

Michigan State Police Retirement System
a Pension Trust Fund of the State of Michigan

**Comprehensive Annual Financial Report
for the Fiscal Year Ended September 30, 2006**



M S P R S

**Prepared by:
Financial Services
for
Office of Retirement Services
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INTRODUCTORY SECTION

Certificate of Achievement
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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, 2005

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.



President

Executive Director

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 8, 2006

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 2006.

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

Public Pension Standards Award



**Public Pension Coordinating Council
Public Pension Standards**

2006 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)

A handwritten signature in cursive script that reads "Alan H. Winkle".

Alan H. Winkle
Program Administrator

INTRODUCTORY SECTION

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, 2005. Actuarial certification and supporting statistics are included in the Actuarial Section of this report.

Report

The 2006 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 System 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 8.1%. A summary of asset allocation and rates of return can be found in the Investment Section of this report.

INTRODUCTORY SECTION

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, 2005. The actuarial value of the assets and actuarial accrued liability of the System were \$1.1 billion and \$1.3 billion, respectively, resulting in a funded ratio of 83.8% at September 30, 2005. 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, 2005, 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 \$467 million and the employer contribution for health care benefits would be 30.0% of payroll.

MAJOR GOALS ACCOMPLISHED

The Michigan Department of Management and Budget, Office of Retirement Services continues to be proactive in identifying and meeting the needs of our customers in a timely and cost-effective manner. Moving forward with our Vision ORS technology project, we implemented a number of solutions that streamline internal process functions, thereby freeing staff to provide more personal one-on-one interactions with customers. Our greatest gains this year came when we converted from our old pension system (CPP) to a new, leading-edge pension payment processing system (Clarety). The new system permits staff access to up-to-date customer information all in a single place and enables us to process pension payments daily instead of once a month, which allows initial pension payments to be issued faster. Other improvements are highlighted below.

Focus on Our Customer

Planning and saving for retirement early in your career received significant emphasis as we interacted with our customers. We encouraged members to take a serious look at their retirement plans to help them be better prepared for a more secure and fulfilling experience when it is time to retire. We used a variety of easy to understand resources to deliver our messages. We redesigned our websites using a life stages approach, making it easier for customers to find the information they need, regardless of whether they're just starting their career or nearing retirement. Our informational booklet for state troopers was completely revamped this year to incorporate the life stages approach to retirement.

INTRODUCTORY SECTION

Letter of Transmittal (Continued)

Forty-three troopers who were nearing retirement eligibility attended a preretirement meeting to learn about the options available to them at retirement. Those who attended this meeting could schedule a personalized telephone appointment to address any specific questions or concerns they might have before retiring.

Most of our customers still view the telephone as their primary means of communicating; this year our Customer Service telephone center answered 216,650 calls. A growing number of customers have found email correspondence better meets their busy lifestyles as demonstrated by the 14,106 emails we responded to this year. Our Customer Service staff also provided face-to-face interaction with 5,387 individuals who visited our main office. Our Detroit office staff met with 2,903 customers who either scheduled an appointment or walked in with questions, and answered 5,606 telephone calls with customers.

Our customer base extends to employers also, and this year we continued enhancing these relationships through regular communications and updated support materials. To strengthen our rapport with our employers, we used email updates to stay connected with our contacts.

Continuously Improve Processes

For the last several years, we have invested substantial time and effort to transform ORS into a leading edge process-based organization. This year we celebrated some of our milestones – our on-line employer reporting and pay-period reporting process is fully implemented and stabilized, and we converted to our new pension payment processing system without incident. Both of these process enhancements are paying off through increased efficiencies and improved services to our external customers as well as our staff.

With the implementation of our new technology enhancements, our work processes are changing, which opens the door for other process improvements. Recognizing this opportunity, our reengineering team began assessing how six of our present processes, consisting of 47 tasks, function and then identified gaps to be resolved, efficiencies to be gained, and savings to reap.

ORS' influence is seen at the national level as well. Because of its reputation, ORS has provided leadership to the Board of National Sector Public Health Care Roundtable. This organization was instrumental in convincing Congress to include public sector health plans in the group eligible to receive the Medicare Part D subsidy. This subsidy is worth about \$103 million annually to the State and the schools.

Promote a Positive Work Environment

Like many other progressive organizations, the need for change has become the norm rather than the exception. With the introduction of technology changes to our core processes, we needed to realign our organizational structure. Clear, straight-forward communications between managers and employees eased the transition.

Management has fostered an open, positive work environment where employees feel they are valued and appreciated. They are empathetic and supportive of others, generously giving to those in need, whether it's donating blood to the Red Cross, volunteering for Habitat for Humanity, or making contributions to United Way, the local food banks, troops stationed in Iraq, holiday giving trees, or a coworker experiencing personal hardships.

Management encourages employees to live out the values of Integrity, Inclusion, Excellence, and Teamwork. This year we instituted an awards program similar to DMB's annual Excellence Awards program to recognize individuals in the categories of Leadership, Innovation, Every Day Hero, Living the Values, and Customer Service. From this group of honorees, who were also nominated for the DMB Excellence Awards, a team of five ORS employees was honored with DMB's Innovator Award.

INTRODUCTORY SECTION

Letter of Transmittal (Continued)

Optimize Technology

Since the recent implementation of our new technology we've identified other ways to enhance our operations. Imaging of current correspondence and documents expanded to include employer correspondence as well as member and retiree correspondence. We've also undertaken an extensive project to begin converting existing paper files to electronic images so staff can quickly access them with a few clicks of a mouse rather than waiting for a paper file to be pulled. As part of this conversion, we scanned 4,680,816 images this year, providing more electronic access to insurance information, death records, tax deferred payment agreements, and pending retiree documentation, and further reducing our reliance on paper documents.

Our Internet activity is expanding as we begin using it for video conferences for employers and pending retirees. This technology improves the reliability and quality of our video presentations. We continue to explore additional opportunities to deliver information to our customers in a fast, convenient, efficient way.

Future enhancements to our pension system continue to move forward. This year we completed the requirements gathering steps for web self service and automating the processing of our forms and letters by using bar coding to speed document handling and trigger work flow processes.

We've learned a number of lessons from our past Vision ORS implementation efforts, and we've used this knowledge to help avoid these pitfalls as we move forward. We're writing better requirements in the initial stages and doing extensive testing of processes before upgrading our system, which has paid off in much smoother program deployments.

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, 2005. 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 15 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.

