Comprehensive Annual Financial Report
Of the

Michigan State Police Retirement System

A Pension Fund of the State of Michigan

For the Fiscal Year Ended September 30, 2005

M S P R S

Prepared by:
Financial Services
For
Office of Retirement Services

<u>**Michigan State Police Retirement System**</u>
a Pension Trust Fund of the State of Michigan

Comprehensive Annual Financial Report for the Fiscal Year Ended September 30, 2005

M S P R S

Prepared by:
Financial Services
for
Office of Retirement Services
P.O. Box 30171
Lansing, Michigan 48909-7671
517-322-5103
1-800-381-5111

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INTRODUCTORY SECTION

Certificate of Achievement

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Michigan State Police Retirement System

For its Comprehensive Annual Financial Report for the Fiscal Year Ended September 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. Zielke

President

Jeffrey R. Esser

Executive Director

Public Pension Standards Award

Public Pension Coordinating Council

Public Pension Standards

2005 Award

Presented to

Michigan Office of Retirement Services

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)

Alan H. Winkle
Program Administrator

INTRODUCTORY SECTION

Letter of Transmittal

State Police Retirement System
P.O. Box 30171
Lansing, Michigan 48909-7671
Telephone 517-322-5103
Outside Lansing 1-800-381-5111

STATE OF MICHIGAN

JENNIFER M. GRANHOLM, Governor

DEPARTMENT OF MANAGEMENT AND BUDGET

December 5, 2005

The Honorable Jennifer M. Granholm
Governor, State of Michigan,

Members of the Legislature
State of Michigan,

Retirement Board Members
and
Members, Retirees and Beneficiaries

Ladies and Gentlemen:

We are pleased to present the comprehensive annual financial report of the Michigan State Police Retirement System (System) for fiscal year 2005.

INTRODUCTION TO REPORT

The System was established by legislation under Public Act 251 of 1935. It now operates under the provisions of Public Act 182 of 1986, as amended, and is administrated by the Office of Retirement Services (ORS). The number of active and retired members and beneficiaries of the System is presented in Note 1 of the financial statements in the Financial Section of this report. The purpose of the System is to provide benefits for all State Police. The services performed by the staff provide benefits to members.

Responsibility

Responsibility for both the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with the leadership team of the System. To the best of our knowledge and belief, the enclosed data is accurate in all material respects and is reported in a manner designed to present fairly the financial position and results of operations of the System.

Internal Control Structure

The leadership team of the System is responsible for maintaining adequate internal accounting controls designed to provide reasonable assurance that transactions are executed in accordance with management's general or specific authorization, and are recorded as necessary to maintain accountability for assets and to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America. The internal

Letter of Transmittal (Continued)

control structure is designed to provide reasonable assurance regarding the safekeeping of assets and reliability of all financial records.

Independent Auditors

Andrews Hooper & Pavlik P.L.C., independent auditors, conducted an annual audit of the System. The independent auditor's report on the System's financial statements is included in the Financial Section of this report.

Statute requires that an annual actuarial valuation be conducted. The purpose of the valuation is to evaluate the mortality, service, compensation and other financial experience of the System and to recommend employer-funding rates for the subsequent year. This annual actuarial valuation was completed by the Segal Company for the fiscal year ended September 30, 2004. Actuarial certification and supporting statistics are included in the Actuarial Section of this report.

Report

The 2005 comprehensive annual financial report is presented in five sections. The Introductory Section contains the transmittal letter and identifies the administrative organization and professional consultants used by the System. The Financial Section contains the independent auditor's report, management's discussion and analysis, financial statements and notes of the System, and certain supplemental schedules. The Investment Section summarizes investment activities. The Actuarial Section contains the independent consulting actuary's certification, an outline of actuarial assumptions and methods, and other actuarial statistics. The Statistical Section contains statistical tables of significant data pertaining to the System.

Management's Discussion and Analysis (MD&A)

Generally Accepted Accounting Principles (GAAP) require that management provide a narrative introduction, overview, and analysis to accompany the Basic Financial Statements in the form of MD&A. This letter of transmittal is intended to complement MD&A and should be read in conjunction with it. The MD&A can be found immediately following the Independent Auditor's Report.

PROFILE OF THE GOVERNMENT

The State Police Retirement System was created by Public Act 251 of 1935 and later superseded by Public Act 182 of 1986. A nine-member board, under the direction of a chairperson elected from the membership, administers the fund to provide retirement benefits for State Police officers. Financing is provided by investment income and by an annual legislative appropriation.

ECONOMIC CONDITIONS AND OUTLOOK

Despite challenging economic times, the System continues to show strong performance.

Investments

The State Treasurer is the investment fiduciary and custodian of all investments of the System pursuant to State law. The primary investment objective is to maximize the rate of return on the total investment portfolio, consistent with a high degree of prudence and sufficient diversity to eliminate inordinate risks and to meet the actuarial assumption for the investment return rate. The investment activity for the year produced a total rate of return on the portfolio of 12.9%. For the last five years, the System has experienced an annualized rate of return of 2.9%. A summary of asset allocation and rates of return can be found in the Investment Section of this report.

Letter of Transmittal (Continued)

Accounting System

Transactions of the System are reported on the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when incurred. Participants' benefits are recorded when payable by law. We believe the accounting and administrative internal controls established by the System provide reasonable assurance the System is carrying out its responsibilities in safeguarding its assets, in maintaining the reliability of the financial records for preparing financial statements, and in maintaining accountability for its assets.

Funding

Funds are derived from the excess of additions to plan net assets over deductions from plan net assets. Funds are accumulated by the System in order to meet future benefit obligations to retirees and beneficiaries. The percentage computed by dividing the actuarial value of assets by the actuarial accrued liability is referred to as the "funded ratio." This ratio provides an indication of the funding status of the System and generally, the greater this percentage, the stronger the System. Effective in fiscal year 2001, the System used the actuarial valuation from the previous fiscal year for this report.

This approach is consistent with Governmental Accounting Standards Board (GASB) Statement Number 25. Consistent with this approach, the most recent actuarial valuation was performed as of September 30, 2004. The actuarial value of the assets and actuarial accrued liability of the System were $1.118 billion and $1.256 billion, respectively, resulting in a funded ratio of 89.0% at September 30, 2004. A historical perspective of funding levels for the System is presented on the Schedule of Funding Progress in the Required Supplementary Information in the Financial Section of this report.

Postemployment Benefits

The System also administers the postemployment health benefits (health, dental, and vision) offered to retirees. The benefits are funded on a cash or "pay-as-you-go" basis. An actuarial valuation was completed as of September 30, 2004, to determine the actuarial accrued liability if the benefits were to be pre-funded. If these benefits were pre-funded, the actuarial accrued liability for these benefits would be approximately $440 million and the employer contribution for health care benefits would be 27.7% of payroll.

MAJOR GOALS ACCOMPLISHED

The Michigan Department of Management and Budget, Office of Retirement Services continues to anticipate and rise to the demands of an increasing and longer-lived retirement population. ORS is committed to being responsive to our customers' needs through the thoughtful application of technology and the streamlining of processes. In this fiscal year, we reaped the initial benefits of our Vision ORS technology in mail management, employer reporting and customer call management and settled in to work on the next set of system improvements. Here are some of the highlights.

Focus on Our Customer

To ensure we are giving customers the best possible service, ORS implemented a quality monitoring system in the call center. Through this tool, managers and employees can and do listen to their calls in an effort to improve and maintain the highest quality response/interaction with customers. These calls, selected at random, are evaluated for completeness, quality and courtesy of the responses. This training and staff management tool has served to validate the quality we already offer and allows us to focus training and coaching in the right areas.

Continuously Improve Processes

Pension plan contributions were adjusted down in 2005 with the continued implementation of the results of our 5-year actuarial study. From this study, we were able to change some actuarial assumptions; which mean employers faced lower contribution rates than those originally projected.

Letter of Transmittal (Continued)

The Deferred Retirement Option Plan, introduced in 2004, now includes 129 state troopers who would have otherwise retired. This program allows state police who are eligible to retire to defer their retirement and keep working. Participants can continue employment for up to six years. ORS calculates what the participant's pension was on the day before the DROP period starts, then credits a percentage of the monthly pension to an interest-bearing account in the participant's name. How much is determined by the length of the DROP period: 30 percent if the officer remains in the DROP program for less than one year and up to 100 percent if the officer remains in the program for six years.

Promote a Positive Work Environment

The 2005 fiscal year was a time to focus on who we are and what we believe. ORS participated with all of state government in living the values of Integrity, Inclusion, Teamwork and Excellence. As part of that effort, all managers and supervisors participated in an MI-360 evaluation. This evaluation gave staff insight as to how they were perceived by their direct reports, their peers and their managers. This enlightening training has helped ORS managers become more effective and understanding leaders. In addition to the MI-360, ORS embarked on organization-wide Foundation Training. This training helped all staff understand our process-based organization, why it is successful, and how each person contributes to making ORS even more successful.

To promote a safe working atmosphere, ORS articulated and documented the safeguards needed to protect ORS's staff, equipment, data and property. From what to do in case of a fire to discontinuing system access when an employee leaves, the Security Handbook addresses the steps needed to keep our employees safe and our data secure. We also renovated our Detroit office in a way that preserves the confidentiality of our customer conversations, but provides a greater measure of safety for our employees.

Optimize Technology

ORS is advancing to the next phase of our Vision ORS project: replacing the benefit processing and payment system. This new functionality will allow faster, easier completion of everyday transactions, allowing ORS to process the higher volumes of work expected from our growing and long-lived retiree population.

We continue to diminish the paper that travels through our office. The scanning and indexing solution has increased confidentiality and simplified access to files. Until 2005, we were still creating paper requests to fill a large number of customer requests. By deploying electronic ticketing, all those requests are created, tracked and resolved electronically.

ORS regularly surveys its customers to make certain we are meeting needs. Results from a recent retiree satisfaction survey showed an overall satisfaction rate of 93.9%. We also survey a random sample of active members and retirees who have called us during the year with questions or concerns. Results from this contact survey showed an overall satisfaction rate of 85.0%. The information gained from these surveys helps assure both active members and retirees of ever-improving customer service from ORS.

AWARDS AND ACKNOWLEDGEMENTS

Certificate of Achievement

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the System for its comprehensive annual financial report for the fiscal year ended September 30, 2004. In order 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 accounting principles generally accepted in the United States of America and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. The System has received a Certificate of Achievement for 14 consecutive years. We believe our current report continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

Letter of Transmittal (Continued)

Public Pension Standards Award

The Public Pension Coordinating Council, a confederation of the National Association of State Retirement Administrators (NASRA), the National Conference on Public Employee Retirement Systems (NCPERS), and the National Council on Teacher Retirement (NCTR), awarded Michigan Office of Retirement Services (ORS) the Public Pension Standards Award for recognition of meeting professional standards for plan design and administration as set forth in the standards for fiscal year 2005. This is the second year ORS has achieved this distinction.

Acknowledgements

The preparation of this report was accomplished with the dedication and cooperation of many people. 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 means for determining responsible stewardship of the funds of the System.

We would, therefore, like to express our appreciation for the assistance given by staff, advisors and the many people who contributed to its preparation. We believe their combined efforts have produced a report that will enable employers and plan members to better evaluate and understand the Michigan State Police Retirement System. Their cooperation contributes significantly to the success of the System.

Sincerely,

Lisa Webb Sharpe, Director
Department of Management and Budget

Chris DeRose

Christopher M. DeRose, Director
Office of Retirement Services

Administrative Organization

Retirement Board Members *

Capt. Christopher Lewis
Representing Director, Dept. of State Police
Statutory Member

George M. Elworth
Representing Attorney General
Statutory Member

Sergeant Richard Hale, Chair
Representing Sergeants and Below
Term Expires December 31, 2006

Sally Corbin
General Public
Term Expires December 31, 2006

David Fink
Director, Office of State Employer
Statutory Member

Scott Strong
Deputy Auditor General

Mark Haas
Representing State Treasurer
Statutory Member

Lieutenant Joseph Thomas
Representing Lieutenants and Above
Term Expires December 31, 2007

F/Lt. Diane Garrison, Retired
Retiree Member
Term Expires December 31, 2005

* Statute provides that board members may continue to serve after their term expires until they are either replaced or reappointed.

Administrative Organization

Department of Management and Budget
Office of Retirement Services
P.O. Box 30171
Lansing, Michigan 48909-7671
517-322-5103
1-800-381-5111

Advisors and Consultants

Actuary
The Segal Company
Michael J. Karlin, F.S.A., M.A.A.A.
New York, New York

Auditors
Thomas H. McTavish, C.P.A.
Auditor General
State of Michigan

Andrews Hooper & Pavlik P.L.C.
Jeffrey J. Fineis, C.P.A.
Okemos, Michigan

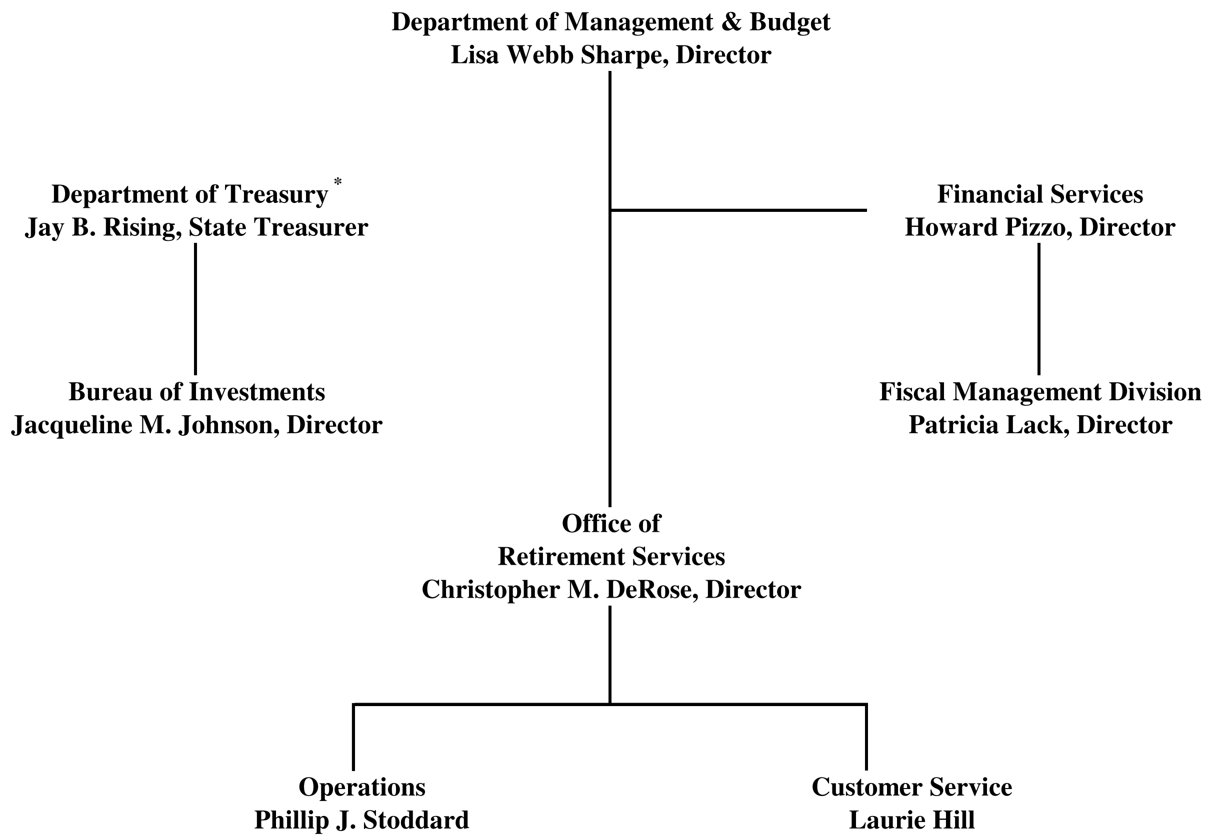
Investment Manager and Custodian
Jay B. Rising
State Treasurer
State of Michigan

Legal Advisor
Mike Cox
Attorney General
State of Michigan

Investment Performance Measurement
State Street Corporation
State Street Analytics
Boston, MA

Administrative Organization (Continued)

Organization Chart



* The investments of the System are managed by the Michigan Department of Treasury. Information on the investments and the fiduciary, Michigan Department of Treasury, can be found in the Investment Section, Introduction. In addition, see the Investment Section, Schedule of Investment Fees and Schedule of Investment Commissions, for information regarding the investment fees and commissions paid as well as investment professionals utilized by the System.

FINANCIAL SECTION

FINANCIAL SECTION

Independent Auditor's Report

ANDREWS HOOPER & PAVLIK P.L.C.
Certified Public Accountants

Ms. Lisa Webb Sharpe, Director, Department of Management and Budget
Mr. Christopher M. DeRose, Director, Office of Retirement Services
Mr. Thomas H. McTavish, CPA, Auditor General, Office of the Auditor General
Michigan State Police Retirement System Board

We have audited the accompanying statements of pension plan and postemployment healthcare plan net assets of the Michigan State Police Retirement System, as of September 30, 2005 and 2004, and the related statements of changes in pension plan and postemployment healthcare plan net assets for the years then ended. These financial statements are the responsibility of the management of the Michigan State Police Retirement System. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial status of the Michigan State Police Retirement System, as of September 30, 2005 and 2004, and the changes in its financial status for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 2, 2005 on our consideration of the Michigan State Police Retirement System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in conjunction with this report in considering the results of our audit.

