduct asset allocation studies to help determine the long term strategic allocations among desired asset classes so as to meet long-term return objectives with the appropriate level of risk.

(c) Content of Strategic Asset Allocations

The strategic asset allocation will set out the asset classes to be used, the long-term strategic "normal" percentage of assets to be invested in each asset class, the short to intermediate term ranges that will be considered allowable temporary deviations from the strategic normal allocation, the investment risk and return expectations for each asset class, the numerical investment return and risk expected to be realized, and the relation of the expected investment return to the real and actuarially assumed investment return.

(d) Strategic Policies

In addition to asset allocation, the Board may from time to time adopt strategic policies. "Strategic policies" are actions by the Board to invest in asset types that have not been singled out as "asset classes" in the asset allocation process, to overweight particular sectors within an asset class, or to employ particular strategies in the investment of Trust assets. The purposes of these actions are either to increase the return above the expected return or to reduce risk. Examples of types of strategic policies include: a tilt towards small capitalization stocks in U.S. equity allocations; a tilt toward mortgage exposures in fixed income; hedging international currency exposures through a currency overlay program, and adding international emerging markets exposure in international equities.

IV. Investment Structure

A. Overall Structure

In making individual investment policy decisions, the Board will have as an overall goal a flexible, simplified structure with clear roles and accountability.

1. Board Ultimately Responsible

The Board is ultimately responsible for all investment activities. In exercising this responsibility, the Board will hire investment personnel and agents and delegate various investment functions to those personnel and agents. Where the Board does not delegate investment powers or duties, the Board will either satisfy itself that it is familiar with such matters, or will retain persons who are familiar with such matters to consult or assist the Board in the exercise of those responsibilities. Where the Board delegates a responsibility, it will be delegated to a person who is familiar with such matters, and the Board will monitor and review the actions of those to whom responsibilities are delegated.

2. General Roles and Responsibilities of Board and Agents

The Board will favor a structure that accommodates a citizen Board and a small staff. The Board and staff will concentrate their activities on:

* Strategic decisions, primarily concerning asset allocation and strategic policies;
* Adjusting the mix between passive and active managers depending on, among other considerations, near-term concerns regarding the U.S. and other capital markets; and
* Delegating and monitoring all other activities, including hiring and monitoring investment managers.

The Board will rely on outside agents, and primarily investment managers, to be responsible for non-strategic decisions. This responsibility includes those investment decisions with shorter-term consequences such as the best near-term securities, regions, asset types, or asset classes.

B. Direct (Non-Delegated) Responsibilities of the Board

1. Specific Responsibilities

The Board will be directly responsible for

* Setting investment policy,
* Determining the investment structure of the Trust,
* Determining the asset classes to be utilized,
* Setting the strategic asset allocation,
* Determining strategic policies;
* Hiring agents to implement the strategic asset allocation;
* Hiring agents to implement strategic policies; and
* Monitoring the compliance of those agents with the investment policies and strategic allocations set by the Board.

2. Delegation and Monitoring of Specific Investment Activities

The Board will normally delegate investment decisions concerning specific securities or assets, or the tactical allocations of assets among asset types, to outside agents. The Board will retain direct responsibility for the monitoring of the activities of those agents through periodic reports from its staff or consultants. The Board may choose to exercise direct investment responsibility if unusual market conditions or other circumstances so indicate.

C. Employees, Consultants, and Advisors to the Board

1. Investment Staff

(a) Duties of Chief Investment Officer and Other Staff

The Board will hire a Chief Investment Officer and such other staff as it considers appropriate who will be generally responsible for the oversight of the investment of Trust assets, and, as part of that overall responsibility, will: (1) supervise, monitor, and evaluate the performance of the investment managers hired by the Board to assure compliance with investment policy and individual guidelines; (2) assist the Board in developing and adjusting investment policy, including reviewing and modifying the asset allocation as conditions warrant; (3) research current market conditions, evaluate new products, and seek out new approaches to improve portfolio return, reduce risk, and reduce costs and fees; (4) work with the consultants, custodians, investment managers, and other agents in the performance of their assigned duties; and (5) assist the Board with education and other efforts to promote good decision making. Except in special circumstances, PERSI staff will not be responsible for the investment, purchase, or sale of specific assets.