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 2006. This is the third 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

INTRODUCTORY SECTION

Letter of Transmittal (Continued)

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



Phillip J. Stoddard, Acting Director
Office of Retirement Services

INTRODUCTORY SECTION

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

Jan Miller
Representing Director, Office of State
Employer
Statutory Member

Craig Murray
Representing Deputy Auditor General
Statutory Member

Mark Haas
Representing State Treasurer
Statutory Member

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

Diane Garrison
Retiree Member
Term Expires December 31, 2008

* 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

Actuaries

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

Gabriel Roeder Smith & Company
Alan E. Sonnanstine
Southfield, Michigan

Legal Advisor

Mike Cox
Attorney General
State of Michigan

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

Robert J. Kleine
State Treasurer
State of Michigan

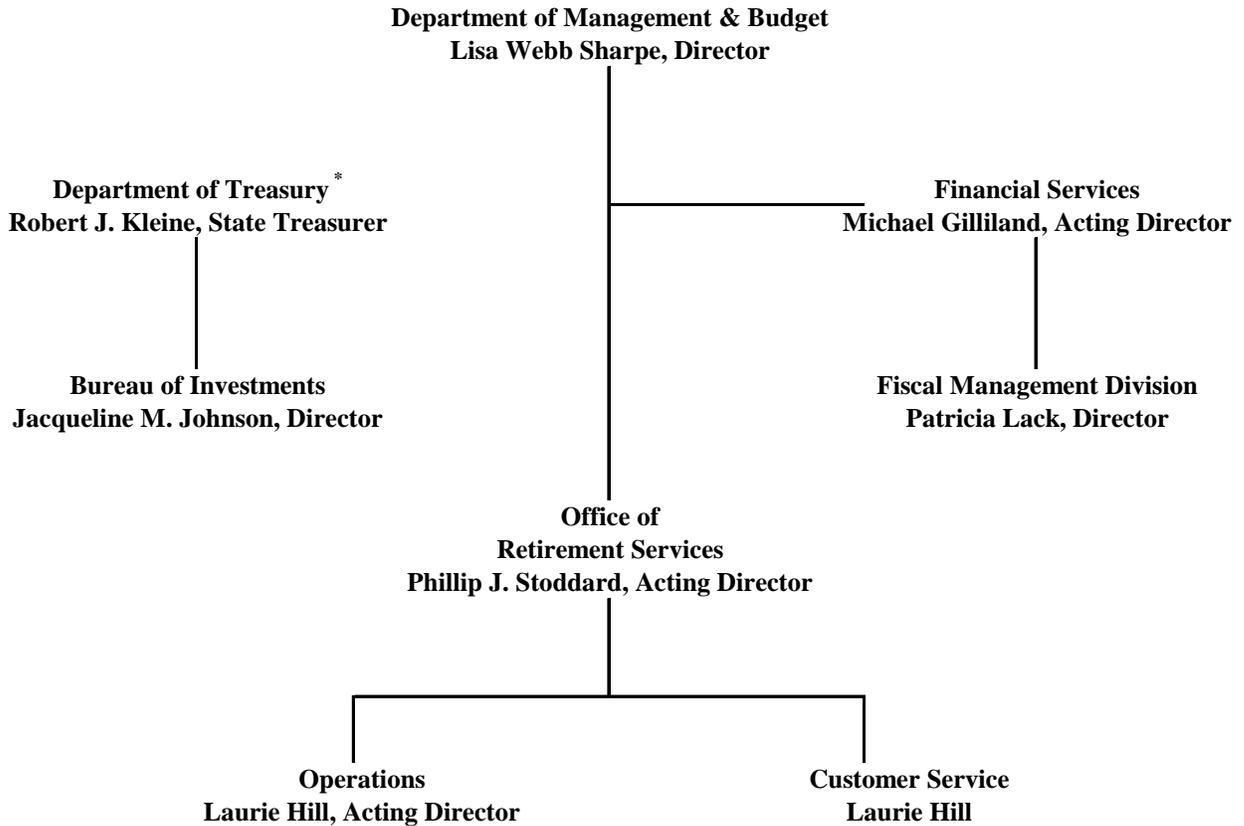
Investment Performance Measurement

State Street Corporation
State Street Analytics
Boston, MA

INTRODUCTORY SECTION

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.

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FINANCIAL SECTION

Independent Auditor's Report
Management's Discussion and Analysis
Basic Financial Statements
Notes to Basic Financial Statements
Required Supplementary Information
Notes to Required Supplementary Information
Supporting Schedules

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. Phillip Stoddard, Acting 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, 2006 and 2005, 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, 2006 and 2005, 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 8, 2006 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.

Independent Auditor's Report (Continued)

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 8, 2006

FINANCIAL SECTION

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, 2006. 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 2006 by \$1.2 billion (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, 2005, the funded ratio was approximately 83.8%.
- Revenues for the year were \$193.2 million, which is comprised of contributions of \$52.6 million and investment gains of \$140.6 million.
- Expenses increased over the prior year from \$107.3 million to \$112.3 million or 4.7%. 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 Statements of Pension Plan and Postemployment Healthcare Plan Net Assets* (page 24) and *The Statements of Changes in Pension Plan and Postemployment Healthcare Plan Net Assets* (page 25). 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 (page 40) and Schedule of Employer Contributions (page 41) to determine whether the System is becoming financially stronger or weaker and to understand changes over time in the funded status of the System.

FINANCIAL SECTION

Management's Discussion and Analysis (Continued)

FINANCIAL ANALYSIS

System total assets as of September 30, 2006, were \$1.4 billion and were mostly comprised of cash, investments and contributions due from employers. Total assets increased \$204.8 million or 17.2 % from fiscal year 2005 primarily due to favorable operating results and increases to invested assets (primarily collateral on loaned securities), and increased \$78.6 million or 7.1% between fiscal years 2004 and 2005 primarily due to increased investment earnings.

Total liabilities as of September 30, 2006, were \$187.8 million and were mostly comprised of warrants outstanding, accounts payable, and obligations under securities lending. Total liabilities increased \$123.9 million or 193.8% between fiscal years 2005 and 2006 primarily due to an increase in obligations under securities lending, and decreased \$1.9 million or 3.0% between fiscal years 2005 and 2004 primarily due to a decrease in obligations under securities lending.

System assets exceeded its liabilities at the close of fiscal year 2006 by \$1.2 billion. Total net assets held in trust for pension and health benefits increased \$80.9 million or 7.2% between fiscal years 2005 and 2006. 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 2005 increased by \$80.6 million or 7.7% from the prior year due to favorable market conditions and an increase in investment earnings.