The Management's Discussion and Analysis (MD&A) is not a required part of the basic financial statements but is supplemental information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this required supplemental information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The Introductory, Investment, Actuarial, and Statistical Sections and the required supplementary information and supporting schedules listed in the table of contents are presented for the purposes of additional analysis and are not a required part of the basic financial statements. The Introductory, Investment, Actuarial, and Statistical Sections and the required supplementary information and supporting schedules are the responsibility of the Michigan State Police Retirement System's management. The Schedules of Funding Progress and Employer Contributions and related notes and the supporting schedules have been subjected to the auditing procedures applied in our audits of the basic financial statements, and in our opinion, are fairly stated in all material respects when considered in relation to the basic financial statements taken as a whole. The Introductory, Investment, Actuarial, and Statistical Sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Andrews Hooper & Pavlik P.L.C.

Okemos, Michigan
December 2, 2005

4295 Okemos Road, Suite 200 • Okemos, Michigan 48864 • ph 517.487.5000 fx 517.487.9535 • www.ahpplc.com

Management's Discussion and Analysis

Our discussion and analysis of the Michigan State Police Retirement System's (System) financial performance provides an overview of the System's financial activities for the fiscal year ended September 30, 2005. Please read it in conjunction with the transmittal letter in the Introductory Section on page 6 and the basic financial statements, which follow this discussion.

FINANCIAL HIGHLIGHTS

- System assets exceeded its liabilities at the close of fiscal year 2005 by $1,123.3 million (reported as *net assets*). Net assets are held in trust to meet future benefit payments.
- System funding objective is to meet long-term benefit obligations through contributions and investment income. As of September 30, 2004, the funded ratio was approximately 89.0%.
- Revenues for the year were $187.9 million, which is comprised of contributions of $56.8 million and investment gains of $131.1 million.
- Expenses increased over the prior year from $107.1 million to $107.3 million or 0.2%. Most of this increase represented increased retirement benefits paid.

THE STATEMENT OF PLAN NET ASSETS AND THE STATEMENT OF CHANGES IN PLAN NET ASSETS

This Comprehensive Annual Financial Report (CAFR) consists of two financial statements; *The Statement of Pension Plan and Postemployment Healthcare Plan Net Assets* (page 20) and *The Statement of Changes in Pension Plan and Postemployment Healthcare Plan Net Assets* (page 21). These financial statements report information about the System, as a whole, and about its financial condition that should help answer the question: Is the System, as a whole, better off or worse off as a result of this year's activities? These statements include all assets and liabilities using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, all revenues and expenses are taken into account regardless of when cash is received or paid.

The Statement of Pension Plan and Postemployment Healthcare Plan Net Assets presents all of the System's assets and liabilities, with the difference between the two reported as net assets. Over time, increases and decreases in net assets measure whether the System's financial position is improving or deteriorating. *The Statement of Changes in Pension Plan and Postemployment Healthcare Plan Net Assets* presents how the System's net assets changed during the most recent fiscal year. These two financial statements should be reviewed along with the Schedule of Funding Progress and Schedule of Employer Contributions to determine whether the System is becoming financially stronger or weaker and to understand changes over time in the funded status of the System.

Management's Discussion and Analysis (Continued)

FINANCIAL ANALYSIS

System total assets as of September 30, 2005, were $1,187.2 million and were mostly comprised of cash, investments and contributions due from employers. Total assets increased $78.6 million or 7.1% from fiscal year 2004 primarily due to favorable operating results and increases to invested assets (primarily collateral on loaned securities), and increased $103.8 million or 10.3% between fiscal years 2003 and 2004 primarily due to increased investment earnings.

Total liabilities as of September 30, 2005, were $63.9 million and were mostly comprised of warrants outstanding, accounts payable, and obligations under securities lending. Total liabilities decreased $1.9 million or 3.0% between fiscal years 2004 and 2005 primarily due to a decrease in obligations under securities lending, and increased $40.2 million or 157.6% between fiscal years 2004 and 2003 primarily due to an increase in obligations under securities lending.

System assets exceeded its liabilities at the close of fiscal year 2005 by $1,123.3 million. Total net assets held in trust for pension and health benefits increased $80.6 million or 7.7% between fiscal years 2004 and 2005. The increase is the result of favorable operating results primarily due to investment earnings and contributions for the year exceeding total deductions to System net assets. Net assets in fiscal year 2004 increased by $63.5 million or 6.5% from the prior year due to favorable market conditions and an increase in investment earnings.

Net Assets
(in thousands)

	2005	Increase (Decrease)	2004	Increase (Decrease)	2003
Assets					
Cash	$ 3,890	(53.6) %	$ 8,386	110.3 %	$ 3,987
Receivables	2,790	80.5	1,546	(68.3)	4,871
Investments	1,180,557	7.5	1,098,673	10.3	995,932
Total Assets	1,187,237	7.1	1,108,605	10.3	1,004,790
Liabilities					
Warrants outstanding	140	(37.5)	224	(0.9)	226
Accounts payable and other accrued liabilities	103	51.5	68	(84.6)	442
Obligations under securities lending	63,653	(2.9)	65,551	163.3	24,894
Total Liabilities	63,896	(3.0)	65,843	157.6	25,562
Total Net Assets	$ 1,123,341	7.7 %	$ 1,042,762	6.5 %	$ 979,228

Management's Discussion and Analysis (Continued)

REVENUES - ADDITIONS TO PLAN NET ASSETS

The reserves needed to finance retirement and health benefits are accumulated through the collection of employer contributions and through earnings on investments. Contributions and net investment income/(losses) for fiscal year 2005 totaled $187.9 million.

Total contributions and net investment income increased $17.2 million from those of fiscal year 2004, due primarily to increased investment earnings. Total contributions and net investment income decreased $19.9 million between fiscal years 2003 and 2004 due to unfavorable market conditions and decreased investment earnings. Total contributions increased between fiscal years 2004 and 2005 by $5.0 million or 9.6%. This increase is primarily due to an increase in the contribution rate. Total contributions decreased between fiscal years 2003 and 2004 by $5.3 million or 9.3% primarily due to a decrease in the contribution rate. Investment income increased from fiscal year 2004 by $12.3 million. Investment income decreased between fiscal years 2003 and 2004 by $14.6 million. The Investment Section of this report reviews the results of investment activity for 2005.

EXPENSES - DEDUCTIONS FROM PLAN NET ASSETS

The primary expenses of the System include the payment of pension benefits to members and beneficiaries, payment for health, dental and vision benefits, refund of contributions to former members, and the cost of administering the System. Total deductions for fiscal year 2005 were $107.3 million, an increase of 0.2% over fiscal year 2004 expenses.

The health, dental and vision care expenses decreased during the year by $2.4 million or 8.1% from $29.2 million to $26.8 million during the fiscal year. This compares to an increase of $2.2 million or 8.0% from $27.0 million to $29.2 million between fiscal years 2003 and 2004. The payment of pension benefits increased by $2.6 million or 3.3% between fiscal years 2004 and 2005 and by $7.4 million or 10.6% between fiscal years 2003 and 2004. The increase in pension benefit expenses resulted from an increase in retirees (29) and an increase in benefit payments to retirees, and in fiscal year 2004 the increase in pension benefit expenses resulted from an increase in retirees (48) and an increase in benefit payments to retirees. Administrative expenses decreased by $22,707 or 7.2% between fiscal years 2004 and 2005, primarily due to a decrease in professional services during the current year for special actuarial studies. Administrative expenses decreased by $106,855 or 25.2% between fiscal years 2003 and 2004, primarily due to a decrease in professional services during the year for special actuarial studies.

Management's Discussion and Analysis (Continued)

Changes in Plan Net Assets
(in thousands)

	2005	Increase (Decrease)	2004	Increase (Decrease)	2003
Member contributions	$ 1,679	4.7 %	$ 1,603	1.5 %	$ 1,579
Employer contributions	55,096	9.7	50,219	(9.6)	55,552
Net investment income	131,111	10.3	118,817	(10.9)	133,378
Miscellaneous income *	-	-	-	-	-
Total Additions	187,886	10.1 %	170,639	(10.4) %	190,509
Pension benefits	80,170	3.3	77,592	10.6	70,152
Health Care benefits	26,842	(8.1)	29,195	8.0	27,036
Refunds of member contributions *	-	(100.0)	1	100.0	-
Administrative expenses	294	(7.3)	317	(25.2)	424
Total Deductions	107,306	0.2 %	107,105	9.7 %	97,612
Net Increase (Decrease)	80,580	26.8	63,534	(31.6)	92,897
Net Assets Beg of Year	1,042,762	6.5	979,228	10.5	886,331
Net Assets End of Year	$ 1,123,342	7.7	$ 1,042,762	6.5	$ 979,228

* Less than one thousand.

Management's Discussion and Analysis (Continued)

RETIREMENT SYSTEM AS A WHOLE

The System's combined net assets experienced an increase for the third consecutive year, following a decrease in fiscal year 2002. This increase is a result of a moderate national economic upturn that resulted in investment income earnings. Management believes, and actuarial studies concur, that the System is in a financial position to meet its current obligations. We believe the current financial position has improved, in part, due to a prudent investment program, cost controls, and strategic planning.

CONTACTING SYSTEM FINANCIAL MANAGEMENT

This financial report is designed to provide the Retirement Board, our membership, taxpayers, investors, and creditors with a general overview of the System's finances and to demonstrate the System's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact the Office of Retirement Services, P.O. Box 30171, Lansing, MI 48909-7671.

Statements of Pension Plan and Postemployment Healthcare Plan Net Assets

As of Fiscal Years Ending September 30, 2005 and 2004

	September 30, 2005			September 30, 2004		
	Pension Plan	Health Plan	Total	Pension Plan	Health Plan	Total
Assets:						
Equity in common cash	$ 3,879,211	$ 11,126	$ 3,890,337	$ 8,385,825		$ 8,385,825
Receivables:						
Amounts due from employer	2,773,583	7,955	2,781,538	1,543,082		1,543,082
Interest and dividends	8,626	25	8,651	2,673		2,673
Total receivables	2,782,209	7,980	2,790,189	1,545,755	-	1,545,755
Investments:						
Short term investment pool	26,776,092	76,800	26,852,892	19,503,679		19,503,679
Total fixed income investment pool	186,981,507	536,305	187,517,812	191,457,940		191,457,940
Total domestic equity investment pool	539,162,382	1,565,483	540,727,865	501,034,771		501,034,771
Real estate investment pool	91,012,525	261,044	91,273,569	76,438,489		76,438,489
Alternative investment pool	131,235,305	376,412	131,611,717	132,258,513		132,258,513
International equities investment pool	138,541,411	378,324	138,919,735	112,428,766		112,428,766
Cash collateral on loaned securities	63,470,946	182,049	63,652,995	65,551,067		65,551,067
Total investments	1,177,180,168	3,376,417	1,180,556,585	1,098,673,225	-	1,098,673,225
Total assets	1,183,841,588	3,395,523	1,187,237,111	1,108,604,805	-	1,108,604,805
Liabilities:						
Warrants outstanding	139,843	401	140,244	223,789		223,789
Accounts payable and other accrued liabilities	102,282	291	102,573	68,281		68,281
Obligations under securities lending	63,470,946	182,049	63,652,995	65,551,067		65,551,067
Total liabilities	63,713,071	182,741	63,895,812	65,843,137	-	65,843,137
Net Assets Held in Trust for Pension and Health Benefits*	$ 1,120,128,517	$ 3,212,782	$ 1,123,341,299	$ 1,042,761,668	$ -	$ 1,042,761,668

*A schedule of funding progress is presented in the Required Supplementary Information of the Financial Section.

The accompanying notes are an integral part of these financial statements.

Statements of Changes in Pension Plan and Postemployment Healthcare Plan Net Assets

For Fiscal Years Ended September 30, 2005 and 2004

	September 30, 2005			September 30, 2004		
	Pension Plan	Health Plan	Total	Pension Plan	Health Plan	Total
Additions:						
Contributions:						
Member contributions	$ 112,303	$ 1,566,646	$ 1,678,949	$ 30,062	$ 1,572,372	$ 1,602,434
Employer contributions	26,607,572	28,488,384	55,095,956	24,792,137	25,426,780	50,218,917
Total contributions	26,719,875	30,055,030	56,774,905	24,822,199	26,999,152	51,821,351
Investment income (loss):						
Investment income (loss)	132,494,702		132,494,702	120,430,613		120,430,613
Investment expenses:						
Real estate operating expenses	(16,180)		(16,180)	(7,393)		(7,393)
Other investment expenses	(1,455,972)		(1,455,972)	(1,681,752)		(1,681,752)
Securities lending activities:						
Securities lending income	1,631,148		1,631,148	703,517		703,517
Securities lending expenses	(1,542,702)		(1,542,702)	(627,816)		(627,816)
Net investment income (loss)	131,110,996	-	131,110,996	118,817,169	-	118,817,169
Miscellaneous income	127		127	125		125
Total additions	157,830,998	30,055,030	187,886,028	143,639,493	26,999,152	170,638,645
Deductions:						
Benefits paid to plan members and beneficiaries:						
Retirement benefits	80,169,608		80,169,608	77,591,542		77,591,542
Health benefits		24,894,119	24,894,119		27,245,933	27,245,933
Dental/vision benefits		1,948,129	1,948,129		1,949,538	1,949,538
Refunds of member contributions	358		358	1,434		1,434
Administrative expenses	294,183		294,183	316,890		316,890
Total deductions	80,464,149	26,842,248	107,306,397	77,909,866	29,195,471	107,105,337
Net Increase (Decrease)	77,366,849	3,212,782	80,579,631	65,729,627	(2,196,319)	63,533,308
Net Assets Held in Trust for Pension and Health Benefits:						
Beginning of Year	1,042,761,668	-	1,042,761,668	977,032,041	2,196,319	979,228,360
End of Year*	$ 1,120,128,517	$ 3,212,782	$ 1,123,341,299	$ 1,042,761,668	$ -	$ 1,042,761,668

* A schedule of funding progress is presented in the Required Supplementary Information of the Financial Section.

The accompanying notes are an integral part of these financial statements.

Notes to Basic Financial Statements

NOTE 1 - PLAN DESCRIPTION

ORGANIZATION

The Michigan State Police Retirement System (System) is a single employer, state-wide, defined benefit public employee retirement plan governed by the State of Michigan (State), originally created under Public Act 251 of 1935, recodified and currently operating under Public Act 182 of 1986. The System was established by the State to provide retirement, survivor and disability benefits to Michigan State Police. The System is a qualified pension trust fund under section 401(a) of the Internal Revenue Code.

The System's financial statements are included as a pension trust fund in the combined financial statements of the State.

The System is administered by the Office of Retirement Services within the Michigan Department of Management and Budget. The Department Director appoints the Office Director who serves as Executive Secretary to the System's Board, with whom the general oversight of the System resides. The State Treasurer serves as the investment officer and custodian for the System.

MEMBERSHIP

At September 30, 2005, and 2004, the System's membership consisted of the following:

Retirees and beneficiaries currently receiving benefits:	2005	2004 *
Regular benefits	2,186	2,167
Survivor benefits	387	381
Disability benefits	153	149
Total	2,726	2,697
Current employees:		
Vested	1,048	947
Non-vested	665	884
Total	1,713	1,831
DROP program participants	132	51
Inactive employees entitled to benefits and not yet receiving them	8	17
Total members	4,579	4,596

* Restated based on more complete information provided by actuary.

Enrollment in the health plan is voluntary. The number of participants is as follows:

Health/Dental/Vision Plan	**2005**	**2004**
Eligible participants	2,726	2,697
Participants receiving benefits:		
Health	2,366	2,321
Dental	2,396	2,377
Vision	2,400	2,379

Notes to Basic Financial Statements (Continued)

BENEFIT PROVISIONS

Introduction

Benefit provisions of the defined benefit pension plan are established by State statute, which may be amended. Public Act 182 of 1986, Michigan State Police Retirement Act, as amended, establishes eligibility and benefit provisions for the defined benefit pension plan. Retirement benefits are determined by final average compensation. Members are eligible to receive a monthly benefit when they meet certain age and service requirements. The System also provides duty disability, non-duty disability, and survivor benefits.

A member who leaves Michigan State Police employment may request a refund of his or her member contribution account. The System is currently non-contributory. A refund cancels a former member's rights to future benefits and there is no provision for repaying the refund of contributions to restore the service represented by the refund.

Regular Retirement

The retirement benefit is available if a member retires after 25 years of credited service (employment). The retirement benefit equals 60% of a member's final average compensation and is payable monthly over the lifetime of a member. Final average compensation is the average annual salary for a member's last two years of service with the Department of State Police.

Deferred Retirement

Any member with 10 or more years of credited service who terminates employment but has not reached the age of 50 is a deferred member and is entitled to receive a monthly allowance upon reaching age 50, provided the member's accumulated contributions have not been refunded. The deferred benefit is equal to two percent of the final average compensation times the years and partial years of service credit.

Non-Duty Disability Benefit

A member with 10 or more years of credited service who becomes totally and permanently disabled not due to performing duties as an employee of the Michigan State Police is eligible for a non-duty disability pension. The non-duty disability benefit is 2.4% of the final average compensation times years and partial years of credited service (but not more than 25 years).

Duty Disability Benefit

A member who becomes totally and permanently disabled from performing duties as a Michigan State Police Officer is eligible for a duty disability pension. The amount, payable monthly, is equal to 60% of the final average compensation.

Survivor Benefit

Upon the death of a member who completed at least 10 years of service, the surviving spouse receives a benefit based on 2.4% of the final average compensation for each year and partial years of credited service. If there is no spouse, surviving children are entitled to equally share the benefit until age 18. If death occurs in the line of duty, the surviving spouse receives a benefit of 60% of the final average compensation. Children receive $100 each month until age 18. A $1,500 funeral expense is also authorized by State statute.

Post Retirement Adjustments

Effective October 1, 1996, the monthly pension was increased 10% if certain requirements were met. This was a one time increase.