(b) Allocation of New Net Contributions

The Chief Investment Officer shall allocate new net contributions to or withdraw net distributions from the system among investment managers in accordance with the strategic and tactical ranges established by the Board in the strategic asset allocation. The Chief Investment Officer shall report to the Board regularly on the allocation of new net contributions or the withdrawal of net distributions.

(c) Tactical Asset Allocation

With prior notice to the Board, the Chief Investment Officer may shift assets among managers (including between passive and active managers) as long as the asset allocation is maintained within the strategic ranges. If conditions do not permit giving prior Board notice, the Chief Investment Officer is authorized to move assets among investment managers within the strategic ranges established by the Board. If such action is taken, the Chief Investment Officer shall notify the Chairman of the Board as soon as is practical either that action is contemplated or has been taken, as circumstances warrant.

(d) Minimum Qualifications of Chief Investment Officer

The Chief Investment Officer shall at least: (a) have a graduate degree in finance, law, business administration, or a related field, or (b) be a Chartered Financial Analyst; or (c) have three or more years experience in the investment of trust assets.

2. Actuaries

The Board will hire an actuary to provide studies that will: (1) determine the long term obligations faced by the System through annual actuarial valuations, (2) set out return objectives or assumptions that will be sufficient to meet those obligations; and (3) provide reviews at least once every four years of the actuarial valuation process, including updating the projections and assumptions in light of the experience of the System. The Board will set its long-term return objectives after considering information provided by those studies.

3. Investment Consultants

The Board will hire a qualified independent consultant, whose relationship does not impose a conflict of interest with the Board or staff, to provide investment performance measurement at least quarterly with the report available to the Board within three months of the quarter end. The report will at least compare actual investment returns of the system -- in total, by each asset class, and for each managed portfolio -- with both the investment objectives of the system and a composite of returns of other institutional investors. The Board may hire other independent investment consultants as needed to assist the Board in the management of its investment activities, including, but not limited to: (1) performing asset allocation studies, and reviewing and recommending modifications of the asset allocation as conditions warrant; (2) assisting in monitoring the investment managers to assure they are in compliance with the investment policy and their individual guidelines; (3) performing manager evaluations and searches as may be necessary; and (4) assisting in the development and adjustment of investment policy. Except for consultants retained solely for purposes of performance measurement, consultants will be fiduciaries of the Trust.

D. Managers or Agents with Delegated Responsibilities

1. Custodian

(a) Responsibilities

The Board will hire custodians and other agents who will be fiduciaries of the Trust and who will assume full responsibility for the safekeeping and accounting of all assets held on behalf of the Trust. Among other duties as may be agreed to, the custodian will be responsible for: (a) the receipt, delivery, and safekeeping of securities; (b) the transfer, exchange, or redelivery of securities; (c) the claiming, receipt, and deposit of all dividend, interest, and other corporate actions due the Trust; (d) the daily sweep of all uninvested funds into a cash management account or accounts; and, (e) the provision of reports to PERSI upon agreed time intervals that will include all purchases and sales of securities, all dividend declarations on securities held by the Trust, a list of securities held by the Trust, and a cash statement of all transactions for the Trust account.

(b) Authorization of Collective Investment Trusts

Assets of the Trust may be invested in any collective investment trust, which at the time of the investment provides for the pooling of the assets of plans described in Section 401(a) of the Internal Revenue Code of 1986, as amended, and which is exempt from Federal income tax. Assets of the Trust may be commingled with assets of other trusts if invested in any collective investment trust authorized by this policy. The provisions of the trust agreement, as amended by the trustee thereof from time to time, of each collective investment trust in which Trust assets are invested are by this reference incorporated as a part of the trust estate comprising the Trust. The provisions of the collective investment trust will govern any investment of Trust assets in that trust.

2. Investment Managers

The Board will hire investment managers who will be fiduciaries of the Trust and who will be responsible for the investment of Trust assets in specific securities or assets within or among the asset classes.