Net Assets (in thousands)

	2006	Increase (Decrease)		2005	Increase (Decrease)		2004
Assets							
Cash	\$ 4,064	4.5 %		\$ 3,890	(53.6) %		\$ 8,386
Receivables	3,090	10.8		2,790	80.5		1,546
Investments	1,384,848	17.3		1,180,557	7.5		1,098,673
Total Assets	1,392,002	17.2		1,187,237	7.1		1,108,605
Liabilities							
Warrants outstanding	206	47.1		140	(37.5)		224
Accounts payable and other accrued liabilities	100	(2.9)		103	51.5		68
Obligations under securities lending	187,448	194.5		63,653	(2.9)		65,551
Total Liabilities	187,754	193.8		63,896	(3.0)		65,843
Total Net Assets	\$ 1,204,248	7.2 %		\$ 1,123,341	7.7 %		\$ 1,042,762

FINANCIAL SECTION

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 2006 totaled \$193.2 million.

Total additions increased \$5.3 million from those of fiscal year 2005, due primarily to increased investment earnings. Total additions increased \$17.2 million between fiscal years 2004 and 2005 due to favorable market conditions and increased investment earnings. Total contributions decreased between fiscal years 2005 and 2006 by \$4.1 million or 7.3%. This decrease is primarily due to a decrease in the contribution rate. Total contributions increased between fiscal years 2004 and 2005 by \$5.0 million or 9.6% primarily due to an increase in the contribution rate. Investment income increased from fiscal year 2005 by \$9.5 million. Investment income increased between fiscal years 2004 and 2005 by \$12.3 million. The Investment Section of this report reviews the results of investment activity for 2006.

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 2006 were \$112.3 million, an increase of 4.7% over fiscal year 2005 expenses.

The health, dental and vision care expenses increased during the year by \$2.7 million or 9.9% from \$26.8 million to \$29.5 million during the fiscal year. This compares to a decrease of \$2.4 million or 8.1% from \$29.2 million to \$26.8 million between fiscal years 2004 and 2005. The payment of pension benefits increased by \$2.1 million or 2.7% between fiscal years 2005 and 2006 and by \$2.6 million or 3.3% between fiscal years 2004 and 2005. The increase in pension benefit expenses resulted from a decrease in retirees (15) and an increase in benefit payments to retirees, and in fiscal year 2005 the increase in pension benefit expenses resulted from an increase in retirees (29) and an increase in benefit payments to retirees. Administrative expenses increased by \$49,022 or 16.6% between fiscal years 2005 and 2006, primarily due to an increase in professional services during the current year for special actuarial studies. Administrative expenses decreased by \$22,707 or 7.3% between fiscal years 2004 and 2005, primarily due to a decrease in professional services during the year for special actuarial studies.

FINANCIAL SECTION

Management's Discussion and Analysis (Continued)

Changes in Plan Net Assets (in thousands)

	<u>2006</u>	<u>Increase (Decrease)</u>		<u>2005</u>	<u>Increase (Decrease)</u>		<u>2004</u>
Member contributions	\$ 1,507	(10.2) %	\$	1,679	4.7 %	\$	1,603
Employer contributions	51,125	(7.2)		55,096	9.7		50,219
Net investment income	140,566	7.2		131,111	10.3		118,817
Miscellaneous income	4	-		-	-		-
Total Additions	<u>193,202</u>	<u>2.8</u>		<u>187,886</u>	<u>10.1</u>		<u>170,639</u>
Pension benefits	82,317	2.7		80,170	3.3		77,592
Health Care benefits	29,493	9.9		26,842	(8.1)		29,195
Refunds of member contributions	143	143.0		-	(100.0)		1
Administrative expenses	343	16.6		294	(7.3)		317
Total Deductions	<u>112,296</u>	<u>4.7</u>		<u>107,306</u>	<u>0.2</u>		<u>107,105</u>
Net Increase	80,906	0.4		80,580	26.8		63,534
Net Assets - Beginning of Year	<u>1,123,342</u>	<u>7.7</u>		<u>1,042,762</u>	<u>6.5</u>		<u>979,228</u>
Net Assets - End of Year	<u>\$ 1,204,248</u>	<u>7.2 %</u>	\$	<u>1,123,342</u>	<u>7.7 %</u>	\$	<u>1,042,762</u>

FINANCIAL SECTION

Management's Discussion and Analysis (Continued)

RETIREMENT SYSTEM AS A WHOLE

The System's combined net assets experienced an increase for the fourth 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.

FINANCIAL SECTION

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FINANCIAL SECTION

Statements of Pension Plan and Postemployment Healthcare Plan Net Assets

As of Fiscal Years Ending September 30, 2006 and 2005

	September 30, 2006			September 30, 2005		
	Pension Plan	Health Plan	Total	Pension Plan	Health Plan	Total
Assets:						
Equity in common cash	\$ 4,063,767	\$ -	\$ 4,063,767	\$ 3,879,211	\$ 11,126	\$ 3,890,337
Receivables:						
Amounts due						
from employer	3,056,390	-	3,056,390	2,773,583	7,955	2,781,538
Interest and dividends	33,698	-	33,698	8,626	25	8,651
Total receivables	3,090,088	-	3,090,088	2,782,209	7,980	2,790,189
Investments:						
Short term investment pools	21,843,600	-	21,843,600	26,776,092	76,800	26,852,892
Fixed income pools	192,055,307	-	192,055,307	186,981,507	536,305	187,517,812
Domestic equity pools	582,758,980	-	582,758,980	539,162,382	1,565,483	540,727,865
Real estate pool	100,633,124	-	100,633,124	91,012,525	261,044	91,273,569
Alternative investment pools	152,186,251	-	152,186,251	131,235,305	376,412	131,611,717
International equities pools	147,922,103	-	147,922,103	138,541,411	378,324	138,919,735
Cash collateral on loaned securities	187,448,116	-	187,448,116	63,470,946	182,049	63,652,995
Total investments	1,384,847,481	-	1,384,847,481	1,177,180,168	3,376,417	1,180,556,585
Total assets	1,392,001,336	-	1,392,001,336	1,183,841,588	3,395,523	1,187,237,111
Liabilities:						
Warrants outstanding	205,957	-	205,957	139,843	401	140,244
Accounts payable and other accrued liabilities	99,596	-	99,596	102,282	291	102,573
Obligations under securities lending	187,448,116	-	187,448,116	63,470,946	182,049	63,652,995
Total liabilities	187,753,669	-	187,753,669	63,713,071	182,741	63,895,812
Net Assets Held in Trust						
for Pension and Health Benefits*	\$ 1,204,247,667	\$ -	\$ 1,204,247,667	\$ 1,120,128,517	\$ 3,212,782	\$ 1,123,341,299

*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.