Notes to Basic Financial Statements (Continued)

Each October 1, the benefits of all pension recipients increase 2% (not to exceed $500). This non-compounding increase is paid to persons who have been retired 12 months.

Contributions

Member Contributions — Members currently participate on a noncontributory basis. Under certain circumstances, members may contribute to the System for the purchase of creditable service, such as military, maternity or paternity leave, Peace Corps or VISTA service. If a member terminates employment before a retirement benefit is payable, the member's contribution and interest on deposit are refunded. If the member dies before being vested, the member's contribution and interest are refunded to the designated beneficiaries.

Employer Contributions — The statute requires that the employer contribute to finance the benefits of plan members. These employer contributions are determined annually by the System's actuary and are based upon level-percent-of-payroll funding principles so that the contribution rates do not have to increase over time. A chart showing the employer contribution rates is included on the Schedule of Revenues by Source in the Statistical Section.

Other Post Employment Benefits

Under the Michigan State Police Retirement Act, all retirees have the option of continuing health, dental, and vision coverage. Retirees with this coverage contribute 5%, 10% and 10% of the monthly premium amount for the health, dental, and vision coverage, respectively. The State funds 95% of the health and 90% of the dental and vision insurance. The employer payroll contribution rate to provide these benefits was 23.89% and 18.0% for 2005 and 2004, respectively.

Retirees are provided with life insurance coverage equal to 25% of the active life insurance coverage, $1,000 for spouse and $1,000 for each dependent under age 23. Premiums are fully paid by the State.

Deferred Retirement Option Plan

Public Act 83 of 2004 amended the State Police Retirement Act to create a Deferred Retirement Option Plan (DROP) for members with 25 years of service. This benefit program allows state police who are eligible to retire to defer their retirement and keep working for up to six years. The participant's pension amount is calculated on the day before the DROP period starts, and a percentage of the equivalent monthly pension is credited to an interest-bearing account in the participant's name. The DROP balance will be available at the time their DROP participation ends.

Banked Leave Time

Public Act 50 of 2004 amended the State Police Retirement Act to include Banked Leave Time (BLT) for members. BLT is an extension of the State's current annual leave program, which banks a predetermined number of hours per pay period. However, the BLT program will not have an effect on a member's Final Average Compensation calculation.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting and Presentation

Financial statements are prepared using the accrual basis of accounting. Contributions from the State are recognized as revenue when due and payable. Benefits and refunds are recognized when due and payable in accordance with the terms of the System.

Reserves

Public Act 182 of 1986, as amended, created the Reserve for Employee Contributions, Reserve for Retired Benefit Payments, Reserve for Employer Contributions, Reserve for Undistributed Investment Income, and Reserve for Health Related Benefits. The financial transactions of the System are recorded in these accounts as required by Public Act 182 of 1986, as amended.

Notes to Basic Financial Statements (Continued)

Reserve for Employee Contributions — Members do not contribute to this fund except to purchase eligible service credit. This fund represents active member contributions and interest less amounts transferred to the Pension Reserve for regular and disability retirement, amounts refunded to terminated members, and unclaimed amounts transferred to the income account. At September 30, 2005, and 2004, the balance in this account was $294.7 thousand and $216.7 thousand, respectively.

Reserve for Employer Contributions — All employer contributions are credited to this reserve. Interest from the Reserve for Undistributed Investment Income is credited annually. Amounts are transferred annually from this reserve to the Reserve for Retired Benefit Payments to fund that reserve. At September 30, 2005, and 2004, the balance in this account was $68.9 million and $87.7 million, respectively.

Reserve for Retired Benefit Payments — This represents the reserves for payment of future retirement benefits to persons already on the retirement rolls. At retirement, a member's accumulated contributions plus interest are transferred into this reserve from the Reserve for Employee Contributions. Monthly benefits, which are paid to the retirees, reduce this reserve. At the end of each fiscal year, an amount is transferred from the Reserve for Employer Contributions to bring the reserve into balance with the actuarial present value of retirement allowances. At September 30, 2005, and 2004, the balance in this account was $883.7 million and $843.9 million, respectively.

Reserve for Undistributed Investment Income — The reserve is credited with all investment earnings and changes in fair value of assets. Interest is transferred annually to the other reserves. Administrative expenses are paid from this reserve account. The legislature appropriates the funds necessary to defray and cover the administration of the plan. At September 30, 2005, and 2004, the balance of this reserve was $167.2 million and $111.0 million, respectively.

Reserve for Health Related Benefits — This reserve is credited with employer contributions for retirees' health benefits. From this reserve, the System pays 95% of the premiums for hospitalization and medical coverage insurance and 90% of the monthly premium for dental and vision coverage insurance. At September 30, 2005, and 2004, the balance in this account was $3.2 million and $0.0 million, respectively.

Section 204 of Public Act 431 of 1984, as amended, provides management the ability to administer selected risk management related programs for insurance or related services. If the Reserve for Health Related Benefits expenses exceed revenues, the State Sponsored Group Insurance Fund, which bears the risk of such losses, will return excess premiums to the System to make the Reserve whole. This is reflected in the Statement of Changes in Pension Plan Net Assets as an employer contribution to the Health Plan. In fiscal year 2004 the expenses exceeded revenues by $6.8 million prior to a return of $4.6 million to the System.

Reporting Entity

The System is a pension trust fund of the State. As such, the System is considered part of the State and is included in the State's Comprehensive Annual Financial Report as a pension trust fund. The System and its Board are not financially accountable for any other entities or other organizations. Accordingly, the System is the only entity included in this financial report.

Benefit Protection

Public Act 100 of 2002 was passed by the Michigan Legislature to protect pension benefits of public employees from alienation (being transferred). Alienation is attachment, garnishment, levy, execution, bankruptcy or other legal process except for divorce orders or eligible domestic relation orders. The statutes governing the System contained an "anti-alienation" clause to provide for this protection; however, many smaller public pension systems did not have the benefit of this protection. Therefore, Public Act 100 of 2002 was passed to establish legal protection of pension assets that encompasses all public employees.

Notes to Basic Financial Statements (Continued)

Fair Value of Investments

Plan investments are reported at fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Corporate bonds not traded on a national or international exchange are based on equivalent values of comparable securities with similar yield and risk. Real estate debt is valued on the basis of future principal and interest payments, and is discounted at prevailing interest rates for similar instruments. The fair value of real estate investments is based on independent appraisals. Other investments not having an established market are recorded at estimated fair value.

Investment Income

Dividend and interest income is recognized on the accrual basis. Fair value changes are recorded as investment income or loss. Purchases and sales of investments are recorded as of the trade date (the date upon which the transaction is initiated), except for purchase and sale of mortgages, real estate, and alternative investments, which are recorded as of the settlement date (the date upon which the transaction is ultimately completed). The effect of recording such transaction as of the settlement date does not materially affect the financial statements.

Costs of Administering the System

Each year a restricted general fund appropriation is requested to fund the on-going business operations of the System. These administrative costs are ultimately funded by the System through the regular transfer of funds from the System to the general fund based on either a direct cost or allocation basis depending on the nature of the expense. Costs of admininstering the System are not financed by investment income or contributions to the System.

Property and Equipment

Office space is leased from the State on a year to year basis. Office equipment is capitalized if the value exceeds $5,000. These assets are recorded at cost and are reported net of depreciation in the Statement of Pension Plan and Postemployment Healthcare Plan Net Assets. Such assets are depreciated on a straight-line basis over 10 years. The System does not have equipment that falls within these parameters.

Related Party Transactions

Leases and Services — The System leases operating space and purchases certain administrative, data processing, legal and investment services from the State. The space and services are not otherwise available by competitive bid. The following summarizes costs incurred by the System for such services.

	2005	2004
Building Rentals	$ 4,505	$ 5,763
Technological Support	55,160	67,475
Attorney General	23,526	19,482
Investment Services	199,594	198,726
Personnel Services	76,497	68,758

Commitment and Contingency – The State has signed a contract with a vendor for technological support through 2005. As of September 30, 2005, the System's portion of this commitment is approximately $78,518.

Cash — On September 30, 2005, and 2004, the System had $3.9 million and $8.4 million, respectively in a common cash investment pool maintained for various State operating funds. The participating funds in the common cash pool earn interest at various rates depending upon prevailing short-term interest rates. Earnings from these activities amounted to $51,475 and $32,864 for the years ended September 30, 2005, and 2004, respectively.

Reclassification of Prior Year Amounts

Certain prior year amounts have been reclassified to conform with the current year presentation.

Notes to Basic Financial Statements (Continued)

NOTE 3 - CONTRIBUTIONS

Members currently participate in the System on a noncontributory basis. Under certain circumstances, members may contribute to the System for the purchase of creditable service, such as military service or maternity leave. The State is required by Public Act 182 of 1986, as amended, to contribute amounts necessary to finance the benefits of its employees. Contribution provisions are specified by State statute and may be amended only by action of the State Legislature.

Periodic employer contributions to the System are determined on an actuarial basis using the entry age normal actuarial cost method. Under this method, the actuarial present value of the projected benefits of each individual included in the actuarial valuation is allocated on a level basis over the service of the individual between entry age and assumed exit age. The portion of this cost allocated to the current valuation year is called the normal cost. The remainder is called the actuarial accrued liability. Normal cost is funded on a current basis. The unfunded (overfunded) actuarial accrued liability is amortized over a 32-year period for the 2004 fiscal year and a 31-year period for the 2005 fiscal year.

Actual employer contributions for retirement benefits were $26.6 million and $24.8 million for fiscal years 2005 and 2004, respectively, representing 20.7% of annual covered payroll for the year ended September 30, 2004. The fiscal year 2005 annual covered payroll is not yet available. Required employer contributions for pensions included:

1. $24.2 million and $24.5 million for fiscal years 2005 and 2004, respectively, for the normal cost of pensions representing 20.5% of annual covered payroll for fiscal year 2004.

2. $7.9 million and $2.5 million for fiscal years 2005 and 2004, respectively, for amortization of overfunded actuarial accrued liability representing 2.1% of annual covered payroll for fiscal year 2004.

NOTE 4 - INVESTMENTS

Investment Authority

Under Public Act 380 of 1965, as amended, the authority for the purchase and the sale of investments resides with the State Treasurer. Investments are made subject to the Michigan Public Pension Investment Act, Public Act 314 of 1965, as amended. The Michigan Public Pension Investment Act authorizes, with certain restrictions, the investment of pension fund assets in stocks, corporate and government bonds and notes, mortgages, real estate, and certain short-term and alternative investments. Investments must be made for the exclusive purposes of providing benefits to active members, retired members and beneficiaries, and for defraying the expenses of investing the assets.

Under Public Act 314 of 1965, as amended, the State Treasurer may invest up to 5% of the System's assets in small businesses having more than one-half of assets or employees in Michigan as described in section 20(a) of the Act and up to 20% of the System's assets in investments not otherwise qualified under the Act as described in section 20(d). Alternative investments include limited partnerships and distributions from these partnerships in the form of bonds, preferred stock, common stock and direct investments.

Derivatives

The State Treasurer employs the use of derivatives in the investment of the pension trust funds.

Derivatives are used in managing pension trust fund portfolios, but uses do not include speculation or leveraging of investments. Less than 12.0% of the total pension trust fund's portfolio has been invested from time to time in futures contracts, collateralized mortgages and swap agreements. State investment statutes limit total derivative exposure to 15.0% of a fund's total asset value, and restrict uses to replication of returns and hedging of assets. Swap agreements represent the largest category of derivatives used, and they represented 10.8% of market value of total System's pooled assets on September 30, 2005, and 10.0% of market value of total System's pooled assets on September 30, 2004. Futures contracts represent the second largest category of derivatives used, and they represented 0.3% of market value of total System's pooled assets on September 30, 2005, and 0.3% of market value of total System's pooled assets on September 30, 2004.

Notes to Basic Financial Statements (Continued)

To enhance management flexibility, the State Treasurer has purchased futures contracts tied to S&P indices. The futures contracts are combined with short-term investments to replicate the return of the S&P indices. The value of these synthetic equity structures is a combination of the value of the futures contract and the value of the dedicated short-term investments.

To diversify the pension fund's portfolio, the State Treasurer has entered into swap agreements with investment grade counterparties, which are tied to stock market indices in the United States and twenty-two foreign countries. The notional amounts of the swap agreements at September 30, 2005, and 2004, were $92.2 million and $93.0 million, respectively. Approximately one half of the notional amount tied to foreign stock market indices is hedged against foreign currency fluctuations. The swap agreements provide that the System will pay quarterly, over the term of the swap agreements, interest indexed to the three month London Inter Bank Offer Rate (LIBOR), adjusted for an interest rate spread, on the notional amount stated in the agreements. At the maturity of the swap agreements, the pension fund will either receive the increase in the value of the equity indices from the level at the inception of the agreements, or pay the decrease in the value of the indices. Swap agreement maturity dates range from October 2005 to September 2008. U.S. domestic LIBOR based floating rate notes were purchased in the open market to correspond with the notional amount of the swap agreements. The State Treasurer maintains custody and control of these notes.

The value of these synthetic equity structures is a combination of the value of the swap agreements and the value of the notes. The book value represents the cost of the notes. The current value represents the current value of the notes and the change in value of the underlying indices from the inception of the swap agreements. The current value is used as a representation of the fair value based on the intention to hold all swap agreements until maturity. Since the inception of the international equity investment program, over $22.8 million of gains on equity exposure and excess interest received have been realized on matured swap agreements.

The unrealized gain of $29.2 million at September 30, 2005, primarily reflects the increase in international stock indices and changes in currency exchange rates. The combined swap structure realizes gains and losses on a rolling three year basis.

The respective September 30, 2005, and 2004 swap values are as follows:

	Notional Value	Current Value
9/30/2005 (dollars in millions)	$ 92.2	$ 121.3
9/30/2004 (dollars in millions)	93.0	103.2

These amounts reflect both the total International Equity Pool swap exposure, and the smaller swap exposure to the S&P Small Cap Index Pool.

Securities Lending

State statutes allow the System to participate in securities lending transactions, and the System has, by way of a Security Lending Authorization Agreement, authorized the agent bank to lend the System's securities to broker-dealers and banks pursuant to a form of loan agreement.

During the fiscal year, the agent bank lent, at the direction of the System, the System's securities and received cash (United States and foreign currency), securities issued or guaranteed by the United States government, sovereign debt rated A or better, convertible bonds and irrevocable bank letters of credit as collateral. The agent bank does not have the ability to pledge or sell collateral securities delivered absent a borrower default. Borrowers are required to deliver collateral for each loan equal to (i) in case of loaned securities denominated in United States dollars or whose primary trading market is located in the United States or sovereign debt issued by foreign governments, 102% of the market value of the loaned securities; and (ii) in the case of loaned securities not denominated in United States dollars or whose primary trading market is not located in the United States, 105% of the market value of the loaned securities.

Notes to Basic Financial Statements (Continued)

The System did not impose any restrictions during the fiscal year on the amount of loans that the agent bank made on its behalf and the agent bank indemnified the System by agreeing to purchase replacement securities, or return cash collateral in the event a borrower failed to return the loaned security or pay distributions thereon. There were no such failures by any borrowers during the fiscal year. Moreover, there were no losses during the fiscal year resulting from a default of the borrowers or the agent bank.

During the fiscal year, the System and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested in a collective investment pool. As of September 30, 2005, such Trust had an average maturity of 45 days and an average weighted maturity of 404 days. Because the loans were terminable at will, their duration did not generally match the duration of the investments made with cash collateral. On September 30, 2005, the System had no credit risk exposure to borrowers. The cash and non-cash collateral held for securities on loan for the System as of September 30, 2005, were $63,652,995 and $2,261,038, respectively. The carrying amount, which is the fair market value, of securities on loan for the System as of September 30, 2005, was $64,347,791.

Gross income from security lending for the fiscal year was $1,631,148. Expenses associated with this income were the borrower's rebate of $1,513,172 and fees paid to the agent of $29,530.

Risk

In accordance with GASB Statement No. 40, investments require certain disclosures regarding policies and practices, and the risks associated with them. The credit risk, (including custodial credit risk and concentration of credit risk), the interest rate risk and the foreign currency risk are discussed in the following paragraphs. Amounts represent the pro rata share of the underlying investments as required by GASB 40. These are held in internal investment pools and reported as such in the financial statements.

<u>Credit Risk</u> - Credit risk is the risk that an issuer will not fulfill its obligations.

- Short Term Fixed Income Investments - Prime commercial paper investments must be rated A-1 or P-1 at the time of purchase as rated by the two major rating services Standard and Poor's Corporation (S&P); and Moody's Investor Service (Moody's), respectively. Borrowers must have at least $400.0 million in commercial paper outstanding, and the State Treasurer may not invest in more than 10% of the borrowers outstanding debt. The investments are further limited to $200.0 million in any borrower, unless the borrower has a A-1+ rating in which case the investment is not to exceed $300.0 million.

- Long Term Fixed Income Investments - All Long term fixed income investments, that are rated, must be investment grade at time of purchase. Investment grade is defined in P.A. 314 of 1965, as amended: as investments in the top four major grades, rated by two national rating services. The State Treasurer's policy is to use S&P (AAA, AA, A, BBB); and Moody's (Aaa, Aa, A, Baa).