(a) Minimum Qualifications

Investment managers shall be registered with the Securities and Exchange Commission (unless they are banks, insurance companies, or other category exempted from such registration requirements), have been in the business of investment management at least two years (or the main personnel of the investment management firm have worked together in the business of investment management for at least two years), and, usually, have other United States pension fund assets under management.

(b) Guidelines

Investment Managers shall manage assets in accordance with additional guidelines established by contract and as may be added to or modified from time to time. The additional guidelines will contain minimum diversification requirements that must be followed by that manager. These guidelines will also set out the investment return expected to be achieved by that manager, and shall be linked to a benchmark that represents the passive index fund that would be used to replicate the manager's assignment.

(c) Responsibilities and Discretion

Subject to the restrictions set out in this policy or as may be set out in individual contracts or guidelines, an investment manager shall have full discretionary power to direct the investment, exchange, and liquidation of the assets entrusted to that manager. The manager shall place orders to buy and sell securities and, by notice to the custodian, cause the custodian to deliver and receive securities on behalf of the Trust.

(d) Corporate Governance

The Board, unless otherwise stated, will delegate the voting of proxies to the investment manager or custodian. The Board will adopt and from time to time modify a proxy voting policy. The staff will review the investment manager's policies governing the voting of proxies to assure consistency both with the policy of the Board and, to the extent feasible, among the various investment managers.

(e) Transactions and Brokerage

All securities transactions shall be executed by reputable broker/dealers or banks, and shall be on a best price and best execution basis.

3. Use of Passive and Active Managers

(a) Purpose and Use of Active Management

The Board recognizes that passive (index fund) investing has lower costs than active investing, with regard to both management fees and transaction costs. Further, the Board also recognizes that there is uncertainty concerning whether active investing can generally outperform passive investing, particularly in the large, liquid, and efficient portions of the capital markets. Also, the Board has great confidence that a passive investment of assets in an efficient asset allocation will likely meet long-term (20 year) obligations.

Contribution rates, COLAs, and the ability to provide for gain-sharing, however, are based on 1-5 year returns. The Board does have concern that over 1-5 year periods the ability consistently to fund COLAs and to keep contribution rates stable are in considerable jeopardy from two sources: (1) expected "normal" market fluctuations are such that annual returns will likely not meet hurdle rates approximately 40% of the time, with actual negative returns to be expected once every six years; and (2) that most of

Trust assets under the strategic asset allocation will be invested in U.S. capital markets, and are thus vulnerable to poor U.S. returns.

One purpose of active management of Trust assets is to address these two concerns. Active managers will be hired for the purpose of providing greater stability of returns, and better returns, than would be achievable under purely passive management over rolling 3-5 year periods. Active managers will be responsible for timing of markets and the tactical allocation of assets among and within the capital markets (including between the U.S. and international markets).

In addition to providing extra returns, active managers will also be employed to smooth returns, provide higher long-term returns, provide protection in adverse markets, and to add exposure and additional diversification to the portfolio than that achievable solely through investment in passive indices representing the strategic asset allocation and strategic policies.

(b) Structure

In using outside managers, the Board will favor a structure using a reasonable number of managers with broad mandates and benchmarks. This preference will be implemented so as to achieve the following goals: to relieve the Board from making timing decisions in allocating assets among numerous specialized managers, to simplify the structure of the fund, and to reduce the number of active managers and thus expenses to the Trust.

Passive managers will be favored for the core, liquid, efficient markets (such as S&P 500 stocks and U.S. Government/Corporate bonds), and active managers will be favored for relatively inefficient markets (such as international emerging markets). Global managers will be used to provide flexibility in reacting to near-term concerns that may arise concerning any particular region or market, particularly the U.S. capital markets, and to provide an appropriate balance between efficient long-term asset allocations (which favor US assets) and near-term allocations (which have a greater preference for international assets) to meet the real (inflation adjusted) return needs of the System. Consequently, actual allocations to international equities in the overall portfolio from time to time may be above that in the strategic asset allocation due to the activities of the global equity managers. The actual exposure to international equities will be maintained within the strategic range unless there is prior review by the Board before those ranges are exceeded.

(c) Balance between Passive and Active Management

The balance between active and passive management will be set from time to time with the following considerations in mind: concentration of active investment efforts where there is the most potential for excess returns, implementation of views concerning the state of the U.S. and international capital markets, and reduction of fees and other costs.