FINANCIAL SECTION

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

For Fiscal Years Ended September 30, 2006 and 2005

	September 30, 2006			September 30, 2005		
	Pension Plan	Health Plan	Total	Pension Plan	Health Plan	Total
Additions:						
Contributions:						
Member contributions	\$ 252,805	\$ 1,254,352	\$ 1,507,157	\$ 112,303	\$ 1,566,646	\$ 1,678,949
Employer contributions	26,103,923	25,021,287	51,125,210	26,607,572	28,488,384	55,095,956
Total contributions	26,356,728	26,275,639	52,632,367	26,719,875	30,055,030	56,774,905
Investment income (loss):						
Investment income (loss)	141,965,437		141,965,437	132,494,702		132,494,702
Investment expenses:						
Real estate operating expenses	(10,033)		(10,033)	(16,180)		(16,180)
Other investment expenses	(1,554,930)		(1,554,930)	(1,455,972)		(1,455,972)
Securities lending activities:						
Securities lending income	4,389,349		4,389,349	1,631,148		1,631,148
Securities lending expenses	(4,224,292)		(4,224,292)	(1,542,702)		(1,542,702)
Net investment income (loss)	140,565,531	-	140,565,531	131,110,996	-	131,110,996
Miscellaneous income	6	4,319	4,325	127		127
Total additions	166,922,265	26,279,958	193,202,223	157,830,998	30,055,030	187,886,028
Deductions:						
Benefits paid to plan members and beneficiaries:						
Retirement benefits	82,316,931		82,316,931	80,169,608		80,169,608
Health benefits		27,090,226	27,090,226	24,894,119		24,894,119
Dental/vision benefits		2,402,514	2,402,514	1,948,129		1,948,129
Refunds of member contributions	142,979		142,979	358		358
Administrative expenses	343,205		343,205	294,183		294,183
Total deductions	82,803,115	29,492,740	112,295,855	80,464,149	26,842,248	107,306,397
Net Increase (Decrease)	84,119,150	(3,212,782)	80,906,368	77,366,849	3,212,782	80,579,631
Net Assets Held in Trust for Pension and Health Benefits:						
Beginning of Year	1,120,128,517	3,212,782	1,123,341,299	1,042,761,668	-	1,042,761,668
End of Year*	\$ 1,204,247,667	\$ -	\$ 1,204,247,667	\$ 1,120,128,517	\$ 3,212,782	\$ 1,123,341,299

* 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.

FINANCIAL SECTION

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, 2006, and 2005, the System's membership consisted of the following:

Retirees and beneficiaries currently receiving benefits:	2006	2005
Regular benefits	2,148	2,186
Survivor benefits	410	387
Disability benefits	153	153
Total	<u>2,711</u>	<u>2,726</u>
Current employees:		
Vested	1,094	1,048
Non-vested	584	660
Total	<u>1,678</u>	<u>1,708</u>
DROP program participants	129	129
Inactive employees entitled to benefits and not yet receiving them	12	11
Total members	<u><u>4,530</u></u>	<u><u>4,574</u></u>

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

Health/Dental/Vision Plan	2006	2005
Eligible participants	2,711	2,726
Participants receiving benefits:		
Health	2,425	2,366
Dental	2,407	2,396
Vision	2,412	2,400

FINANCIAL SECTION

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.

FINANCIAL SECTION

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 21.0% and 23.9% for 2006 and 2005, 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.

FINANCIAL SECTION

Notes to Basic Financial Statements (Continued)

Reserve for Employee Contributions — Members do not contribute to this reserve except to purchase eligible service credit. This reserve 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, 2006, and 2005, the balance in this account was \$553.6 thousand and \$294.7 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, 2006, and 2005, the balance in this account was \$69.4 million and \$68.9 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. Also included are reserves for casualty experience (injury or death of a member, or vested former member). The initial actuarial casualty valuation determined the full funding reserve requirements to be allocated from assets of the reserve. All retiree casualty payments are made from this account. At September 30, 2006, and 2005, the balance in this account was \$903.1 million and \$883.7 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, 2006, and 2005, the balance of this reserve was \$231.3 million and \$167.2 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, 2006, and 2005, the balance in this account was \$0.0 million and \$3.2 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 2006 the expenses exceeded revenues by \$1.1 million prior to a return of \$1.1 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.

FINANCIAL SECTION

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 administering the System are financed by undistributed investment income of 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.

	<u>2006</u>	<u>2005</u>
Building Rentals	\$ 5,631	\$ 4,505
Technological Support	76,204	55,160
Attorney General	28,386	23,526
Investment Services	225,515	199,594
Personnel Services	82,643	76,497

Commitment and Contingency – The State has signed a contract with a vendor for technological support through 2006. As of September 30, 2006, the System's portion of this commitment is approximately \$42,000.

Cash — On September 30, 2006, and 2005, the System had \$4.1 million and \$3.9 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 \$100,086 and \$51,475 for the years ended September 30, 2006, and 2005, respectively.

Reclassification of Prior Year Amounts

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

FINANCIAL SECTION

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 30-year period for the 2006 fiscal year and a 31-year period for the 2005 fiscal year.

Actual employer contributions for retirement benefits were \$26.1 million and \$26.6 million for fiscal years 2006 and 2005, respectively, representing 22.6% of annual covered payroll for the year ended September 30, 2005. The fiscal year 2006 annual covered payroll is not yet available. Required employer contributions for pensions included:

1. \$23.9 million and \$24.2 million for fiscal years 2006 and 2005, respectively, for the normal cost of pensions representing 20.6% of annual covered payroll for fiscal year 2005.
2. \$12.2 million and \$7.9 million for fiscal years 2006 and 2005, respectively, for amortization of overfunded actuarial accrued liability representing 6.7% of annual covered payroll for fiscal year 2005.

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 leverage of investments. Less than 12.0% of the total pension trust fund's portfolio has been invested from time to time in futures contracts, swap agreements, and option contracts. 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 9.1% of market value of total pooled assets on September 30, 2006 and 10.8% of market value of total pooled assets on September 30, 2005. Option contracts represent the second largest category of reported derivatives used, and they represented 0.6% of market value of total pooled assets on September 30, 2006, and 0.0% of market value of total pooled assets on September 30, 2005. Futures contracts

FINANCIAL SECTION

Notes to Basic Financial Statements (Continued)

represent the third largest category of derivatives used, and they represented 0.0% of market value of total pooled assets on September 30, 2006, and 0.3% of market value of total pooled assets on September 30, 2005.

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 capitalize on shorter-term windows of investment opportunities, the State Treasurer has purchased option contracts. Options allow more flexibility in achieving investment goals without disturbing the return/risk profiles of the longer-term strategies of the underlying 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, 2006, and 2005, were \$79.9 million and \$92.2 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 Retirement 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 2006 to July 2009.

U.S. domestic LIBOR based floating rate notes and other investments earning short-term interest are held to correspond with the notional amount of the swap agreements. The State Treasurer maintains custody and control of these dedicated notes and short-term investments.