Notes to Basic Financial Statements (Continued)

Rated Debt Investments
(in thousands)
September 30, 2005

Investment Type	Fair Value	S&P	Fair Value	Moody's
Short Term	$ 38,671	A-1	$ 42,365	P-1
	1,754	A-2	1,754	P-2
	8,527	NR	4,833	NR
Government Securities				
U.S. Agencies- Sponsored	55,767	AAA	55,767	Aaa
Corporate Bonds & Notes				
	15,755	AAA	15,755	Aaa
	21,460	AA	25,516	Aa
	37,927	A	33,268	A
	8,867	BBB	11,172	Baa
	7,141	BB	3,157	Ba
	1,445	NR	3,727	NR
International *				
	19,279	AAA	19,279	Aaa
	22,084	AA	37,778	Aa
	46,182	A	29,816	A
	2,242	BB	2,242	Ba
			672	NR
Equity*	1,115	AA	2,229	Aa
	1,114	A	-	
Total	$ 289,330		$ 289,330	

NR - not rated

* International and Equity Investment types consist of domestic floating rate note used as part of a Swap strategy

Notes to Basic Financial Statements (Continued)

Custodial Credit Risk - Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty, the State will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party.

- Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the government and are held by either:
- The counterparty or
- The counterparty's trust department or agent but not in the government name.

The State Treasurer does not have a policy for custodial credit risk. However, the State's custodial bank had a credit rating of AA at September 30, 2005. As of September 30, 2005, and 2004 Government securities with a market value of $1,113 thousand and $1,193 thousand respectively were exposed to custodial credit risk. These securities were held by the counterparty not in the name of the System.

Concentration of Credit Risk - Concentration of credit Risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer.

Other than obligations issued, assumed or guaranteed by the United States, its agencies or United States government sponsored enterprises, the System is prohibited by P.A. 314 of 1965, as amended, from investing in more than 5% of the outstanding obligations of any one issuer or investing more than 5% of a system's assets in the obligations of any one issuer.

At September 30, 2005, and 2004 there were no investments in any single issuer that accounted for more than 5% of the System's assets nor were there any investments totaling more than 5% of the obligations of any one issuer, other than U.S. Government Securities as described above.

Interest Rate Risk - Fixed Income Investments - Interest rate risk is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment.

The State Treasurer's policy states that cash equivalents are invested in short term fixed income securities with an average weighted maturity of less than one year to provide liquidity and safety of principal from capital market and default risk. At September 30, 2005, and September 30, 2004, the fair value of the System's prime commercial paper was $48,952 thousand and $61,057 thousand with the weighted average maturity of 38 days and 41 days, respectively.

The State Treasurer does not have a policy regarding interest rate risk for long term debt investments. However, the pension funds are invested with a long-term strategy. The goal is to balance higher returns while accepting minimum risk for the return. Analyzing the yield curve on individual securities as compared to U.S. Treasuries determines, in part, what is an acceptable risk for the return. Therefore, market conditions such as lower interest rates result in shorter duration and higher interest rates result in longer duration.

Notes to Basic Financial Statements (Continued)

Debt Securities
(in thousands)
For the Year Ended September 30, 2005 and 2004

	2005		2004 **
	Fair Value	Effective Duration in Years	Fair Value
Government			
U. S. Treasury	$ 8,888	4.3	$ 10,975
U. S. Agencies - Backed	25,312	5.3	24,068
U. S. Agencies - Sponsored	55,767	2.5	47,104
Corporate	92,595	4.1	95,180
International*			
U. S. Agencies - Sponsored	1,120	0.1	1,131
Corporate	88,667	0.2	89,465
Equities*	2,229	0.2	2,229
Total	$ 274,578		$ 270,152

*International and Equities contain Domestic Government and Corporate Securities as a part of their derivative strategies. The interest rates reset on a quarterly basis for these securities.

**Effective duration ratings are not available for fiscal year 2004.

Foreign Currency Risk - Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or deposit.

The System invests in various securities denominated in foreign currencies. These investments are limited to 20% of the total assets of the System with an additional limit of 5% of the outstanding foreign securities of any single issuer. No investment is allowed in a country that has been identified by the United States State Department as engaging in or sponsoring terrorism. These limits are set forth in P.A. 314 of 1965, as amended. The types of foreign securities include equities, fixed income, mutual funds, and limited partnerships. At September 30, 2005, and 2004 the total amount of foreign investment subject to foreign currency risk were $50,166 thousand and $35,366 thousand which amounted to 4.5% and 3.4% of total investments of the System, respectively.

Notes to Basic Financial Statements (Continued)

Foreign Currency Risk
(in thousands)
September 30, 2005

Region	Country	Currency	Alt. Invest. Market Value in U.S. $	Equity Market Value in U.S. $	International Equities Market Value in U.S. $	International Derivatives Market Value in U.S. $ *
America						
	Mexico	Peso		$ 5,611		
Europe						
	European Union	Euro	$ 7,597		$ 1,523	$ 3,783
	Switzerland	Franc		701		579
	Sweden	Krona			10	336
	Denmark	Krone			36	208
	Norway	Krone			40	201
	U.K.	Sterling	669	3,769	933	2,110
Pacific						
	Australia	Dollar			10	943
	HongKong	Dollar			137	253
	Japan	Yen	193		100	2,875
	New Zealand	Dollar				42
	Singapore	Dollar				141
	South Korea	Won				554
Various						
	Mutual Funds	Various			16,812	
	Total		$ 8,459	$ 10,081	$ 19,601	$ 12,025

* Note: International derivatives market value exposure to foreign currency risk is the net amount of unrealized gains and unrealized losses. Maturity dates on these investments range from October 2005 through September 2008 with an average maturity of 1.5 years. For more information on derivaties see Note 4.

Notes to Basic Financial Statements (Continued)

Foreign Currency Risk
(in thousands)
September 30, 2004

Region	Country	Currency	Alt. Invest. Market Value in U.S. $	Equity Market Value in U.S. $	International Equities Market Value in U.S. $	International Derivatives Market Value in U.S. $ *
America						
	Mexico	Peso		$ 2,729		
Europe						
	European Union	Euro	$ 7,495		$ 1,227	$ 2,206
	Switzerland	Franc		435		277
	Sweden	Krona			8	275
	Denmark	Krone			45	90
	Norway	Krone			26	74
	U.K.	Sterling	658	7,259	781	1,422
Pacific						
	Australia	Dollar			10	565
	HongKong	Dollar			117	118
	Japan	Yen	133		87	1,145
	New Zealand	Dollar				37
	Singapore	Dollar				127
	South Korea	Won				173
Various						
	Mutual Funds	Various			7,847	
	Total		$ 8,286	$ 10,423	$ 10,148	$ 6,509

* Note: International derivatives market value exposure to foreign currency risk is the net amount of unrealized gains and unrealized losses. Maturity dates on these investments range from October 2004 through September 2007 with an average maturity of 1.5 years. For more information on derivaties see Note 4.

Notes to Basic Financial Statements (Continued)

NOTE 5 – ACCOUNTING CHANGES

In fiscal year 2005, the State implemented Governmental Accounting Standards Board (GASB) Statement No. 40, *Deposit and Investment Risk Disclosures* (an amendment of GASB No. 3), which modifies and expands disclosure requirements for deposits and investments. The new requirements are effective for fiscal periods beginning after June 15, 2004. Information within this financial report is presented on a comparative basis.

The GASB has issued Statement No. 44, *Economic Condition Reporting: The Statistical Section*, which provides guidance on the tables and narrative explanations in the statistical section. The requirements of this statement are effective for fiscal periods beginning after June 15, 2005.

The GASB has issued Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which establishes uniform standards of financial reporting by state and local governmental entities for other postemployment benefit plans (OPEB plans). The requirements of this statement are effective one year prior to the effective date of the related Statement (GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions)* for the employer or the largest employer in the plan. Because the State of Michigan is a phase 1 government (those with total annual revenues of $100 million or more), the System is required to implement this statement in financial statements for periods beginning after December 15, 2005.

NOTE 6 - COMMITMENTS AND CONTINGENCIES

Under the Administrative Procedures Act, members may appeal a decision by the Board. Once the administrative procedure has been exhausted, the decision may be appealed in Michigan's court system. Various cases that have exhausted the administrative procedures have been appealed in the court system. These cases are in the normal course of business and the System does not anticipate any material loss as a result of the contingent liabilities.

Required Supplementary Information

Schedule of Funding Progress

Expressing the net assets available for benefits as a percentage of the actuarial accrued liability provides one indication of the System's funding status. Analysis of this percentage over time indicates whether the System is becoming financially stronger or weaker. Generally, the greater this percentage, the stronger the System. Trends in unfunded actuarial accrued liability and annual covered payroll are both affected by inflation. Expressing the unfunded or over-funded actuarial accrued liability as a percentage of annual covered payroll approximately adjusts for the effects of inflation and aids analysis of progress made in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the stronger the System.

Retirement Benefits (in millions)

Valuation Date Sept 30	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded (Overfunded) Accrued Liability (UAAL) (b-a)	Funded Ratio AAL (a/b)	Covered Payroll (c)	UAAL as a % of Covered Payroll ((b-a)/c)
1995	$ 622.6	$ 798.8	$ 176.2	77.9 %	$ 104.5	168.6 %
1996	697.9	823.5	125.5	84.8	106.8	117.5
1997	787.2	880.3	93.1	89.4	110.1	84.6
1997 (1)	928.7	880.3	(48.4)	105.5	110.1	(44.0)
1997 (3)	928.7	876.8	(52.0)	105.9	110.1	(47.2)
1998	974.4	943.7	(30.6)	103.2	108.2	(28.3)
1998 (2)	974.4	962.5	(11.9)	101.2	108.2	(11.0)
1999	1,036.8	1,006.5	(30.3)	103.0	116.9	(25.9)
2000	1,113.1	1,040.7	(72.4)	107.0	116.6	(62.1)
2001	1,148.6	1,073.6	(75.0)	107.0	118.8	(63.1)
2002	1,141.3	1,135.7	(5.6)	100.5	124.4	(4.6)
2003	1,139.1	1,186.4	47.3	96.0	113.2	41.8
2004 (4)	1,117.7	1,255.8	138.1	89.0	119.7	115.4

(1) Change in asset valuation method.

(2) Assumption change.

(3) Change in inflation.

(4) Change in assumptions and benefit provisions.

Required Supplementary Information (Continued)

Schedule of Employer Contributions

Fiscal Year Ended Sept. 30	Required Contribution (ARC)	Actual Contribution	Percentage Contributed
1996	$ 35,149,438	$ 35,994,833	102.4 %
1997	30,821,696	35,142,572	114.0
1998	20,257,237	20,003,807	98.7
1999	22,733,833	21,609,520	95.1
2000	24,266,567	22,107,292	91.1
2001	21,989,439	24,064,039	109.4
2002	22,041,827	22,456,469	101.9
2003	26,683,625	25,931,762	97.2
2004	26,997,861	24,792,137	91.8
2005	32,151,494	26,607,572	82.8

Notes to Required Supplementary Information

NOTE A - DESCRIPTION

Ten year historical trend information designed to provide information about the System's progress made in accumulating sufficient assets to pay benefits when due is presented in the preceding schedules. Other ten year historical trend information related to the System is presented in the Statistical and Actuarial Sections of the report. This information is presented to enable the reader to assess the progress made by the System in accumulating sufficient assets to pay pension benefits as they become due.

The comparability of trend information is affected by changes in actuarial assumptions, benefit provisions, actuarial funding methods, accounting policies, and other changes. Those changes usually affect trends in contribution requirements and in ratios that use the pension benefit obligation as a factor.

The Schedule of Funding Progress and Schedule of Employer Contributions are reported as historical trend information. The Schedule of Funding Progress is presented to measure the progress being made to accumulate sufficient assets to pay benefits when due. The Schedule of Employer Contributions is presented to show the responsibility of the Employer in meeting the actuarial requirements to maintain the System on a sound financial basis.

NOTE B - SUMMARY OF ACTUARIAL ASSUMPTIONS

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows:

Valuation Date	9/30/2004
Actuarial Cost Method	Entry Age, Normal
Amortization Method	Level Percent of Payroll, Closed
Remaining Amortization Period	32 years
Asset Valuation Method	5-Year Smoothed Market
Actuarial Assumptions:	
Inflation Rate	3.5%
Investment Rate of Return	8%
Projected Salary Increases	3.5% - 93.5%
Cost-of-Living Adjustments	2% Annual Non-Compounded with Maximum Annual Increase of $500 for those eligible

Supporting Schedules

Comparative Summary Schedule of
Pension Plan Administrative Expenses
For the Years Ended September 30, 2005 and 2004

	2005	2004
Personnel Services:		
Staff Salaries	$ 52,693	$ 48,443
Retirement and Social Security	14,445	11,368
Other Fringe Benefits	9,359	8,947
Total	76,497	68,758
Professional Services:		
Accounting	12,506	8,181
Actuarial	63,000	63,000
Attorney General	23,526	19,482
Audit	13,693	31,296
Consulting	4,971	6,774
Medical	3,183	14,713
Total	120,879	143,446
Building Equipment		
Building Rentals	4,505	5,763
Equipment Purchase, Maintenance, and Rentals	653	312
Total	5,158	6,075
Miscellaneous:		
Travel and Board Meetings	284	144
Office Supplies	714	710
Postage, Telephone and Other	31,927	25,937
Printing	3,564	4,345
Technological Support	55,160	67,475
Total	91,649	98,611
Total Administrative Expenses	$ 294,183	$ 316,890

Supporting Schedules (Continued)

Schedule of Investment Expenses

	2005	2004
Real Estate Operating Expenses	$ 16,180	$ 7,393
Securities Lending Expenses	1,542,702	627,816
Other Investment Expenses*	1,455,972	1,681,752
Total Investment Expenses	$ 3,014,854	$ 2,316,961

* Refer to Investment Section for fees paid to investment professionals.

Schedule of Payments to Consultants

	2005	2004
Independent Auditors	$ 13,693	$ 31,296
Consulting	4,971	6,774
Medical	3,183	14,713
Attorney General	23,526	19,482
Accounting	12,506	8,181
Actuary	63,000	63,000
Total Payment to Consultants	$ 120,879	$ 143,446

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Supporting Schedules (Continued)

Detail of Changes in Plan Net Assets (Pension and Postemployment Healthcare Benefits)

For the Year Ended September 30, 2005

	Employee Contributions	Employer Contributions	Retired Benefit Payments*	Undistributed Investment Income	Health Related Benefits	Total
Additions:						
Contributions:						
Member contributions	$ 112,303				$ 1,566,646	$ 1,678,949
Employer contributions		$ 26,607,572			28,488,384	55,095,956
Total Contributions	112,303	26,607,572	-	-	30,055,030	56,774,905
Investment income (loss):						
Investment income (loss)				$ 132,494,702		132,494,702
Investment expenses:						
Real estate operating expenses				(16,180)		(16,180)
Other investment expenses				(1,455,972)		(1,455,972)
Securities lending activities:						
Securities lending income				1,631,148		1,631,148
Securities lending expenses				(1,542,702)		(1,542,702)
Net investment income (loss)	-	-	-	131,110,996	-	131,110,996
Miscellaneous income				127		127
Total additions	112,303	26,607,572	-	131,111,123	30,055,030	187,886,028
Deductions:						
Benefits paid to plan members and beneficiaries:						
Retirement benefits			$ 80,169,608			80,169,608
Health benefits					24,894,119	24,894,119
Dental/vision benefits					1,948,129	1,948,129
Refunds of member contributions	358					358
Administrative expenses				294,183		294,183
Total deductions	358	-	80,169,608	294,183	26,842,248	107,306,397
Net Increase (Decrease)	111,945	26,607,572	(80,169,608)	130,816,940	3,212,782	80,579,631
Other Changes in Net Assets:						
Interest allocation	9,222	7,012,530	67,513,609	(74,535,361)		-
Transfers upon retirement	(43,154)	(52,408,045)	52,451,199			-
Total other changes in net assets	(33,932)	(45,395,515)	119,964,808	(74,535,361)	-	-
Net Increase (Decrease) After Other Changes	78,013	(18,787,943)	39,795,200	56,281,579	3,212,782	80,579,631
Net Assets Held in Trust for Pension and Health Benefits:						
Beginning of Year	216,704	87,656,627	843,920,117	110,968,220	-	1,042,761,668
End of Year	$ 294,717	$ 68,868,684	$ 883,715,317	$ 167,249,799	$ 3,212,782	$ 1,123,341,299

*Casualty Reserve is included.

Supporting Schedules (Continued)

Detail of Changes in Plan Net Assets (Pension and Postemployment Healthcare Benefits)
For the Year Ended September 30, 2004

	Employee Contributions	Employer Contributions	Retired Benefit Payments*	Undistributed Investment Income	Health Related Benefits	Total
Additions:						
Contributions:						
Member contributions	$ 30,062				$ 1,572,372	$ 1,602,434
Employer contributions		$ 24,792,137			25,426,780	50,218,917
Total Contributions	30,062	24,792,137	-	-	26,999,152	51,821,351
Investment income (loss):						
Investment income (loss)				$ 120,430,613		120,430,613
Investment expenses:						
Real estate operating expenses				(7,393)		(7,393)
Other investment expenses				(1,681,752)		(1,681,752)
Securities lending activities:						
Securities lending income				703,517		703,517
Securities lending expenses				(627,816)		(627,816)
Net investment income (loss)	-	-	-	118,817,169	-	118,817,169
Miscellaneous income				125		125
Total additions	30,062	24,792,137	-	118,817,294	26,999,152	170,638,645
Deductions:						
Benefits paid to plan members and beneficiaries:						
Retirement benefits			$ 77,591,542			77,591,542
Health benefits					27,245,933	27,245,933
Dental/vision benefits					1,949,538	1,949,538
Refunds of member contributions	1,434					1,434
Administrative expenses				316,890		316,890
Total deductions	1,434	-	77,591,542	316,890	29,195,471	107,105,337
Net Increase (Decrease)	28,628	24,792,137	(77,591,542)	118,500,404	(2,196,319)	63,533,308
Other Changes in Net Assets:						
Interest allocation	9,547	13,191,074	59,721,139	(72,921,760)		-
Transfers upon retirement	(61,272)	(115,215,012)	115,276,284			-
Total other changes in net assets	(51,725)	(102,023,938)	174,997,423	(72,921,760)	-	-
Net Increase (Decrease) After Other Changes	(23,097)	(77,231,801)	97,405,881	45,578,644	(2,196,319)	63,533,308
Net Assets Held in Trust for Pension and Health Benefits:						
Beginning of Year	239,801	164,888,428	746,514,236	65,389,576	2,196,319	979,228,360
End of Year	$ 216,704	$ 87,656,627	$ 843,920,117	$ 110,968,220	$ -	$ 1,042,761,668

*Casualty Reserve is included.