(d) Monitoring Standards

Active managers will be monitored under two standards: First, over rolling 3-5 year periods managers will be expected to exceed, after fees, the benchmark index that represents the passive alternative to the mandate given the manager, and to rank in the top half of the universe of managers that best fits that manager's mandate. Second, over shorter periods of time, managers will be expected to maintain key personnel, a consistent style, and investment capability. Passive managers will be monitored on their ability to track their benchmark index over both short (1 quarter to one year) and long periods (3 to 5 year). The Board may consider other information it considers relevant, including composite manager indices, in determining whether to retain or terminate managers.

V. Asset Class Policies

A. U.S. Equities

1. Objective

The overall objective of the U.S. equity asset class is to obtain, over time, a return after fees that equals or exceeds the returns of the Russell 3000 Index, both absolutely and on a risk-adjusted basis.

2. Allowable Investments

Managers may invest in stocks that do not pay dividends. Managers may invest in equity securities outside of the Russell 3000 Index. Managers may use derivative securities for purposes of enhancing liquidity, reducing transaction or other costs, or partially hedging an existing exposure in the portfolio.

3. Manager Styles

Managers for this asset class may include index funds, style managers (such as value and growth), “core” managers, and global managers. Global managers are managers who may invest in securities located anywhere in the world, both within and outside of the United States.

4. Benchmarks

The Russell 3000 index will be the benchmark for the passive index funds, core managers, and global managers. Other style or capitalization indices maintained by a qualified organization may be used as the benchmark for style managers. Active U.S. equity managers are expected to exceed, over rolling 3-5 year intervals, the applicable benchmark by 75 basis points annually after fees, and to rank in the top 50th percentile of active managers with similar mandates.

B. International Equities

1. Objective

The overall objective of the International Equity Asset Class is to obtain, over time, a return after fees that equals or exceeds the returns of the Morgan Stanley Capital International Europe, Australia, and Far East (MSCI EAFE) Index (unhedged), or the FT Actuaries World ex U.S. Index, both absolutely and on a risk-adjusted basis.

2. Allowable Investments

Managers may invest in stocks that do not pay dividends. Managers may invest in American Depository Receipts or American Depository Shares. Managers may invest in equity securities of companies or in countries that are not included in the indices. Managers may use derivative securities for purposes of enhancing liquidity, reducing transaction or other costs, or partially hedging an existing exposure in the portfolio. Managers may, at their discretion, hedge the currency exposure of all or part of their portfolios. Managers may not overhedge their portfolio, although proxy hedging for purposes of liquidity and cost savings is allowed.

3. Manager Styles

Managers for this asset class may include index funds, general international managers, regional or specialized managers (such as emerging markets), and global managers. The Board may from time to time hire a currency overlay manager to hedge the currency exposure in those portfolios where managers do not actively or normally consider hedging their exposure.

4. Benchmarks

The MSCI EAFE Index (unhedged), or the FT Actuaries World ex U.S. (unhedged) will be the benchmark for the passive index funds, general international managers, and global managers. Regional or specialized indices (unhedged) maintained by a qualified organization may be used as the benchmark for other active managers. Active international equity managers are expected to exceed, over rolling 3-5 year intervals, the applicable benchmark by 75 basis points annually after fees, and to rank in the top 50th percentile of active managers with similar mandates.

C. Fixed Income

1. Objectives

The overall objective of the Fixed Income Asset Class is to obtain, over time, a return after fees that equals or exceeds the returns of the Lehman Brothers Aggregate Bond Index (Aggregate Bond Index) both absolutely and on a risk-adjusted basis.

The Fixed Income Asset Class shall consist of investments in mortgages and in both dollar and non-dollar fixed income securities. Mortgages shall consist of investments in mortgage backed securities, and direct ownership of commercial mortgages through the Idaho Commercial Mortgage Program.

The objective of the non-mortgage fixed income securities is to obtain, over time, a return after fees that equals or exceeds the returns of the Lehman Brothers Government/Credit Bond Index (Government/Credit Bond Index) on a risk-adjusted basis. The overall objective of the mortgage securities is to obtain, over time, a return after fees that equals or exceeds the returns of the Lehman Brothers Mortgage Index (Mortgage Index) on a risk-adjusted basis.