The value of these synthetic equity structures is a combination of the value of the swap agreements and the value of the notes and short-term investments. The book value represents the cost of the notes and short-term investments. The current value represents the current value of the notes and short-term investments 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. For fiscal years ending September 30, 2006, and 2005, international equity investment programs involving swaps, received realized gains and earned interest income of \$18.0 million and \$7.9 million, respectively.

The unrealized gain of \$30.0 million at September 30, 2006, and 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 generally realizes gains and losses on a rolling three year basis.

The respective September 30, 2006, and 2005 swap values are as follows:

	<u>Notional Value</u>	<u>Current Value</u>
9/30/06 (dollars in millions)	\$ 79.9	\$ 109.8
9/30/05 (dollars in millions)	92.2	121.3

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

FINANCIAL SECTION

Notes to Basic Financial Statements (Continued)

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 did not have the ability to pledge or sell collateral securities delivered absent a borrower default. Borrowers were 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 was 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 was not located in the United States, 105% of the market value of the loaned securities.

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 any 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 collateral account dedicated to the System. As of September 30, 2006, such account had an average weighted maturity to next reset of 22 days and an average weighted maturity of 678 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, 2006, the System had no credit risk exposure to borrowers. The cash held for securities on loan for the System as of September 30, 2006 was \$187,448,116. The carrying amount, which is the fair market value, of securities on loan for the System as of September 30, 2006, was \$182,643,181.

Gross income from security lending for the fiscal year was \$4,389,349. Expenses associated with this income were the borrower's rebate of \$4,184,778 and fees paid to the agent of \$39,514.

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.

Credit Risk - 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 - These investments must be investment grade or better at the time of purchase unless specific requirements are met, as defined by PA 314 of 1965 as amended and the State Treasurer's investment policy. Law defines investment grade as investments in the top four major grades, rated by two national rating services, S&P (AAA, AA, A, BBB) and Moody's (Aaa, Aa, A, Baa). At September 30, 2006, the System was in compliance with the policy in all material aspects.

FINANCIAL SECTION

Notes to Basic Financial Statements (Continued)

Rated Debt Investments
(In thousands of dollars)
As of September 30, 2006 and 2005

Investment Type	September 30, 2006				September 30, 2005			
	Fair Value	S&P	Fair Value	Moody's	Fair Value	S&P	Fair Value	Moody's
Short Term	\$ 55,498	A-1	\$ 65,420	P-1	\$ 38,671	A-1	\$ 42,365	P-1
	1,909	A-2	2,672	P-2	1,754	A-2	1,754	P-2
	14,496	NR	3,811	NR	8,527	NR	4,833	NR
U.S. Agencies- Sponsored								
	64,671	AAA	64,671	Aaa	55,767	AAA	55,767	Aaa
	1,739	NR	1,739	NR				
Corporate Bonds & Notes								
	12,438	AAA	12,756	Aaa	15,755	AAA	15,755	Aaa
	17,374	AA	23,435	Aa	21,460	AA	25,516	Aa
	31,539	A	20,968	A	37,927	A	33,268	A
	7,906	BBB	10,141	Baa	8,867	BBB	11,172	Baa
	130	BB	471	Ba	7,141	BB	3,157	Ba
	74	B	-	B				
	1,767	NR	3,457	NR	1,445	NR	3,727	NR
International *								
	8,671	AAA	7,574	Aaa	19,279	AAA	19,279	Aaa
	19,319	AA	30,842	Aa	22,084	AA	37,778	Aa
	25,461	A	12,184	A	46,182	A	29,816	A
	-	BB	-	Ba	2,242	BB	2,242	Ba
	-	NR	2,851	NR			672	NR
Equity*								
	1,116	AA	7,357	Aa	1,115	AA	2,229	Aa
	6,241	A	-		1,114	A	-	
Total	<u>\$ 270,349</u>		<u>\$ 270,349</u>		<u>\$ 289,330</u>		<u>\$ 289,330</u>	

NR - not rated

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

FINANCIAL SECTION

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, 2006. As of September 30, 2006, and 2005 Government securities with a market value of \$527 thousand and \$1,113 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, 2006, and 2005 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, 2006, and September 30, 2005, the fair value of the System's prime commercial paper was \$71,903 thousand and \$48,952 thousand with the weighted average maturity of 41 days and 38 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.

FINANCIAL SECTION

Notes to Basic Financial Statements (Continued)

Debt Securities (in thousands) As of September 30, 2006 and 2005

	2006		2005	
	Fair Value	Effective Duration in Years	Fair Value	Effective Duration in Years
Government				
U. S. Treasury	\$ 12,567	3.1	\$ 8,888	4.3
U. S. Agencies - Backed	27,113	5.7	25,312	5.3
U. S. Agencies - Sponsored	66,409	3.7	55,767	2.5
Corporate	71,228	4.4	92,595	4.1
International*				
U. S. Treasury	2,190	0.5	-	
U. S. Agencies - Sponsored	1,092	0.1	1,120	0.1
Corporate	52,359	0.1	88,667	0.2
Equities*				
Corporate	7,357	0.6	2,229	0.2
Total	<u>\$ 240,315</u>		<u>\$ 274,578</u>	

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

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 investments include equities, fixed income, mutual funds, real estate, and limited partnerships. At September 30, 2006, and 2005 the total amount of foreign investment subject to foreign currency risk were \$69,546 thousand and \$50,166 thousand which amounted to 5.8% and 4.5% of total investments of the System, exclusive of cash collateral on loaned securities, respectively.

FINANCIAL SECTION

Notes to Basic Financial Statements (Continued)

Foreign Currency Risk
(in thousands)
As of September 30, 2006

Region	Country	Currency	Alt. Invest. Market Value in U.S. \$	Equity Market Value in U.S. \$	Real Estate Market Value in U.S. \$	International	
						Equities Market Value in U.S. \$	Derivatives Market Value in U.S. \$ *
<u>AMERICA</u>							
	Canada	Dollar		\$ 405			
	Mexico	Peso		1,572			
<u>EUROPE</u>							
	European Union	Euro	\$ 10,103	2,727		\$ 706	\$ 5,153
	Switzerland	Franc		904			1,131
	Sweden	Krona		186			237
	Denmark	Krone				13	176
	Norway	Krone		92		1	192
	U.K.	Sterling	537	1,220		53	2,815
<u>PACIFIC</u>							
	Australia	Dollar		325			700
	Hong Kong	Dollar		64			475
	Japan	Yen	181	1,651		7	2,599
	Singapore	Dollar					109
	South Korea	Won		199			889
<u>VARIOUS</u>							
				13,711	\$ 4,622	15,791	
	Total		\$ 10,821	\$ 23,056	\$ 4,622	\$ 16,571	\$ 14,476

* 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 2006 through November 2008 with an average maturity of 1.1 years.