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INVESTMENT SECTION

Prepared by Michigan Department of Treasury, Bureau of Investments

Jacqueline M. Johnson, CFA, Director

INVESTMENT SECTION

Report on Investment Activity

INTRODUCTION

The State Treasurer reports the investment activity quarterly to the Investment Advisory Committee (Committee), which reviews the investments, goals, and objectives of the retirement funds and may submit recommendations regarding them to the State Treasurer. The Investment Advisory Committee may also, by a majority vote, direct the State Treasurer to dispose of any holdings that, in the Committee's judgment, are not suitable for the funds involved, and may, by unanimous vote, direct the State Treasurer to make specific investments.

The Investment Advisory Committee was created by Act 380 of the Public Acts of 1965. The three public members of the five-member committee are appointed by the Governor with the advice and consent of the Senate for three-year terms. The Director of the Department of Labor and Economic Growth and the Director of the Department of Management and Budget are ex-officio members. In fiscal 2005, members of the Committee were as follows: David G. Sowerby, CFA (public member), Robert E. Swaney, CFA (public member), Marina v.N. Whitman (public member), David Hollister (ex-officio member), and Lisa Webb Sharpe (ex-officio member). The public members serve without pay, but may be paid actual and necessary travel and other expenses.

INVESTMENT POLICY & GOALS

Investment policy states that the fiduciary will operate within standard investment practices of the prudent person and in accordance with Public Employee Retirement System Investment Act 314 of 1965. The fiduciary is authorized to invest in government obligations, corporate debt obligations, various short-term debt obligations, corporate (domestic and international) stocks, venture capital interests, mutual funds, real estate interests, and other investments subject to specific parameters. Above all, pension fund assets are to be invested for the exclusive benefit of the members of the System.

The System's Proxy Voting Policy sets forth directives on the following issues: Boards of Directors, corporate governance, social issues, corporate restructurings and defenses. All proxies are reviewed and voted in accordance with the System's policy.

The primary function of the System is to provide retirement, survivor and disability benefits to its members. The State Treasurer is the sole investment fiduciary and custodian of the System's investments pursuant to State law. The primary investment objective is to maximize the rate of return on the total investment portfolio, consistent with a high degree of prudence and sufficient diversity to eliminate inordinate risks and to meet the actuarial assumption for the investment rate of return, at a reasonable cost achieved by cultivating a motivated team of dedicated professionals. The goals of the System are:

1. Achieve the optimal rate of return possible within prudent levels of risk.
2. Maintain sufficient liquidity to pay benefits.
3. Diversify assets to preserve capital and avoid large losses.
4. Meet or exceed the actuarial assumption over the long term.
5. Perform in the top half of the public plan universe over the long term.
6. Exceed individual asset class benchmarks over the long term.
7. Operate in a cost-effective manner relative to peers.

The strategy for achieving these goals is carried out by investing the assets of the System according to a five-year asset allocation model. The System currently has seven different asset classes, which provides for a well-diversified portfolio.

Report on Investment Activity (Continued)

Asset Allocation
(Excludes Collateral on Loaned Securities)

Investment Category	As of 9/30/05 Actual %		Five-Year Target %
Domestic Equity - Active	32.5%		34.0%
Large Cap Value Pool		15.2%	
Large Cap Growth Pool		15.6%	
Mid Cap Pools		0.9%	
Small Cap Pools		0.8%	
Domestic Equity - Passive	15.8%		14.0%
S&P 500 Index Pool		13.4%	
S&P MidCap Index Pool		2.1%	
S&P Small Cap Index Pool		0.3%	
International Equity Pool	12.4%		11.0%
International Equity Pool - Passive		11.8%	
International Equity Pool - Active		0.6%	
Alternative Investments Pool	11.7%		13.0%
Real Estate Pool	8.1%		10.0%
Fixed Income	16.8%		16.0%
Government Bond Pool		8.2%	
Corporate Bond Pool		8.6%	
Short Term Investment Pool	2.7%		2.0%
Total	**100.0%**		**100.0%**

INVESTMENT AUTHORITY

Pursuant to State Law (Section 91 of Act No. 380 of the Public Acts of 1965, as amended), the State Treasurer, State of Michigan, is the investment fiduciary for the following four State sponsored retirement systems: Michigan Public School Employees' Retirement System, Michigan State Employees' Retirement System, Michigan State Police Retirement System, and Michigan Judges' Retirement System.

Act No. 314 of the Public Acts of 1965, as amended, authorizes the investment of assets of public employee retirement systems or plans created and established by the State or any political subdivision.

INVESTMENT RESULTS

Total Portfolio Results

For the fiscal year ended September 30, 2005, the total System's rate of return was 12.9% as compiled by State Street Analytics. Annualized rates of return for the three-year period ending September 30, 2005, were 13.3%; for the five-year period were 2.9%; and for the ten-year period were 8.9%.

Returns were calculated using a time-weighted rate of return in accordance with standards of the CFA Institute, unless a modification is described in the discussion of the reported return.

These results were driven by double-digit returns from every major asset class except fixed income. Equity performance was a mirrored reflection of the previous year. Stocks started the year on a very strong note, reflecting the solid economy and low inflation. As the year drew to a close, several factors caused equity markets to level off. The U.S. Gulf Coast was

Report on Investment Activity (Continued)

wracked by Hurricanes Katrina and Rita that hindered oil and gas production. This sent energy prices soaring and inflation climbing. Interest rates were again volatile throughout the year. Alternative Investments continued to reap the benefits of a series of investments that were made in prior years. Real Estate gains reflected a favorable environment to also realize double-digit gains. Bonds experienced a relatively volatile year as the markets struggled with rising short-term rates countered by strong demand for long-term bonds. As a result, bonds turned in low single-digit gains for the year. Conversely, returns for the short-term pool improved throughout the year, benefiting from rising short-term rates.

For the fiscal year, the Dow Jones Industrial Average provided a total return of 7.2%, while the broader S&P 500 returned 12.3%. The Lehman Brothers U.S. Government/Credit Bond Index appreciated 2.6%.

The U.S. economy grew at a rate of 3.0% in fiscal year 2005 as measured by real gross domestic product. The first half of the period was stronger while the second half was buffeted by soaring energy prices and the devastation caused by twin hurricanes in the Gulf States. Corporate earnings remained robust, led by record earnings for energy companies. Inflation, as measured by the consumer price index, increased a relatively tame 3.2% in spite of higher energy prices.

The Federal Reserve continued its “measured pace” of monetary tightening in spite of economic disruptions caused by the hurricanes and with no apparent intention of stopping. It raised the Fed Funds rate by 0.25% at each of its eight Federal Open Market Committee meetings during the fiscal year. This resulted in a Fed Funds rate of 3.75% by the end of fiscal 2005, up two full percentage points from the prior year.

The System remains well diversified, both across and within asset classes, and positioned to benefit from moderate economic growth and rising interest rates.

Large Cap Value Pool

The primary objective of the pool of large company value stocks is to generate a rate of return from investment in common stocks and equity equivalents that exceeds that of the S & P Barra Value Index.

The pool invests in equities and equity-related securities primarily of U.S. companies with market capitalization generally greater than $5 billion that are significantly under-priced as measured by price-to-earnings and/or price-to-book value ratios and below fair value as determined by quantitative and qualitative models. The focus is on companies with a strong presence in depressed categories, experienced management and conservative accounting practices. At times a portion of the pool may be invested in fixed-income short-term securities with maturities of less than one year.

The pool invests in equities and equity related securities that are listed on U.S. national securities exchanges, including American Depository Receipts (ADRs). It may also invest in stocks that are traded over-the-counter. The pool diversifies its investments by allocating its equities into ten sectors, and monitors the weightings and performance of these sectors relative to that of the S & P Barra Value Index. The following summarizes the sector weightings of the pool as of September 30, 2005:

Finance	40.6 %
Consumer Discretionary	9.8
Energy	9.7
Industrials	8.6
Utilities	8.4
Technology	7.2
Health Care	7.0
Short Term Investments	3.7
Materials	3.0
Other	1.8
Consumer Staples	0.2
Total	**100.0** %

Report on Investment Activity (Continued)

The System's Large Cap Value pool achieved a total rate of return of 12.7% for fiscal 2005. This compared with 13.8% for the S&P 500 Barra Value Index.

At the close of fiscal year 2005, the Large Cap Value pool represented 15.2% of total investments. This compares to 16.7% for fiscal year 2004. The following summarizes the System's 2.2 % ownership share of the Large Cap Value pool at September 30, 2005:

Large Cap Value Pool
(in thousands)

Short Term Pooled investments	$	6,093
Equities		164,652
Settlement Principal Payable		(1,396)
Settlement Proceeds Receivable		731
Accrued dividends		133
Total	**$**	**170,213**

Large Cap Growth Pool

The primary investment objective is to generate a rate of return from investment in common stocks and equity equivalents that exceeds that of the S & P Barra Growth Index.

The pool invests in equities and equity-related securities primarily of U.S. companies with market capitalization generally greater than $5 billion whose earnings growth rates are expected to exceed the growth rate of the S & P 500 Index and are priced at or below fair value as determined by quantitative and qualitative models. The focus is on companies with a strong presence in categories anticipated to be fast growing, with high rates of unit sales growth and seasoned management. At times a portion of the pool may be invested in fixed-income short-term securities with maturities of less than one year.

The pool invests in equities and equity related securities that are listed on U.S. national securities exchanges, including American Depository Receipts (ADRs). It may also invest in stocks that are traded over-the-counter. The pool diversifies its investments by allocating its equities into ten sectors, and monitors the weightings and performance of these sectors relative to that of the S & P Barra Growth Index.

The following summarizes the sector weightings of various sectors in the pool as of September 30, 2005:

Technology	25.6	%
Health Care	16.9	
Consumer Staples	14.5	
Industrials	14.1	
Energy	9.7	
Consumer Discretionary	9.3	
Financials	4.0	
Short Term Investments	1.8	
Utilities	1.5	
Other	1.4	
Materials	1.2	
Total	**100.0**	%

Report on Investment Activity (Continued)

The Large Cap Growth pool's total rate of return was 8.5% for the fiscal year versus 10.7% for the S&P 500 Barra Growth Index.

At the close of fiscal year 2005, the Large Cap Growth pool represented 15.6% of total investments. This compares to 15.3% for fiscal year 2004. The following summarizes the System's 2.2% ownership share of the Large Cap Growth pool at September 30, 2005:

Large Cap Growth Pool
(in thousands)

Short Term Pooled investments	$	3,687
Equities		171,151
Settlement Principal Payable		(645)
Settlement Proceeds Receivable		357
Accrued dividends		192
Total	**$**	**174,742**

Mid Cap Pools

Four Mid Cap managers were selected in fiscal year 2005, and they began managing money for the System beginning May 2, 2005. They were funded from short-term investments out of the Large Cap Value and Large Cap Growth pools. Their investment objective is to generate a rate of return from investment in common stocks and equivalents that exceeds that of the S&P 400 Mid Cap Index.

The System invests in the Artisan Midcap, the Cramer Rosenthal McGlynn Midcap, the Los Angeles Capital Midcap Plus, and the Wellington Management Midcap pools.

The Mid Cap pools combined rate of return from inception to fiscal year end was 11.6%.

At the close of fiscal year 2005, the Mid Cap pools represented 0.9% of total investments. The following summarizes the System's ownership share and composition of the four Mid Cap pools at September 30, 2005:

Mid Cap Pools
(in thousands)

	Artisan Midcap	Cramer Rosenthal McGlynn	Los Angeles Capital Midcap	Wellington Management Midcap
Total Equities	$ 1,799	$ 2,952	$ 1,820	$ 3,030
Ownership Percentage	2.2%	2.2%	2.2%	2.2%

Small Cap Pools

The System invests in the Delaware and Putnam small cap growth pools. These are investment positions with the small company growth managers at Delaware Investment Advisors (Delaware) and Putnam Investments (Putnam). The primary investment objective of the small cap growth pools is to generate a rate of return from investment in common stocks and equivalents that exceeds that of the Russell 2000 Growth Index.

Report on Investment Activity (Continued)

The System's Small Cap Growth pool invested with Delaware achieved a total rate of return of 11.7% for fiscal 2005, while Putnam's total rate of return was 22.6%, resulting in a combined return of 15.2%. The Russell 2000 Growth Index total return was 18.0%.

Three Small Cap Value managers were selected at the beginning of the fiscal year to manage money for the System beginning October 1, 2004. They were funded from short term investments out of the Large Cap Value pool. The primary investment objective of the small cap value pools is to generate a rate of return from investment in common stocks and equivalents that exceeds that of the Russell 2000 Value Index.

The System invests in the Putnam, Northpointe, and Fisher small cap value pools. These are investment positions with the small company value managers at Putnam Investments (Putnam), Northpointe Capital (Northpointe) and Fisher Investments, Inc. (Fisher).

The System's Small Cap Value pool invested with Putnam achieved a total rate of return of 18.3% for fiscal 2005, Northpointe's total rate of return was 20.8% and Fisher's total rate of return was 18.1%, resulting in a combined return of 19.1%. This compared favorably with the Russell 2000 Value Index total return of 17.8%.

At the close of fiscal year 2005, the five Small Cap pools represented 0.8% of total investments. The following summarizes the System's ownership share and composition of the five pools at September 30, 2005:

Small Cap Pools
(in thousands)

	Delaware Growth	Putnam Growth	Putnam Value	Northpoint Value	Fisher Value
Total Equities	$ 3,403	$ 1,740	$ 1,283	$ 1,310	$ 1,280
Ownership percentage	2.3%	2.3%	2.2%	2.2%	2.2%

S&P 500 Index Pool

The objective of the enhanced S&P 500 Index pool is to closely match the return performance of its benchmark, the S&P 500 Index, and to use low risk strategies to offset transaction costs and add to performance when possible. The pool generally holds all 500 stocks that make up the Standard & Poor's 500 Index in proportion to their weighting in the index. The following summarizes the sector weightings of the pool as of September 30, 2005:

Financials	20.1 %
Information Technology	15.3
Health Care	13.3
Industrials	11.1
Consumer Discretionary	10.7
Energy	10.3
Consumer Staples	9.6
Utilities	3.6
Telecomm. Services	3.1
Materials	2.9
Total	**100.0** %

The S&P 500 Index pool return for the fiscal year was 12.3% versus the benchmark's 12.3%.

Report on Investment Activity (Continued)

At the close of fiscal year 2005, the S&P 500 Index pool represented 13.4% of total investments. This compares to 13.9% for fiscal year 2004. The following summarizes the System's 2.2% ownership share of the S&P 500 Index pool at September 30, 2005:

S&P 500 Index Pool
(in thousands)

Short Term Pooled investments	$	3,720
Equities		146,494
Hedge Contracts		7
Settlement Principal Payable		(69)
Accrued dividends		163
Total	**$**	**150,315**

S&P MidCap Pool

The objective of the S&P MidCap Index pool is to closely match the return performance of its benchmark, the S&P MidCap, and use low risk strategies to offset transaction costs and add to performance when possible. The pool invests in equities of mid-size firms.

The S&P MidCap Index pool return for the fiscal year was 22.3% versus its benchmark's 22.2%.

At the close of fiscal year 2005, the S&P MidCap Index pool represented 2.1% of total investments. This compares to 1.9% for fiscal year 2004. The following summarizes the System's 2.4% ownership share of the S&P MidCap Index pool at September 30, 2005:

S&P MidCap Index Pool
(in thousands)

Short Term Pooled investments	$	1,182
Equities		22,438
Hedge Contracts		4
Accrued dividends		13
Total	**$**	**23,637**

S&P Small Cap Index Pool

The objective of the S&P Small Cap Index pool is to match the return of its benchmark, the S&P 600 Small Cap Index. The S&P Small Cap Index pool return for the fiscal year was 21.2% versus the benchmark's 21.2%.

The pool achieves exposure to small cap equity returns primarily by investing in a combination of fixed income notes and equity swap agreements tied to the S&P 600 index. The total notional amount of the S&P 600 swap agreements is invested in dedicated fixed income notes. Interest from the dedicated notes is exchanged for S&P 600 stock returns. Use of swap agreements for a core position began in 2002, and an S&P 600 Exchange Traded Fund was added to this pool in 2004 to enhance management flexibility.

Report on Investment Activity (Continued)

At the close of fiscal year 2005, the S&P Small Cap Index pool represented 0.3% of total investments. This compares to 0.3% for fiscal year 2004.

The following summarizes the System's 2.2% ownership share of the S&P Small Cap Index pool at September 30, 2005:

S&P Small Cap Index Pool
(in thousands)

Short Term Pooled investments	$	24
Equities		524
Debt Securities		2,229
Hedge Contracts		421
Accrued dividends		5
Total	**$**	**3,203**

International Equities Pool - Passive

The objective of the International Equities Pool - Passive is to match the return performance of the S&P/Citigroup Broad Market Index (BMI) Europe and Pacific Composite (EPAC) adjusted for net dividends. Fifty percent of the benchmark is hedged to the U.S. Dollar and the other half is impacted by foreign currency exchange rate changes. The total passive international return was 27.3% in the fiscal year compared to the Citigroup BMI-EPAC return of 29.4%.