2. Allowable Investments

Managers may invest in debt securities that do not pay interest. Active managers may invest in securities in companies or countries not included in the indices. Managers may use derivative securities for purposes of enhancing liquidity, reducing transaction or other costs, or partially hedging an existing exposure in the portfolio. Fixed income managers may, at their discretion and to the extent allowed by their contracts and guidelines, use currency forward or futures markets as may be considered appropriate to implement fixed income strategies.

3. Manager Styles

Managers in this asset class may include index funds, domestic bond managers, specialized managers, and global managers.

4. Benchmarks

The Government/Corporate Index or Aggregate Index will be the benchmark for all non-mortgage fixed income managers. The Mortgage Index will be the benchmark for all mortgage managers. The Aggregate Index will be the benchmark for the asset class. Active fixed income managers are expected to exceed, over rolling 3-5 year intervals, the applicable benchmark by 25 basis points annually after fees, and to rank in the top 50th percentile of active managers with similar mandates.

D. Real Estate

1. Objectives

Private equity real estate investments will be considered part of the U.S. Equity asset class. The overall objective of private equity real estate investments is to attain a 6% real rate of return overall, over a long-term holding period, as long as this objective is consistent with maintaining the safety of principal. The 6% real rate of return includes both income and appreciation, is net of investment management fees, and is net of inflation as is measured annually by the Consumer Price Index. Over a short term basis, the objective is to earn a nominal minimum income yield of 6% on each individual investment, or inflation plus 3%, whichever is greater.

2. Allowable Investments

Allowable private equity real estate investments will include open-end and closed-end commingled real estate funds, publicly traded real estate investment trusts, and direct real estate investments originated by selected real estate advisors who structure similar investments with other institutional investors. The real estate asset sector will not include solely debt obligations; in particular, straight mortgage interests will be considered part of the fixed income asset class.

3. Need for Income Component of Return

Upon acquisition, each real estate investment must have as a goal the expectation of production of annual income measured by realized return and not capital appreciation. Thus, a significant proportion of income producing properties and not purely development properties should be the objective of any commingled fund acquired.

4. Protection of the Trust

Investment vehicles should be chosen that will protect the Trust, including provision for investments that do not contain debt or liability with recourse beyond the Trust commitment to the related business entity, provision for inspection and evaluation of environmental hazards prior to the purchase of any property, and the provision of insurance coverage to protect against environmental and natural hazards.

5. Reporting

A comprehensive reporting system for individual investments or funds will be maintained so that poorly performing investments and deficiencies in portfolio diversification can be identified and active portfolio management facilitated. Investment managers shall be required to present opinions of fair market value as part of quarterly and annual reporting requirements, and audited financial statements shall be required at least annually for each investment entity.

E. Alternative Investments

1. Definition and Board Approval

The Board may from time to time authorize the investment of Trust assets in entities or structures that do not fit the asset descriptions listed above. Examples of such investments are venture capital partnerships, private equity, leveraged buy-out funds, private debt, and direct ownership of individual assets such as oil and gas partnerships. These investments shall only be entered into with the specific approval by the Board or a subcommittee given specific delegation by the Board of each investment vehicle, or investment manager.

2. Objectives and Benchmarks

If the alternative investment is an equity investment, the objective for the investment will be to exceed, over time and after fees, the return achieved by the Russell 2000 Index times 1.35. If the alternative investment is a debt investment, then the objective will be to exceed, over time and after fees, the returns achieved by the Lehman Brothers Government/Credit Index plus 3%. It is recognized that these investments will experience greater volatility than the comparable publicly traded securities and indices.

VI. GASB 40 Reporting (Section VI adopted May 26, 2005)

A. Purpose

The Governmental Accounting Standards Board has identified that state and local governments have deposits and investments which are exposed to risks that may result in losses. GASB Statement number 40 (GASB 40) is intended to inform users of the financial statements about the risks that could affect the ability of a government entity to meet its obligations. GASB 40 has identified general deposit and investment risks as credit risk, including concentration of credit risk and custodial credit risk, interest rate risk, and foreign currency risk and requires disclosures of these risks and of policies related to these risks. This portion of the Investment Policy addresses the monitoring and reporting of those risks.