FINANCIAL SECTION

Notes to Basic Financial Statements (Continued)

Foreign Currency Risk (in thousands) As of September 30, 2005

<u>Region</u>	<u>Country</u>	<u>Currency</u>	<u>Alt. Invest. Market Value in U.S. \$</u>	<u>Equity Market Value in U.S. \$</u>	<u>International</u>	
					<u>Equities Market Value in U.S. \$</u>	<u>Derivatives Market Value in U.S. \$ *</u>
<u>AMERICA</u>						
	Mexico	Peso		\$ 5,611		
<u>EUROPE</u>						
	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
<u>PACIFIC</u>						
	Australia	Dollar			10	943
	Hong Kong	Dollar			137	253
	Japan	Yen	193		100	2,875
	New Zealand	Dollar				42
	Singapore	Dollar				141
	South Korea	Won				554
<u>VARIOUS</u>					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.

FINANCIAL SECTION

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. This statement was adopted in fiscal year 2006 and is reflected in this report.

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 Statement No. 43 in financial statements for periods beginning after December 15, 2005.

The GASB has issued Statement No. 47, *Accounting for Termination Benefits*, which provides guidance on how employers should account for benefits associated with either voluntary or involuntary termination. The requirements of the new statement become effective for fiscal periods beginning after June 15, 2005 (except for those provisions involving other postemployment benefits, which only take effect upon the implementation of GASB Statement 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions*). It has been determined, upon review of GASB Statement No. 47, that the Statement has no effect on reporting for the System.

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.

FINANCIAL SECTION

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 overfunded 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)
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
2005	1,090.3	1,300.3	210.0	83.8	117.6	178.5

(1) Change in asset valuation method.

(2) Assumption change.

(3) Change in inflation.

(4) Revised actuarial assumptions and benefit provisions.

FINANCIAL SECTION

Required Supplementary Information (Continued)

Schedule of Employer Contributions

<u>Fiscal Year Ended Sept. 30</u>	<u>Required Contribution (ARC)</u>	<u>Actual Contribution</u>	<u>Percentage Contributed</u>
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
2006	36,063,260	26,103,923	72.4

FINANCIAL SECTION

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	9/30/2005
Actuarial Cost Method	Entry Age, Normal
Amortization Method	Level Percent of Payroll, Closed
Remaining Amortization Period	31 years *
Asset Valuation Method	5-Year Smoothed Market
Actuarial Assumptions:	
Wage 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

* When the actuarial accrued liability for a defined benefit pension plan is underfunded or overfunded, the difference should be amortized over a period not to exceed forty years for the fiscal periods beginning prior to June 15, 2006. After that date, the amortization period may not exceed thirty years.

FINANCIAL SECTION

Supporting Schedules

Comparative Summary Schedule of Pension Plan Administrative Expenses As of September 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Personnel Services:		
Staff Salaries	\$ 56,565	\$ 52,693
Retirement and Social Security	15,490	14,445
Other Fringe Benefits	10,588	9,359
Total	<u>82,643</u>	<u>76,497</u>
Professional Services:		
Accounting	11,898	12,506
Actuarial	63,492	63,000
Attorney General	28,386	23,526
Audit	30,795	13,693
Consulting	9,342	4,971
Medical	4,704	3,183
Total	<u>148,617</u>	<u>120,879</u>
Building Equipment		
Building Rentals	5,631	4,505
Equipment Purchase, Maintenance, and Rentals	499	653
Total	<u>6,130</u>	<u>5,158</u>
Miscellaneous:		
Travel and Board Meetings	313	284
Office Supplies	655	714
Postage, Telephone, and Other	24,899	31,927
Printing	3,745	3,564
Technological Support	76,203	55,160
Total	<u>105,815</u>	<u>91,649</u>
Total Administrative Expenses	<u>\$ 343,205</u>	<u>\$ 294,183</u>

FINANCIAL SECTION

Supporting Schedules (Continued)

Schedule of Investment Expenses

	<u>2006</u>	<u>2005</u>
Real Estate Operating Expenses	\$ 10,033	\$ 16,180
Securities Lending Expenses	4,224,292	1,542,702
Other Investment Expenses*		
ORS-Investment Expenses	225,515	199,594
Custody Fees	25,938	32,113
Management Fees-Real Estate	63,870	17,471
Management Fees-Alternative	1,216,000	1,183,750
Research Fees	23,607	23,045
Total Investment Expenses	\$ 5,789,255	\$ 3,014,854

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

Schedule of Payments to Consultants

	<u>2006</u>	<u>2005</u>
Independent Auditors	\$ 30,795	\$ 13,693
Consulting	9,342	4,971
Medical	4,704	3,183
Attorney General	28,386	23,526
Accounting	11,898	12,506
Actuary	63,492	63,000
Total Payment to Consultants	\$ 148,617	\$ 120,879

FINANCIAL SECTION

Supporting Schedules (Continued)

Detail of Changes in Plan Net Assets (Pension and Postemployment Healthcare Benefits) For the Year Ended September 30, 2006

	Employee Contributions	Employer Contributions	Retired Benefit Payments*	Undistributed Investment Income	Health Related Benefits	Total
Additions:						
Contributions:						
Member contributions	\$ 252,805				\$ 1,254,352	\$ 1,507,157
Employer contributions		\$ 26,103,923			25,021,287	51,125,210
Total Contributions	<u>252,805</u>	<u>26,103,923</u>	<u>-</u>	<u>-</u>	<u>26,275,639</u>	<u>52,632,367</u>
Investment income (loss):						
Investment income (loss)				\$ 141,965,437		141,965,437
Investment expenses:						
Real estate operating expenses				(10,033)		(10,033)
Other investment expenses				(1,554,930)		(1,554,930)
Securities lending activities:						
Securities lending income				4,389,349		4,389,349
Securities lending expenses				(4,224,292)		(4,224,292)
Net investment income (loss)	<u>-</u>	<u>-</u>	<u>-</u>	<u>140,565,531</u>	<u>-</u>	<u>140,565,531</u>
Miscellaneous income				6	4,319	4,325
Total additions	<u>252,805</u>	<u>26,103,923</u>	<u>-</u>	<u>140,565,537</u>	<u>26,279,958</u>	<u>193,202,223</u>
Deductions:						
Benefits paid to plan members and beneficiaries:						
Retirement benefits			\$ 82,316,931			82,316,931
Health benefits					27,090,226	27,090,226
Dental/vision benefits					2,402,514	2,402,514
Refunds of member contributions	802	142,177				142,979
Administrative expenses				343,205		343,205
Total deductions	<u>802</u>	<u>142,177</u>	<u>82,316,931</u>	<u>343,205</u>	<u>29,492,740</u>	<u>112,295,855</u>
Net Increase (Decrease)	<u>252,003</u>	<u>25,961,746</u>	<u>(82,316,931)</u>	<u>140,222,332</u>	<u>(3,212,782)</u>	<u>80,906,368</u>
Other Changes in Net Assets:						
Interest allocation	11,234	5,509,495	70,697,225	(76,217,954)		-
Transfers upon retirement	(4,330)	(30,973,208)	30,977,538			-
Total other changes in net assets	<u>6,904</u>	<u>(25,463,713)</u>	<u>101,674,763</u>	<u>(76,217,954)</u>	<u>-</u>	<u>-</u>
Net Increase (Decrease) After Other Changes	<u>258,907</u>	<u>498,033</u>	<u>19,357,832</u>	<u>64,004,378</u>	<u>(3,212,782)</u>	<u>80,906,368</u>
Net Assets Held in Trust for Pension and Health Benefits:						
Beginning of Year	<u>294,717</u>	<u>68,868,684</u>	<u>883,715,317</u>	<u>167,249,799</u>	<u>3,212,782</u>	<u>1,123,341,299</u>
End of Year	<u>\$ 553,624</u>	<u>\$ 69,366,717</u>	<u>\$ 903,073,149</u>	<u>\$ 231,254,177</u>	<u>\$ -</u>	<u>\$ 1,204,247,667</u>