The passive international return was 22.8% for three years compared to the benchmark's return of 23.3% over the same period.

Core passive exposure to international equity returns is achieved primarily by investing in a combination of fixed income notes and equity swap agreements on foreign stock indices in developed markets. Interest on the dedicated notes is exchanged for international stock returns, and the total notional amount of the swap agreements is invested in the approximate proportions of the S&P/Citigroup Broad Market Index (BMI) Europe and Pacific Composite (EPAC) country weightings in related indices. Use of swap agreements for a core position began in 1993, an American Depository Receipts (ADR) and index-related security portfolio was added in June of 1999 to increase management flexibility, and a country fund portfolio was added in September of 2002 to improve exposure to the smallest companies in the BMI index.

The combination of fixed income LIBOR notes and equity swap agreements was valued at $118.6 million on September 30, 2005. That valuation included a net unrealized gain of $28.8 million on equity index exposures and an unrealized loss of $31 thousand on LIBOR note investments held. The combined Swap agreement and LIBOR portfolio structure continues to perform like a stock index fund that realizes all gains and losses on a rolling three year basis. During fiscal year 2005, $6.5 million of gains on equity exposures were realized, $1.8 million of interest in excess of obligations on completed swaps were recognized, and $11 thousand of gains on LIBOR notes were realized.

At the close of fiscal year 2005, the International Equities – Passive pool represented 11.8% of total investments. This compares to 10.9% for fiscal year 2004. The following summarizes the System's 2.2% ownership share of the International Equities Pool - Passive at September 30, 2005:

International Equities Pool - Passive
(in thousands)

Short Term Pooled investments	$	472
Equities		12,961
Debt Securities		89,787
Hedge Contracts		28,577
Accrued dividends and interest		483
Total	**$**	**132,280**

Report on Investment Activity (Continued)

International Equities Pool - Active

The primary investment objective is to generate a rate of return from investment in common stocks and equivalents that exceeds the S&P Citigroup Broad Market Index (BMI) World Ex-United States. All of the benchmark is impacted by foreign currency exchange rate changes.

The System invests in the Alliance International Large Cap Growth and Value pools. The pools represent equity investments managed by international value and growth managers at Alliance Capital. The pool is composed of 49.8% Large Cap Growth and 50.2% Large Cap Value.

The System's pool invested with Alliance Large Cap Growth achieved a total rate of return of 13.3% since the fund's inception on May 2, 2005, while Alliance Large Cap Value achieved a total rate of return of 16.1%, resulting in a combined return of 14.7%. This compared favorably with the S&P Citigroup Broad Market Index (BMI) World Ex-United States total return of 13.9%

At the close of fiscal year 2005, the International Equities - Active pool represented 0.6% of total investments. The following summarizes the System's 2.2% ownership share and composition of the pool at September 30, 2005:

International Equities Pools - Active
(in thousands)

	Alliance
Total Equities	$ 6,640

Alternative Investments Pool

The Alternative Investments pool objective is to meet or exceed the S&P 500 Index plus 300 basis points for all private equity pools over long time periods.

Alternative Investments are investments in the private equity market, primarily through limited partnerships. The following summarizes the weightings of the pool as of September 30, 2005:

Buyout Funds	59.7 %
Venture Capital Funds	16.4
Special Situation Funds	11.4
Fund of Funds and Hedge Funds	7.8
Mezzanine Funds	3.7
Short Term Investments	1.0
Total	**100.0 %**

The Alternative Investments pool had a return of 21.8% for the fiscal year ended September 30, 2005, as compiled by State Street Analytics versus the S&P 500 Index plus 300 basis points of 15.4%.

Credit Suisse Asset Management (CSAM) manages the stock distributions of the Alternative Investments. The CSAM pool return for the fiscal year ending September 30, 2005, was -9.0%.

Report on Investment Activity (Continued)

At the close of fiscal year 2005, the Alternative Investments pool represented 11.6% of total investments and Credit Suisse Asset Management pool represented 0.1% of total investments. This compares to 12.7% for Alternative and 0.1% for CSAM for fiscal year 2004. The following summarizes the System's ownership share and composition of the Alternative Investments pool and the Credit Suisse Asset Management pool at September 30, 2005:

Alternative Investments Pool
(in thousands)

	Alternative	CSAM
Short Term Pooled investments	$ 1,385	$ 25
Settlement Proceeds Receivable	-	7
Equities	129,613	581
Total	**$ 130,998**	**$ 613**
Ownership percentage	2.2%	2.2%

Real Estate Pool

The Real Estate pool seeks favorable risk-adjusted returns through rental income and appreciation of real estate investments. Real estate investments are typically held through various legal investment entities, such as limited partnerships or limited liability companies, established for the specific purpose of owning, leasing, managing, financing, or developing real estate and real estate related investments. Independent third parties regularly value the real estate investments to establish current market values.

The Real Estate pool may invest in each of the following four quadrants of the real estate capital markets:

- Private equity markets - An ownership interest in stabilized real estate assets, which may also include development and redevelopment of real estate.
- Public equity markets - Securities of publicly traded equity real estate companies whose primary purpose is to own, lease, manage, and develop real estate.
- Private debt markets - Mortgage loans secured by real estate.
- Public debt markets - Publicly traded commercial mortgage-backed securities market.

The Real Estate pool diversifies its holdings by:

- Geographic region - The pool is broadly diversified geographically across the country. Emphasis is placed upon U.S. real estate investments, but may also include foreign real estate investments. Foreign investments are currently less than one percent of the total equity value of the pool, and are not expected to exceed ten percent of the total equity value of the pool.
- Property (size and value) - The pool diversifies its holdings so that it is not concentrated in a few large real estate assets.
- Property type - The pool is diversified by type of property and by class of property.

Report on Investment Activity (Continued)

Major property types as of September 30, 2005:

Multi-family apartments	33.5	%
Commercial office buildings	22.1	
Retail shopping centers	13.0	
Hotels	11.1	
For sale housing, land, self-storage, and senior living	10.5	
Industrial warehouse buildings	7.4	
Short Term Investments	2.4	
Total	**100.0**	**%**

The net total return for the fiscal year ending September 30, 2005, was 14.4%, as compiled by State Street Analytics. This compares to the benchmark return of 18.4%. The benchmark is the National Council of Real Estate Investment Fiduciaries Property Index (NPI) less 75 basis points. The adjustment to the NPI is made to approximate industry comparable returns due to the fact that the Real Estate pool's returns are calculated net of all overhead and management fees, while the NPI calculates returns on a gross property level basis before overhead and standard investment management fees. The benchmark does not include short term investments, and the amount of purchase and sale activity during the fiscal year resulted in a high average short term investment balance that dampened performance within the Real Estate pool.

At the close of fiscal year 2005, the Real Estate pool had a total net equity value of $91.3 million that represented 8.1% of total investments. This compares to 7.4% for fiscal year 2004. The following summarizes the System's 2.3% ownership share of the Real Estate pool at September 30, 2005:

Real Estate Pool
(in thousands)

Short Term Pooled investments	$	2,202
Equities		89,072
Debt Securities		-
Total	**$**	**91,274**

Government Bond Pool

The objectives are to maximize the rate of return consistent with sound portfolio management principles and to outperform the benchmark, Lehman Brothers Government Index.

The pool invests in a diversified portfolio of government bonds including, but not limited to, treasuries, agencies, and government sponsored enterprises. To achieve above average returns, the pool emphasizes those sectors exhibiting the best risk reward relationship relative to historical norms and the outlook for interest rates.

For the fiscal year ending September 30, 2005, the Government Bond pool returned 3.4%, which compared favorably to the Lehman Brothers Government Index of 2.5%.

Rates continued to be volatile during the year. Ten-year treasuries started the year at 4.11%, rose to 4.64%, plunged to 3.89%, and ended at 4.33%. The yield curve continued to flatten with short and intermediate rates continuing to rise over the year while long rates declined marginally.

Report on Investment Activity (Continued)

The following summarizes the security type breakdown of the pool as of September 30, 2005:

U.S. Agency	60.4 %
GNMA	21.7
U.S. Treasury	9.7
U.S. Guaranteed	6.3
Short Term Investments	1.9
Total	**100.0** %

At the close of fiscal year 2005, the Government Bond pool represented 8.2% of total investments. This compares to 9.2% for fiscal year 2004. The following summarizes the System's 2.2% ownership share of the Government Bond pool at September 30, 2005:

Government Bond Pool
(in thousands)

Short Term Pooled investments	$	1,001
Debt Securities		89,967
Accrued dividends		753
Total	**$**	**91,721**

Corporate Bond Pool

The objectives are to maximize the rate of return consistent with sound portfolio management principles and to outperform the Lehman Brothers Credit Index.

The pool invests in a diversified portfolio of investment grade corporate issues. Such issues are rated in the top four categories by nationally recognized rating agencies. Non-rated bonds are acceptable if they are determined to be of comparable quality. To achieve above average returns, the pool emphasizes those sectors exhibiting the best risk reward relationship relative to historical norms and the outlook for interest rates.

For the fiscal year ending September 30, 2005, the Corporate Bond pool returned 2.1% compared to the Lehman Brothers Credit Index of 2.8%.

The pool's performance improved as the year progressed due to the continued rise in rates later in the year. The underperformance for the fiscal year reflected the strength of long rates early in the year declining from 4.9% in October 2004 to 4.19% in June before rising to 4.57% at year-end.

Report on Investment Activity (Continued)

The following summarizes the security type breakdown of the pool as of September 30, 2005:

Financials	39.9 %
Health Care	11.9
Consumer Discretionary	10.7
Industrials	9.4
Consumer Staples	7.3
Utilities	5.9
Materials	5.4
Other	4.0
Short Term Investments	3.3
Information Technology	2.2
Total	**100.0 %**

At the close of fiscal year 2005, the Corporate Bond pool represented 8.6% of total investments. This compares to 9.3% for fiscal year 2004. The following summarizes the System's 2.3% ownership share of the Corporate Bond pool at September 30, 2005:

Corporate Bond Pool
(in thousands)

Short Term Pooled investments	$	2,309
Debt Securities		92,595
Settlement Principal Payable		(174)
Accrued dividends		1,067
Total	**$**	**95,797**

Short Term Investments Pool

The objective of the Short Term Investment pool is to closely match the return performance of its benchmark, the 30 day Treasury bill. The Short Term Investment pool return for the fiscal year was 2.3% versus the benchmark's 2.5%.

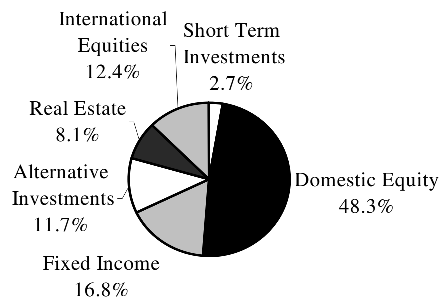
Potential areas of investment are:

- Obligations of the United States or its agencies.
- Banker's acceptances, commercial accounts, certificates of deposit or depository receipts.
- Repurchase agreements for the purchase of securities issued by the US government or its agencies.
- Commercial paper rated at the time of purchase within the two highest classifications established by not less than two national rating services as determined by the State Treasurer.

As of September 30, 2005, the Short Term Investment pool was 100% invested in commercial paper because of its advantages in yield and flexibility in maturities.

At the close of fiscal year 2005, the Short Term Investment pool represented 2.7% of total investments. This compares to 1.9% for fiscal year 2004. The System's ownership of the Short Term Investment pool at September 30, 2005, was $30,743,229 composed of debt securities and equity in common cash.

Asset Allocation – Security Type



Investment Results for the Period Ending September 30, 2005

Investment Category	Current Year	Annualized Rate of Return [1] 3 Years	5 Years	10 Years
Total Portfolio	12.9 %	13.3 %	2.9 %	8.9 %
Total Domestic Equity	11.8	16.8	(0.5)	10.0
S&P 1500 Index	13.4	17.5	(0.5)	9.8
Large Cap Value Pool	12.7			
Large Cap Growth Pool	8.5			
Mid Cap Pools	11.6			
Small Cap Value Pools	19.1			
Small Cap Growth Pools	15.2			
S&P 500 Index Pool	12.3			
S&P MidCap Index Pool	22.3			
S&P Small Cap Index Pool	21.2			
International Equity Pool - Passive	27.3	22.8	2.6	7.7
S&P Citigroup BMI - EPAC - 50/50	29.4	23.3	2.8	7.3
International Equity Pool - Active	14.7			
Alternative Investments Pool	21.8	14.5	0.9	12.8
S&P 500 Index plus 300 Basis Points	15.4	19.9	2.0	13.0
Credit Suisse Asset Management (Stock Distributions)	(9.0)			
Real Estate Pool	14.4	9.6	9.3	10.3
NCREIF Property Index minus 75 Basis Points	18.4	12.3	10.2	10.9
Total Fixed Income	2.7	3.9	6.2	6.3
Lehman Brothers Government/Credit	2.6	4.1	6.9	6.6
Government Bond Pool	3.4			
Corporate Bond Pool	2.1			
Short Term Investment Pool	2.3	1.6	2.4	4.2
30 Day Treasury Bill	2.5	1.5	2.2	3.5

[1] Calculations used a time-weighted rate of return based on the market rate of return in accordance with the CFA Institute's Performance Presentation Standards.

Largest Assets Held

Largest Stock Holdings (By Market Value)*
September 30, 2005

Rank	Shares	Stocks	Market Value
1	298,518	Exxon Mobil Corporation	$ 18,967,857
2	485,059	General Electric Corporation	16,360,527
3	333,926	Citigroup Incorporated	15,200,291
4	504,238	Microsoft Corporation	12,974,049
5	443,315	Pfizer Incorporated	11,069,569
6	206,403	Bank of America Corporation	8,689,575
7	133,273	Johnson and Johnson	8,433,509
8	131,100	American International Group	8,122,965
9	280,087	Intel Corporation	6,904,146
10	92,323	Altria Group Incorporated	6,805,137

Largest Bond Holdings (By Market Value)*
September 30, 2005

Rank	Par Amount	Description	Market Value
1	$ 5,065,414	U.S. Treasury Strip 0% Coupon Due 11-15-2011	$ 4,839,497
2	4,492,454	US Bank NA 4.07688% FRN Due 4-5-2007	4,492,214
3	4,484,780	Bank Nova Scotia FRN Due 10-12-2007	4,484,257
4	3,475,705	Wells Fargo & Company 3.75% FRN Due 8-4-2006	3,475,034
5	3,376,375	Canadian Imperial Bank 4.12688% FRN Due 1-5-2007	3,376,194
6	3,376,375	Wells Fargo & Company 4.06% FRN Due 9-28-2007	3,375,760
7	3,363,585	Household Finance Corporation 3.75% FRN Due 10-22-2007	3,362,984
8	3,363,585	Bayerische Landesbank NY 3.91063% FRN Due 3-17-2006	3,362,388
9	2,915,107	Citigroup Global Markets 3.75% FRN Due 1-30-2007	2,914,532
10	2,802,988	JPMorgan Chase & Co 3.76913% FRN Due 7-28-2006	2,802,471

* A complete list of stock and bond holdings is available from the Michigan Department of Treasury.

* The System's investments are commingled in various pooled accounts. Shares, par and market value represent the System's pro-rata ownernship through its ownership of the pools.

Schedule of Investment Fees

The State Treasurer is the investment fiduciary and custodian of the System's funds pursuant to State law. Outside advisors are utilized to augment the State Treasurer's internal staff. Only 21.8% of the total investment portfolio is managed by fully discretionary outside advisors. The Michigan Department of Treasury's cost of operations applicable to the System for the fiscal year amounted to $200 thousand or two and three tenths basis points (.023%) of the market value of the portfolio.

State law created an Investment Advisory Committee (Committee) comprised of the directors of the Department of Labor and Economic Growth and Department of Management and Budget, or their duly authorized representatives, and three public members appointed by the Governor with the advice and consent of the Senate. The public members serve without pay, but may be paid actual and necessary travel and other expenses. The Committee meets quarterly to review investments, goals and objectives and may submit recommendations to the State Treasurer. The Committee may also, by a majority vote, direct the State Treasurer to dispose of any holding, which in the Committee's judgment is not suitable for the fund involved, and may by unanimous vote direct the State Treasurer to make specific investments.

Schedule of Investment Fees

Investment Managers' Fees:

	Assets under Management	Fees	Basis Points *
State Treasurer	$ 875,923,105	$ 199,594	2.3
Outside Advisors -			
Mid Cap Equity	9,601,337	0	0.0
Small Cap Equity	9,016,287	69,673	77.3
International Equity	16,812,328	2,727	1.6
Alternative	130,193,505	1,184,989	91.0
Real Estate	79,247,365	17,471	2.2
Total	$ 1,120,793,927		

Other Investment Services Fees:

Custody & Research Fees	$ 1,090,050,352	$ 51,152
Security Lending Fees	643,477,913	29,530

* Outside Advisors Fees are netted against income for Small Cap, Mid Cap, and International Equity. For Alternative partnership agreements that define the management fees, the asset management fees range from 150 to 250 basis points of the committed capital. For Real Estate the asset management fee ranges from 50 to 125 basis points. Alternative and Real Estate fees, in most cases, are netted against income.