In general, the risks identified in GASB 40, while present, are diminished when the entire portfolio is viewed as whole. For example, interest rate risk experienced by fixed income instruments often react in the exact opposite direction as that experienced by equities. Thus, interest rate exposure as set out in GASB 40 will not reflect the cross-influences of impacts across the broad range of investments that make up the PERSI portfolio. And, in fact, the general underlying measures used in GASB 40 across most of the risks identified (credit, concentration, and interest rate risk in particular) were tools that were developed primarily for portfolios dominated by fixed income investments, and are often only poorly transferred, if at all, to portfolios, like PERSI's, that are dominated by equity interests.

Consequently, it is the policy of PERSI that the risks addressed in GASB 40 are to be monitored and addressed primarily through the guidelines agreed to by those managers, and by regular disclosures in reports by managers of levels of risks that may exceed expected
limits for those portfolios.

B. Specific Areas of Risk

1. Credit Risk

Summary: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to PERSI.

Policy: Managers will provide PERSI with expected credit risk exposures in their portfolio guidelines. If the actual credit risk exposure falls outside of these expectations, managers will be required to report these occurrences to Staff and these disclosures are to be made available to the Board.

2. Custodial Credit Risk

Summary: 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.

Policy: PERSI minimizes exposure to custodial credit risk by requiring that investments, to the extent possible, be clearly marked as to PERSI ownership and further to the extent possible, be held in the System's name.

3. Concentration of Credit Risk

Summary: Concentration of credit risk is the risk of loss that may be attributed to the magnitude of a government's investment in a single issue.

Policy: Managers will provide PERSI with expected concentration of credit risk exposures in their portfolio guidelines. If the concentration of credit risk exceeds expectations, managers are to be required to report these occurrences to Staff and these disclosures are to be made available to the Board. For the portfolio as a whole, staff will report to the Board at a regular Board meeting if the exposure to a non-US government guaranteed credit exceeds 5% of the total PERSI portfolio.

4. Interest Rate Risk

Summary: Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Interest rate risk to PERSI's fixed income portfolio is monitored using the effective duration methodology. Effective duration measures the volatility of the price of a bond given a change in interest rates, taking into account the optionality on the underlying bond.

Policy: Managers will provide PERSI with the expected portfolio duration in their portfolio guidelines. If the duration of the portfolio differs from expectations, managers are to be required to report these occurrences to Staff and these disclosures are to be made available to the Board.

5. Foreign Currency Risk

Summary: Foreign currency risk is the risk that changes in exchange rates will adversely impact the fair value of an investment. PERSI's currency risk exposures, or exchange rate risk, primarily reside within the international equity investment holdings.

Policy: The PERSI Board recognizes that international investments (equity or fixed income) will have a component of currency risk associated with it. Currency risk and hedging exposures are dependent on the underlying international exposure, which fluctuates over time. The individual manager guidelines will outline the expected currency exposures (either specifically or through ranges of security exposures to particular currency areas) of the underlying portfolio and if the actual currency exposure differs from the expected, managers are to be required to report these occurrences to staff and these disclosures are to be made available to the Board.

VII. Asset Allocation

For purposes of asset allocation, alternative equity investments will be treated as part of the U.S. equity asset class, and alternative debt investments will be treated as part of the fixed income asset class.

STRATEGIC ASSET ALLOCATION

Asset Class	Expected Return	Expected Risk	Strategic Normal	Strategic Ranges	Actual Allocation Year Ended June 30, 2005
U.S. Equity	10.4%	19%	54%	44% - 57%	55%
International Equity	11.0%	22%	15%	12% - 25%	15%
Total Equities			69%	66% - 75%	70%
Fixed Income	6.6%	7%	30%	27% - 33%	30%
Cash	4.0%	1%	1%	0% - 5%	0%

Total Fund	Expected Return	Expected Inflation	Expected Real Return	Expected Risk
Actuary	8.00%	4.25%	3.75%	n/a
Portfolio	9.30%	3.75%	5.55%	13.50%