*Casualty Reserve is included.

FINANCIAL SECTION

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	<u>112,303</u>	<u>26,607,572</u>	-	-	<u>30,055,030</u>	<u>56,774,905</u>
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)	<u>-</u>	<u>-</u>	<u>-</u>	<u>131,110,996</u>	<u>-</u>	<u>131,110,996</u>
Miscellaneous income						
				127		127
Total additions	<u>112,303</u>	<u>26,607,572</u>	<u>-</u>	<u>131,111,123</u>	<u>30,055,030</u>	<u>187,886,028</u>
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	<u>358</u>	<u>-</u>	<u>80,169,608</u>	<u>294,183</u>	<u>26,842,248</u>	<u>107,306,397</u>
Net Increase (Decrease)	<u>111,945</u>	<u>26,607,572</u>	<u>(80,169,608)</u>	<u>130,816,940</u>	<u>3,212,782</u>	<u>80,579,631</u>
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	<u>(33,932)</u>	<u>(45,395,515)</u>	<u>119,964,808</u>	<u>(74,535,361)</u>	<u>-</u>	<u>-</u>
Net Increase (Decrease) After Other Changes	<u>78,013</u>	<u>(18,787,943)</u>	<u>39,795,200</u>	<u>56,281,579</u>	<u>3,212,782</u>	<u>80,579,631</u>
Net Assets Held in Trust for Pension and Health Benefits:						
Beginning of Year	<u>216,704</u>	<u>87,656,627</u>	<u>843,920,117</u>	<u>110,968,220</u>	<u>-</u>	<u>1,042,761,667</u>
End of Year	<u>\$ 294,717</u>	<u>\$ 68,868,684</u>	<u>\$ 883,715,317</u>	<u>\$ 167,249,799</u>	<u>\$ 3,212,782</u>	<u>\$ 1,123,341,299</u>

*Casualty Reserve is included.

INVESTMENT SECTION

Prepared by Michigan Department of Treasury, Bureau of Investments

Jacqueline M. Johnson, CFA, Director

Report on Investment Activity

Asset Allocation

Investment Results

List of Largest Stock Holdings

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INVESTMENT SECTION

Report on Investment Activity

INTRODUCTION

The State Treasurer reports 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 2006, 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), Robert W. Swanson (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.

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.

INVESTMENT SECTION

Report on Investment Activity (Continued)

Asset Allocation (Excludes Collateral on Loaned Securities)

<u>Investment Category</u>	<u>As of 9/30/06 Actual %</u>	<u>Five-Year Target %</u>
Domestic Equity - Active	29.1%	26.5%
Large Cap Value Pool	13.0%	
Large Cap Growth Pool	13.0%	
Mid Cap Pool	2.1%	
Small Cap Pool	1.0%	
Domestic Equity - Passive	19.4%	19.5%
S&P 500 Index Pool	16.6%	
S&P MidCap Index Pool	2.0%	
Tactical Asset Allocation Pool	0.6%	
S&P Small Cap Index Pool	0.2%	
International Equity	12.3%	10.0%
International Equity Pool - Passive	10.6%	
International Equity Pool - Active	1.7%	
Alternative Investments Pool	12.7%	12.0%
Real Estate Pool	8.4%	10.0%
Fixed Income	16.0%	16.0%
Government Bond Pool	8.3%	
Corporate Bond Pools	5.8%	
Fixed Income Bond Pools	1.9%	
Short Term Investment Pool	2.1%	2.0%
Commodities	0.0%	4.0%
Total	<u>100.0%</u>	<u>100.0%</u>

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, 2006, 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, 2006, were 12.7%; for the five-year period were 8.1%; and for the ten-year period were 8.7%.

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

INVESTMENT SECTION

Report on Investment Activity (Continued)

Investment results were once again driven by double-digit returns from every major asset class except fixed income and short-term investments. Equity performance was strong much of the year in spite of soaring commodity and energy prices. Reversing a multi-year trend, the stocks of larger companies (S&P 500) outperformed those of mid-cap (S&P 400) and small cap (S&P 600), while non-U.S. markets performed better than U.S. indices. Residential housing experienced a meaningful slowdown during the year due to higher interest rates and stricter lending regulations. Alternative Investments continued to reap the benefits of a number of investments made in prior years as well as favorable markets for monetization of gains. Robust commercial real estate markets allowed the Real Estate pool to experience gains from both sales and appraisals of property. Bond markets struggled with the fear of higher inflation and a Federal Reserve intent on controlling inflation with higher short-term rates. Returns for the short-term pool climbed throughout the year to more than 4.5%.

For the fiscal year, the Dow Jones Industrial Average provided a total return of 13.3%, while the broader based S&P 500 returned 10.8%. The Lehman Brothers U.S. Government/Credit Bond Index appreciated 3.3%.

The U.S. economy grew at a rate of 3.1% in fiscal year 2006 as measured by real gross domestic product. The December quarter was negatively affected by the impact of last year's hurricane season, but growth came roaring back in the March quarter. The second half of the year settled back to more normal, sustainable growth levels. Corporate earnings remained strong, led by robust profits from energy companies. Strong demand sent commodity and energy prices climbing during most of the year, with oil coming close to \$80 per barrel in August before selling off sharply to nearly \$60 by the end of the year. Inflation, as measured by the consumer price index, increased 3.7%.