Schedule of Investment Commissions

	Commissions Paid [1]	Number of Shares Traded [1]	Average Commission Rate Per Share	Estimated Trade Costs Per Share	Estimated Research Costs Per Share	Estimated Trade Costs	Estimated Research Costs
	Fiscal Year Ended September 30, 2005						
Investment Brokerage Firms:							
Banc/America Secur LLC Montgomey Div	$ 4,234	87,659	$ 0.05	$ 0.03	$ 0.02	$ 2,630	$ 1,604
Bear, Stearns & Co. Inc.	14,242	321,603	0.04	0.03	0.01	9,648	4,594
Bridge Trading	11,519	253,586	0.05	0.03	0.02	7,608	3,912
BNY Brokerage Inc.	34	682	0.05	0.03	0.02	20	14
B-Trade Services LLC	71	3,548	0.02	0.02	0.00	71	0
Buckingham Research Group	2	43	0.05	0.03	0.02	1	1
Cantor Fitzgerald & Co.	2,857	94,317	0.03	0.02	0.01	1,886	971
Cap Institutional Services Inc. Equities	63	1,261	0.05	0.03	0.02	38	25
Charles Schwab Co., Inc.	709	14,170	0.05	0.03	0.02	425	283
Citigroup Global Markets, Inc.	23,297	576,773	0.04	0.03	0.01	17,303	5,993
Credit Suisse First Boston Corporation	16,402	363,131	0.05	0.03	0.02	10,894	5,508
Deutsche Bank Securities Inc.	3,301	70,566	0.05	0.03	0.02	2,117	1,184
Friedman Billings Ramsey	11	280	0.04	0.03	0.01	8	3
Fulcrum Global Partners	116	2,312	0.05	0.03	0.02	69	46
Goldman Sachs	21,410	509,569	0.04	0.03	0.01	15,287	6,123
Griswold Company	6,683	409,307	0.02	0.02	0.00	6,683	0
Howard Weil Division Legg Mason	535	13,370	0.04	0.03	0.01	401	134
Investment Technology Group Inc.	19	944	0.02	0.02	0.00	19	0
Instinet	139	4,620	0.03	0.03	0.00	139	0
ISI Group Inc.	4,697	97,523	0.05	0.03	0.02	2,926	1,771
J P Morgan Securities Inc.	8,584	192,977	0.04	0.03	0.01	5,789	2,795
Jones & Associates	36	710	0.05	0.03	0.02	21	14
Leerink Swann & Co.	88	1,856	0.05	0.03	0.02	56	32
Legg Mason Wood Walker	652	13,046	0.05	0.03	0.02	391	261
Lehman Brothers Inc.	23,283	603,726	0.04	0.03	0.01	18,112	5,171
Liquidnet Inc.	91	4,539	0.02	0.02	0.00	91	0
Merrill Lynch, Pierce, Fenner & Smith, Inc.	23,494	549,771	0.04	0.03	0.01	16,493	7,001
Morgan Stanley Co. Inc.	11,806	247,494	0.05	0.03	0.02	7,425	4,381
OTA Research	5,246	108,486	0.05	0.03	0.02	3,255	1,991
Pershing LLC	196	6,523	0.03	0.03	0.00	196	0
Pipeline Trading Systems LLC	12	577	0.02	0.02	0.00	12	0
Prudential Equity Group	10,445	231,326	0.05	0.03	0.02	6,940	3,506
Raymond James & Associates Inc.	14	273	0.05	0.03	0.02	8	5
RBC Capital Markets	108	2,151	0.05	0.03	0.02	65	43
SG Americas Securities LLC	10	203	0.05	0.03	0.02	6	4
S.G. Cowen & Co., LLC	7,968	164,088	0.05	0.03	0.02	4,923	3,045
Sanders Morris Mundy	151	3,021	0.05	0.03	0.02	91	60
Sanford Bernstein Co. LLC	6,301	136,147	0.05	0.03	0.02	4,084	2,217
State Street Brokerage Services	31	615	0.05	0.03	0.02	18	12
Suntrust Capital Markets Inc.	20	397	0.05	0.03	0.02	12	8
Thomas Weisel Partners	275	5,549	0.05	0.03	0.02	166	109
US Bancorp Piper Jaffray Inc.	85	1,697	0.05	0.03	0.02	51	34
UBS Securities LLC	13,456	308,567	0.04	0.03	0.01	9,257	4,199
US Clearing Corporation	19	374	0.05	0.03	0.02	11	7
Wayne Company	331	7,446	0.04	0.03	0.01	223	107
Weeden & Co.	298	5,995	0.05	0.03	0.02	180	119
Total	$ 223,341	5,422,818	$ 0.04 [2]	$ 0.03	$ 0.01	$ 156,049	$ 67,287

[1] Commissions are included in purchase and sale prices of investments. The commissions and shares represent the System's pro-rata share of commission and share transactions based on ownership in the investment pools.

[2] The average commission rate per share for all brokerage firms.

Investment Summary

Fiscal Year Ended September 30, 2005

	Market Value (a)	Percent of Total Market Value	Investment & Interest Income (b)	Percent of Investment & Interest Income
Fixed Income:				
Government Bond Pool	$ 91,721,025	8.2%	$ 2,963,382	2.2%
Corporate Bond Pool	95,796,787	8.6%	2,006,718	1.5%
Total Fixed Income Pools	187,517,812	16.8%	4,970,100	3.7%
Equity Pools	540,727,865	48.3%	58,195,757	43.9%
Real Estate Pool	91,273,569	8.1%	11,498,499	8.7%
Alternative Investment Pools	131,611,717	11.7%	26,602,825	20.1%
International Equities Pools	138,919,735	12.4%	30,381,768	22.9%
Short Term Investments Pool	30,743,229	2.7%	845,753	0.6%
Total	$ 1,120,793,927	100.0%	$ 132,494,702	99.9%

(a) Market value excludes $63,652,995 in cash collateral for security lending for fiscal year 2005.

(b) Total Investment & Interest Income excludes net security lending income of $88,446.

Investment Summary (Continued)

Fiscal Year Ended September 30, 2004

	Market Value (a)	Percent of Total Market Value	Investment & Interest Income (b, c)	Percent of Investment & Interest
Fixed Income:				
Government Bonds	$ 95,458,458	9.2%	$ 2,919,045	2.4%
Corporate Bonds	95,999,482	9.3%	3,628,675	3.0%
Total Fixed Income	191,457,940	18.5%	6,547,720	5.4%
Common and Preferred Stock	501,034,771	48.5%	60,323,855	50.1%
Real Estate and Mortgages	76,438,489	7.4%	6,477,066	5.4%
Alternative Investments	132,258,513	12.8%	28,120,518	23.3%
International Equities	112,428,766	10.9%	18,363,457	15.3%
Short Term Investments (b)	19,503,679	1.9%	597,997	0.5%
Total	$ 1,033,122,158	100.0%	$ 120,430,613	100.0%

(a) Market value excludes $8,385,825 and $65,551,067 in equity in common cash and cash collateral for security lending for fiscal year 2004.

(b) Total Investment & Interest Income excludes net security lending income of $75,701.

(c) Effective July 1, 2004, the System's investments were contributed to the various investment pools listed above. The income on investments for the first nine months of the fiscal year is reported as income for the pool to which the security was contributed.

ACTUARIAL SECTION

Actuary's Certification

SEGAL

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Michael J. Karlin, F.S.A., M.A.A.A.
Senior Vice President & Actuary
mkarlin@segalco.com

November 22, 2005

Ms. Lisa Webb Sharpe
Director
Department of Management and Budget
and
Retirement Board
Michigan State Police Retirement System
P.O. Box 30176
Lansing, Michigan 48909

Ladies and Gentlemen:

The Michigan State Police Retirement System (MSPRS) is funded on an actuarial reserve basis. The basic financial objective of MSPRS is to establish and receive contributions that remain approximately level as a percentage of active member payroll over a long period of years.

Actuarial valuations are prepared annually to determine MSPRS's actuarial liabilities and the employer contributions required to fund the System in accordance with the actuarial reserve funding provisions of the governing State Statute. The most recent actuarial valuation as of September 30, 2004 included a total of 4,596 members of MSPRS. The actuarial value of MSPRS's assets amounted to approximately $1,117.7 million on September 30, 2004.

The assumptions used in the 2004 valuation produce valuation results which we consider to be reasonably indicative of the plan's underlying cost. Also, in our opinion, the actuarial assumptions and methods used for funding purposes meet the parameters for the disclosures presented in the financial section by GASB Statement No. 25.

Our actuarial valuation of MSPRS as of September 30, 2004 was performed by qualified actuaries in accordance with accepted actuarial procedures. In our opinion, the calculated contribution rate meets the fundamental objectives of State law. Based on the 2004 valuation results, it is also our opinion that the Michigan State Police Retirement System continues in sound condition, in accordance with actuarial principles of level cost financing.

Most of the information used in the supporting schedules in the Actuarial and Statistical Sections, as well as the Schedules of Funding Progress and the employer contributions shown in the Schedules of Employer Contributions in the Financial Section of this report were provided by our firm.

Sincerely,

Michael Karlin

Michael Karlin, F.S.A., M.A.A.A.
Senior Vice President & Actuary

Summary of Actuarial Assumptions and Methods

1. The investment return rate used in making the valuations was 8% per year, compounded annually. This rate of return is not the assumed real rate of return. Considering other financial assumptions, this 8% investment return rate translates to an assumed real rate of return of 4.5%. Adopted 2004.

2. The mortality table used in evaluating allowances to be paid was the 1994 Group Annuity Mortality Table. Adopted 2004.

3. Sample probabilities of retirement with an age and service allowance are shown in Schedule 1 on the next page. Adopted 2004.

4. Sample probabilities of withdrawal from service and disability, together with individual pay increase assumptions, are shown in Schedule 2 on the next page. Adopted 2004.

5. Total active member payroll is assumed to increase 3.5% per year. This represents the portion of the individual pay increase assumptions attributable to inflation. In effect, this assumes no change in the number of active members. Adopted 1998.

6. An individual entry age actuarial cost method of valuation was used in determining age and service allowance actuarial liabilities and normal cost. Unfunded actuarial accrued liabilities, including actuarial gains and losses, are financed over a period of 50 years and over a declining 40 year period for years beginning October 1, 1986. Adopted 1986.

7. The Department of Management and Budget approved the use of market value of assets as of September 30, 1997, for actuarial valuation purposes. For investment gains or losses that occur after that date, a 5-year smoothing technique will be used. Specifically, the excess (shortfall) of actual investment income (including interest, dividends, realized and unrealized gains or losses) over the imputed income at the valuation interest rate is considered the gain (loss), which is spread over 5 years. Adopted 1997.

8. The data about persons now covered and about present assets was furnished by the System's administrative staff. Although examined for general reasonableness, the data were not audited by the actuary.

9. The actuarial valuation computations were made by or under the supervision of a Member of the American Academy of Actuaries (MAAA). The assumptions used in the actuarial valuations were adopted by the System's Board after consulting with the actuary.

Summary of Actuarial Assumptions and Methods (Continued)

SCHEDULE 1

Percent of Eligible Active Members Retiring Within Next Year

Retirement Ages	Not Electing DROP	Electing DROP	
First year eligible to retire			
49 and under	50 %	100 %	
After year eligible to retire			
46 and under	35	100	
47	25	100	
48-49	25	100	
		Over 25 Years	**Under 25 Years**
All Members			
50-51	20	100 %	20 %
52-60	25	100	25
61	50	100	50
62	70	100	70
63 and over	100	100	100

SCHEDULE 2

Separation From Active Employment Before Age & Service Retirement & Individual Pay Increase Assumptions

Sample Ages	Years of Service	Percent of Active Members Withdrawing Within Next Year (Men and Women)	Percent of Active Members Becoming Disabled Within Next Year		Percent Increase In Pay During Next Year*
All	0	6.50 %			93.50 %
	1	5.00			21.50
			Duty	**Non-duty**	
20	2 & Over	2.00	0.25 %	0.25 %	9.90
25	"	2.00	0.25	0.25	9.40
30	"	1.50	0.26	0.26	6.61
35	"	0.60	0.27	0.27	5.26
40	"	0.35	0.33	0.33	4.54
45	"	0.35	0.39	0.39	4.28
50	"	0.35	0.46	0.46	4.22
55	"		0.55	0.55	4.02
60 & Over	"		0.63	0.63	4.02

*These rates apply after 2 years of service. During the first 2 years, the assumed increases are 93.50% and 21.50% respectively.

Actuarial Valuation Data

Schedule of Active Member Valuation Data

Valuation Date Sept. 30	Number	Reported Annual Payroll	Average Annual Pay	% Increase	Average Age	Average Service
1995	2,181	$ 104,500,048	$ 47,914	7.7 %	37.9	13.0
1996	2,135	106,826,272	50,036	4.4	38.2	13.1
1997	2,090	110,085,960	52,673	5.3	38.2	12.9
1998	2,220	108,183,040	48,731	(7.5)	37.5	11.6
1999	2,216	116,910,216	52,757	8.3	37.0	11.5
2000	2,210	116,558,417	52,741	(0.0)	37.2	11.6
2001	2,137	118,788,227	55,586	5.4	37.9	12.2
2002	2,048	124,366,038	60,726	9.3	38.5	12.8
2003	1,848	113,201,430	61,256	0.9	38.3	12.5
2004 [1]	1,831	119,721,613	65,386	6.7	38.1	10.6

[1] Excludes 51 additional DROP program participants who are still actively employed.

Retirant and Beneficiary Data Rolls End of Year

Year Ended Sept. 30	Number			Average Monthly Benefit			Average Age		
	Pensioners	Widows	Children	Pensioners	Widows	Children	Pensioners	Widows	Children
1995	1,548	279	4	$ 1,770	$ 962	$ 100	60.8	69.6	14.8
1996	1612	397	6	1,845	1,001	100	61.6	69.3	10.3
1997	1,703	310	5	1,963	1,192	419	62.5	70.4	10.7
1998	1,820	314	5	2,062	1,225	499	62.8	71.0	10.1
1999	1,893	334	4	2,141	1,263	499	63.1	71.5	10.8
2000	1,968	345	6	2,227	1,308	366	61.9	71.9	10.4
2001	2,023	353	6	2,298	1,357	366	62.5	73.3	11.4
2002	2,095	361	6	2,378	1,415	366	62.6	72.7	16.3
2003	2,280	364	5	2,506	1,464	419	62.2	73.1	16.3
2004	2,167	313	8	2,609	1,502	475	62.8	73.5	17.5

Prioritized Solvency Test

The System's funding objective is to meet long term benefit promises through contributions that remain approximately level from year to year as a percent of member payroll. If the contributions to the System are level in concept and soundly executed, the System will pay all promised benefits when due, the ultimate test of financial soundness. Testing for level contribution rates is the long-term solvency test.

A prioritized solvency test is another means of checking a system's progress under its funding program. In a short condition test, the plan's present assets (cash and investments) are compared with: (1) active member contributions on deposit; (2) the liabilities for future benefits to present retired lives; and (3) the liabilities for service already rendered by active and inactive members. In a system that has been following the discipline of level percent of payroll financing, the liabilities for active member contributions on deposit (liability 1) and the liabilities for future benefits to present retired lives (liability 2) will be fully covered by present assets (except in rare circumstances). In addition, the liabilities for service already rendered by active members (liability 3) is normally partially covered by the remainder of present assets. Generally, if the System has been using level-cost financing, the funded portion of liability 3 will increase over time. Liability 3 being fully funded is not necessarily a by-product of level percent of payroll funding methods.

The schedule below illustrates the history of the liabilities of the System and is indicative of the System's policy of following the discipline of level percent of payroll financing.

	Actuarial Present Value of Actuarial Accrued Liability (in Thousands)				Portion of Present Value Covered by Assets			
Valuation Date Sept. 30	(1) Active Member Contributions	(2) Retirants and Beneficiaries	(3) Active and Inactive Members (Employer Financed Portion)	Valuation Assets	(1)	(2)	(3)	(4) [3]
1995	$ 1,497	$ 422,960	$ 374,363	$ 622,626	100 %	100 %	52.9 %	77.9 %
1996	1,183	459,985	362,293	697,923	100	100	65.3	84.8
1997	847	516,379	363,100	787,240	100	100	74.4	89.4
1997 [1]	847	516,379	363,100	928,714	100	100	113.3	105.5
1997 [2]	847	516,379	395,533	928,714	100	100	104.0	101.7
1998	614	593,169	349,941	974,365	100	100	108.8	103.2
1998 [3]	614	604,724	357,130	974,365	100	100	103.3	101.2
1999	464	643,284	362,780	1,036,840	100	100	108.4	103.0
2000	383	685,272	355,059	1,113,065	100	100	120.3	107.0
2001	368	717,244	356,021	1,148,609	100	100	121.1	107.0
2002	329	759,929	375,400	1,141,348	100	100	101.5	100.5
2003	240	861,504	324,666	1,139,138	100	100	85.4	96.0
2004 [4]	217	894,962	360,646	1,117,704	100	100	61.7	89.0

[1] Revised asset valuation method.

[2] Revised inflation assumption.

[3] Revised asset valuation assumptions.

[4] Change in assumptions and benefit provisions.

Analysis of Financial Experience

Gains/(Losses) in Accrued Liabilities During Year Ended September 30, 2004
Resulting from Differences Between Assumed Experience & Actual Experience

	Type of Activity	Gain/(Loss)
1.	**Retirements (including Disability Retirement).** If members retire at older ages or with lower final average pay than assumed, there is a gain. If younger ages or higher average pays, a loss.	$ 5,599,341
2.	**Withdrawal From Employment** (including death-in-service). If more liabilities are released by withdrawals and deaths than assumed, there is a gain. If smaller releases, a loss.	(12,494)
3.	**Pay Increases.** If there are smaller pay increases than assumed, there is a gain. If greater increases, a loss.	(11,944,708)
4.	**Investment Income.** If there is greater investment income than assumed, there is a gain. If less income, a loss.	(57,683,625)
5.	**Death After Retirement.** If retirants live longer than assumed, there is a loss. If not as long, a gain.	(4,557,110)
6.	**New entrants.** New entrants into the System will generally result in an actuarial loss. This does not apply to plans closed to new entrants.	(117,165)
7.	**Other.** Miscellaneous gains and losses resulting from data adjustments, timing of financial transactions, etc.	17,365,956 *
8.	**Composite Gain (or Loss) During Year**	$ (51,349,805)

* Consists primarily of gain of approximately $18 million due to a change in the reporting of benefit service (prior to 2004, data included time worked in other Michigan systems, as well as overstating credited service of part-time employees).

Summary of Plan Provisions

Our actuarial valuation of the System as of September 30, 2004, is based on the present provisions of Public Act 182 of 1986, as amended.

Regular Retirement

Eligibility - 25 years of credited service with no age requirement; or age 50 with 10 years credited service.

Annual Amount - If member has 25 or more years of credited service, 60% of final average compensation; if member has less than 25 years of credited service, total credited service times 2% of final average compensation.

Type of Final Average Compensation - Average of 2 final years.

Early Retirement

None.

Deferred Retirement (vested benefit)

Eligibility - 10 years of credited service. Benefit commences at age 50.

Annual Amount - Computed as Regular Retirement benefit based on credited service and final average compensation at termination.

Duty-Disability Retirement

Eligibility - No age or service requirement.

Annual Amount - 60% of final average compensation. Disability benefit plus workers' compensation benefit, if any, shall not exceed 100% of final average compensation.

Non-Duty Disability Retirement

Eligibility - 10 years of credited service.

Annual Amount - 2.4% of final average compensation times years of credited service, to a maximum of 60% of final average compensation.

Duty Death Before Retirement

Eligibility - No age or service requirement.

Annual Amount - 60% of final average compensation is payable to surviving spouse; additional $1,200 per year for each child under 18 is also payable. If no surviving spouse, children under 18 share in 60% benefit until attainment of age 18. If no spouse or children, dependent parents are eligible for 60% benefit (plus $1,200 per dependent sibling under 18). Retirement benefit plus workers' compensation, if any, shall not exceed 100% of final average compensation.

Lump Sum Payment - A $1,500 funeral benefit is also payable.

Summary of Plan Provisions (Continued)

Non-Duty Death Before Retirement

Eligibility - 10 years of credited service.

Annual Amount - 2.4% of final average compensation times years of credited service, to a maximum of 60% of final average compensation, payable to surviving spouse. If no surviving spouse, children under 18 share in benefit until attainment of age 18.

Death After Retirement

The retired member's benefit continues to the surviving spouse. If no surviving spouse, children under 18 share in the continued benefit until attainment of age 18.

DROP Program Provisions

DROP Eligibility - Any age with 25 years of service.

Maximum Years of DROP - 6 years.

Retirement Benefit - Monthly benefit frozen at date of DROP election.

DROP Account – Amount credited – 100% of the participant's Retirement Benefit if stay full six years (for all 6 years); 90% if stay 5 years; 80% if stay 4 years; 70% if stay 3 years; 60% if stay 2 years; 50% if stay 1 year; 30% if stay less than 1 year.

Interest Rate - 3%

COLA - No Cola adjustment on Retirement Benefit until the end of the DROP period.

Benefit Options - At termination of DROP participation and commencement of retirement, options are lump sum of DROP account, partial lump sum, or maintain funds in account.

Post-Retirement Cost-of-Living Adjustments

All members retiring (or leaving employment with vested benefits), and their survivors, are eligible for automatic 2% annual (non-compounded) benefit increases, with a maximum annual increase of $500.

Post-Retirement Health Insurance Coverage

Persons in receipt of retirement allowances, and their dependents, are eligible for 95% State-paid health insurance coverage and 90% State-paid dental and vision insurance.

Member Contributions

None.

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STATISTICAL SECTION

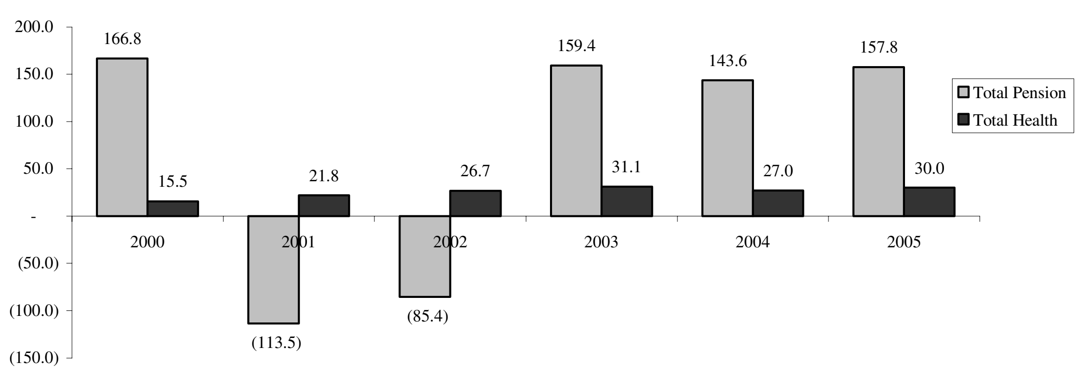
Schedule of Pension Plan Revenues by Source

Fiscal Year Ended Sept. 30	Member Contributions	Employer Contributions Dollars	Employer Contributions % of Annual Covered Payroll	Net Investment & Other Income	Total
2000	$ 16,793	$ 22,107,292	19.0 %	$ 144,657,843	$ 166,781,928
2001	197,234	24,064,039	20.3	(137,798,523)	(113,537,250)
2002	113,114	22,456,469	18.1	(108,017,248)	(85,447,665)
2003	78,111	25,931,762	22.9	133,377,555	159,387,428
2004	30,062	24,792,137	N/A	118,817,294	143,639,493
2005	112,303	26,607,572	N/A	131,111,123	157,830,998

Schedule of Health Plan Revenues by Source

Fiscal Year Ended Sept. 30	Member Contributions	Employer Contributions Dollars	Employer Contributions % of Annual Covered Payroll	Net Investment & Other Income	Total
2000	$ 1,098,440	$ 14,421,517	12.4 %		$ 15,519,957
2001	1,265,408	20,581,979	17.3		21,847,387
2002	1,380,199	25,270,639	20.3		26,650,838
2003	1,501,196	29,620,331	26.2		31,121,527
2004	1,572,372	25,426,780	N/A		26,999,152
2005	1,566,646	28,488,384	N/A		30,055,030

Total Revenue
Year Ended September 30
(in millions)



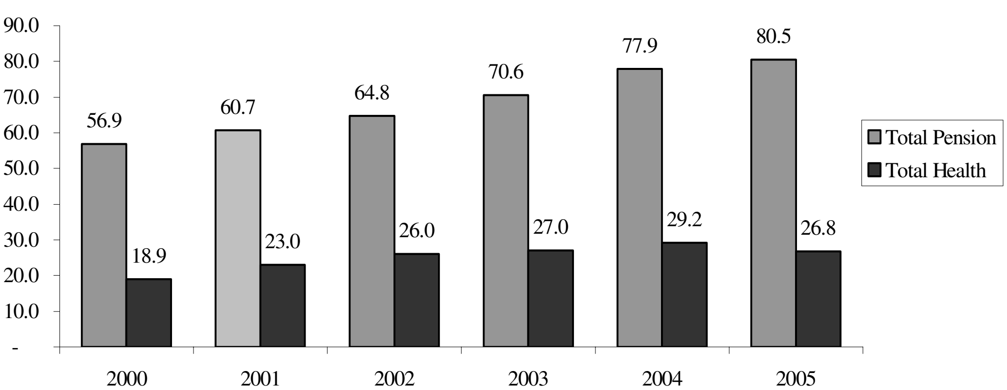
Schedule of Pension Plan Expenses by Type

Fiscal Year Ended Sept. 30	Benefit Payments	Refunds and Transfers	Administrative and Other Expenses	Total
2000	$ 56,693,183		$ 158,935	$ 56,852,118
2001	60,407,395	$ 6	298,711	60,706,112
2002	64,418,130		353,403	64,771,533
2003	70,152,288		423,745	70,576,033
2004	77,591,542	1,434	316,890	77,909,866
2005	80,169,608	358	294,183	80,464,149

Schedule of Health Plan Expenses by Type

Fiscal Year Ended Sept. 30	Benefit Payments	Refunds and Transfers	Administrative and Other Expenses	Total
2000	$ 18,938,222			$ 18,938,222
2001	23,024,104			23,024,104
2002	26,029,522			26,029,522
2003	27,035,862			27,035,862
2004	29,195,471			29,195,471
2005	26,842,248			26,842,248

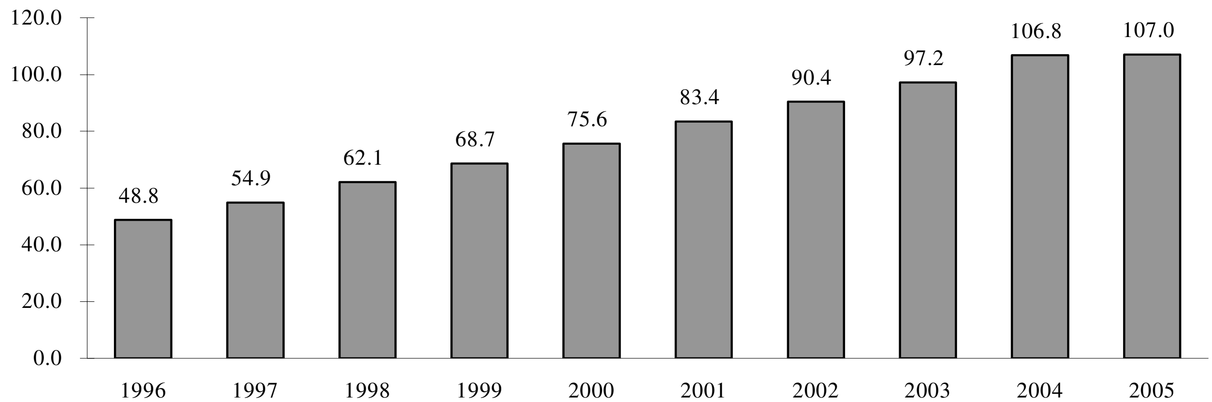
Total Expenses
Year Ended September 30
(in millions)



Schedule of Benefit Expenses by Type

Fiscal Year Ended Sept. 30	Regular Benefits	Disability Benefits	Funeral Benefits	Health Benefits	Total
1996	$ 35,794,961	$ 2,482,429	$ 1,500	$ 10,516,619	$ 48,795,509
1997	40,536,134	2,782,100		11,594,161	54,912,395
1998	45,216,692	3,010,640		13,856,103	62,083,435
1999	49,330,784	3,155,805		16,206,544	68,693,133
2000	53,466,267	3,223,915	3,000	18,938,222	75,631,405
2001	57,019,158	3,388,237		23,024,104	83,431,499
2002	60,747,711	3,670,419		26,029,522	90,447,652
2003	66,277,685	3,873,103	1,500	27,035,862	97,188,150
2004	73,358,911	4,232,631		29,195,471	106,787,013
2005	75,606,407	4,563,201		26,842,248	107,011,856

Total Benefit Expenses
For Year Ended September 30
(in millions)



Schedule of Retired Members by Type of Benefit

September 30, 2004

Amount Monthly Benefit	Number of Retirees	Type of Retirement *						Option**
		1	2	3	4	5	6	Life
$ 001 - 400	36	26	1	2	1	4	2	36
401 - 800	145	118	7	4	6	0	10	145
801 - 1,200	317	145	122	22	3	16	9	317
1,201 - 1,600	300	180	72	27	10	6	5	300
1,601 - 2,000	200	148	21	16	5	3	7	200
2,001 - 2,400	155	108	19	15	7	2	4	155
2,401 - 2,800	352	295	25	23	6	1	2	352
2,801 - 3,200	498	469	11	10	3	2	3	498
3,201 - 3,600	385	375	4	4	0	0	2	385
3,601 - 4,000	209	204	1	4	0	0	0	209
Over 4,000	100	99	0	1	0	0	0	100
Totals	2,697	2,167	283	128	41	34	44	2,697

* Type of Retirement
1 - Normal retirement for age & service
2 - Survivor payment - normal retirement
3 - Duty disability retirement
4 - Non-duty disability retirement
5 - Survivor payment - duty death in service
6 - Survivor payment - non-duty death in service

**Selected Option
Life - 100% Joint and Survivors

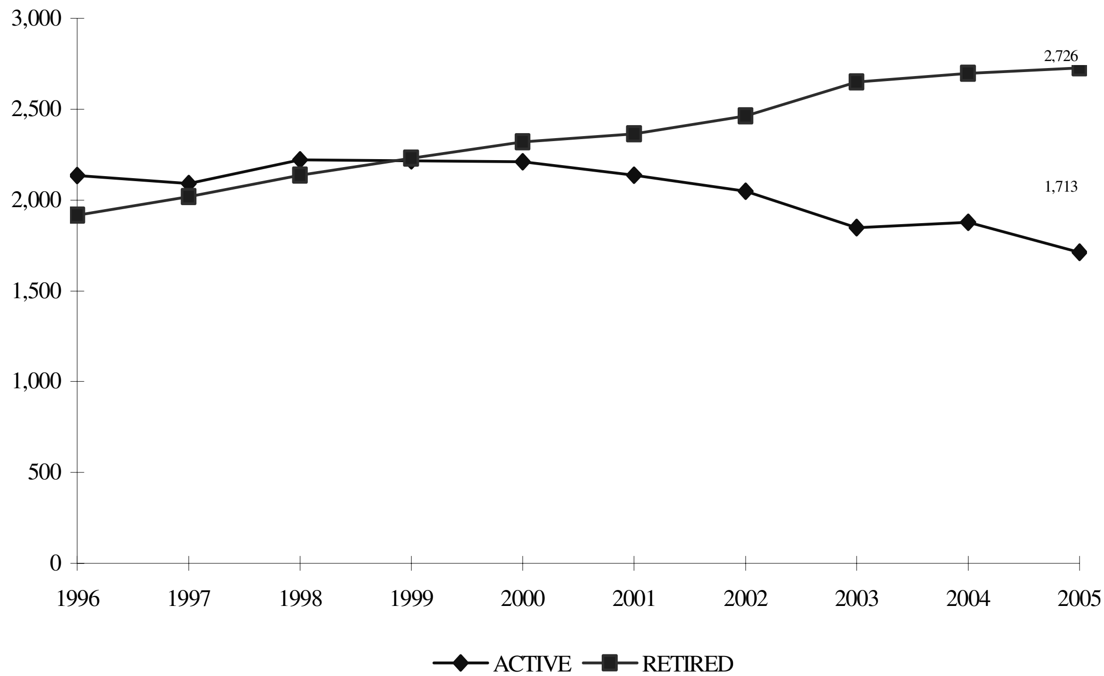
Source: The Segal Company

Schedule of Average Benefit Payments

Retirement Effective Dates	Years Credited Service							
	0-5	5-10	10-15	15-20	20-25	25-30	30+	Total
Period 10/1/98 to 9/30/99:								
Average Monthly Benefit	$ 731	$ 1,188	$ 819	$ 1,114	$ 1,351	$ 2,084	$ 2,392	$ 1,936
Average Final Average Salary	2,116	21,238	23,006	22,791	26,112	36,912	44,432	34,509
Number of Active Retirants	98	22	75	70	98	1,548	227	2,138
Period 10/1/99 to 9/30/00:								
Average Monthly Benefit	$ 746	$ 1,196	$ 856	$ 1,120	$ 1,401	$ 2,173	$ 2,489	$ 2,006
Average Final Average Salary	1,852	22,257	24,530	22,790	27,318	38,441	45,879	35,702
Number of Active Retirants	112	23	85	70	102	1,601	238	2,231
Period 10/1/00 to 9/30/01:								
Average Monthly Benefit	$ 938	$ 1,408	$ 854	$ 1,124	$ 1,421	$ 2,267	$ 2,569	$ 2,086
Average Final Average Salary	8,313	25,199	24,827	23,537	27,727	39,975	47,088	37,065
Number of Active Retirants	141	25	86	67	103	1,651	246	2,319
Period 10/1/01 to 9/30/02:								
Average Monthly Benefit	$ 1,074	$ 1,464	$ 891	$ 1,164	$ 1,451	$ 2,344	$ 2,618	$ 2,154
Average Final Average Salary	11,602	26,268	25,563	24,298	27,958	41,278	47,650	38,158
Number of Active Retirants	161	29	85	63	107	1,684	253	2,382
Period 10/1/02 to 9/30/03:								
Average Monthly Benefit	$ 1,689	$ 1,579	$ 915	$ 1,299	$ 1,572	$ 2,546	$ 2,848	$ 2,359
Average Final Average Salary	14,507	31,832	25,938	27,928	29,701	44,536	50,383	39,364
Number of Active Retirants	240	32	94	69	105	1,838	271	2,649
Period 10/1/03 to 9/30/04:								
Average Monthly Benefit	$ 860	$ 1,613	$ 1,010	$ 1,425	$ 1,638	$ 2,642	$ 2,896	$ 2,413
Average Final Average Salary	1,192	32,786	27,675	30,487	30,472	46,696	52,623	42,564
Number of Active Retirants	165	30	101	77	105	1,940	279	2,697

Source: The Segal Company

Ten Year History of Membership
Fiscal Year Ended September 30



Source: The Segal Company

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The *Michigan State Police Retirement System Comprehensive Annual Financial Report* is prepared by Financial Services, Fiscal Management Division. Staff of the division for the fiscal year 2004-2005 report included:

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The report may be viewed on-line at: www.michigan.gov/ors