Federal Reserve Chairman Alan Greenspan retired after nineteen years at the helm and Ben Bernanke was appointed his successor on February 1, 2006. The Federal Reserve continued to raise short-term rates by 25 basis points at each of its first six meetings in the fiscal year, but left rates unchanged at 5.25% in both August and September after seventeen consecutive rate hikes.

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

Large Cap Value Pool

The 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 Citigroup Value Index.

The pool invests primarily in equities and equity-related securities 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 with weightings that approximate the weightings of the S&P Citigroup Value Index.

INVESTMENT SECTION

Report on Investment Activity (Continued)

The following summarizes the weightings of the pool as of September 30, 2006:

Financials	38.1 %
Industrials	13.7
Technology	10.0
Consumer Discretionary	8.6
Energy	8.5
Utilities	8.3
Materials	4.3
Other	3.5
Healthcare	2.7
Consumer Staples	2.3
Total	<u>100.0 %</u>

The System's Large Cap Value pool achieved a total rate of return of 15.8% for fiscal 2006. This compared with 14.0% for the S&P 500 Citigroup Value Index.

At the close of fiscal year 2006, the Large Cap Value pool represented 13.0% of total investments. This compares to 15.2% for fiscal year 2005. The following summarizes the System's 2.1% ownership share of the Large Cap Value pool at September 30, 2006:

Large Cap Value Pool (in thousands)

Short Term Pooled Investments	\$ 5,243
Equities	150,308
Settlement Principal Payable	(145)
Settlement Proceeds Receivable	88
Accrued dividends	182
Total	<u>\$ 155,676</u>

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 Citigroup Growth Index.

The pool invests primarily in equities and equity-related securities 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.

INVESTMENT SECTION

Report on Investment Activity (Continued)

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 with weightings that approximate the weightings of the S&P Citigroup Growth Index. The following summarizes the weightings of various sectors in the pool as of September 30, 2006:

Technology	22.4 %
Healthcare	20.3
Consumer Discretionary	12.5
Consumer Staples	12.1
Financials	11.1
Energy	10.7
Industrials	8.7
Other	1.0
Utilities	0.7
Materials	0.5
Total	<u>100.0 %</u>

The Large Cap Growth pool's total rate of return was 7.2% for the fiscal year versus 7.4% for the S&P 500 Citigroup Growth Index.

At the close of fiscal year 2006, the Large Cap Growth pool represented 13.0% of total investments. This compares to 15.6% for fiscal year 2005. The following summarizes the System's 2.2% ownership share of the Large Cap Growth pool at September 30, 2006:

Large Cap Growth Pool (in thousands)

Short Term Pooled Investments	\$ 1,509
Equities	154,572
Settlement Principal Payable	(180)
Accrued dividends	115
Total	<u>\$ 156,016</u>

Mid Cap Pool

Five Mid Cap managers were selected in December 2005, and added to the four managers selected in May 2005. The new managers began managing assets for the System in December 2005 and they were funded out of the Large Cap Value and Growth pools. The investment objective of the Mid Cap manager pool is to generate a rate of return from investment in common stocks and equivalents that exceeds the S&P 400 Mid Cap Index.

The Mid Cap pool return for the fiscal year was 7.1% versus the benchmark's 6.6%.

INVESTMENT SECTION

Report on Investment Activity (Continued)

At the close of fiscal year 2006, the Mid Cap pool represented 2.1% of total investments. This compares to 0.9% for fiscal year 2005. The following summarizes the System's ownership share and composition of the Mid Cap pool at September 30, 2006:

Mid Cap Value and Core Pools (in thousands)

	Artisan Midcap Value	Cramer Rosenthal McGlynn Midcap Value	Los Angeles Capital Midcap Core	Wellington Management Midcap Core
Total Investment	\$ 4,225	\$ 3,935	\$ 2,551	\$ 3,804
Ownership Percentage	2.2%	2.2%	2.2%	2.2%

Mid Cap Growth Pools (in thousands)

	Alliance Midcap Growth	Putnam Midcap Growth	Rainer Midcap Growth	UBS Midcap Growth	Wellington Midcap Growth
Total Investment	\$ 2,651	\$ 1,090	\$ 2,314	\$ 2,281	\$ 2,370
Ownership Percentage	2.2%	2.2%	2.2%	2.2%	2.2%

Small Cap Pool

The primary investment objective is to generate a rate of return from investment in common stocks and equivalents that exceeds the S&P 600 Small Cap Index.

The System's Small Cap pool is invested with two Growth managers and three Value managers.

The Small Cap pool return for the fiscal year was 8.3% versus the benchmark's 7.2%.

At the close of fiscal year 2006, the Small Cap pool represented 1.0% of total investments. This compares to 0.8% for fiscal year 2005. The following summarizes the System's ownership share and composition of the Small Cap Pool at September 30, 2006:

Small Cap Pool (in thousands)

	Delaware Growth	Putnam Growth	Putnam Value	Northpointe Value	Fisher Value
Total Investment	\$ 3,573	\$ 2,262	\$ 1,951	\$ 1,867	\$ 2,313
Ownership Percentage	2.3%	2.3%	2.3%	2.4%	2.2%

INVESTMENT SECTION

Report on Investment Activity (Continued)

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, 2006:

Financials	22.3 %
Information Technology	15.3
Healthcare	12.7
Industrials	10.9
Consumer Discretionary	10.1
Consumer Staples	9.6
Energy	9.3
Telecomm. Services	3.5
Utilities	3.4
Materials	2.9
Total	<u>100.0 %</u>

The S&P 500 Index pool return for the fiscal year was 10.8% versus the benchmark's 10.8%.

At the close of fiscal year 2006, the S&P 500 Index pool represented 16.6% of total investments. This compares to 13.4% for fiscal year 2005. The following summarizes the System's 2.2% ownership share of the S&P 500 Index pool at September 30, 2006:

S&P 500 Index Pool (in thousands)

Short Term Pooled Investments	\$ 866
Equities	198,692
Settlement Proceeds Receivable	14
Settlement Principal Payable	(47)
Accrued dividends	216
Total	<u>\$ 199,741</u>

S&P MidCap Index 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 6.9% versus its benchmark's 6.6%.

INVESTMENT SECTION

Report on Investment Activity (Continued)

At the close of fiscal year 2006, the S&P MidCap Index pool represented 2.0% of total investments. This compares to 2.1% for fiscal year 2005. The following summarizes the System's 2.4% ownership share of the S&P MidCap Index pool at September 30, 2006:

S&P MidCap Index Pool (in thousands)

Short Term Pooled Investments	\$	210
Equities		25,059
Futures Contracts		(1)
Settlement Proceeds Receivable		47
Settlement Principal Payable		(75)
Accrued dividends		20
Total	\$	<u>25,260</u>

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 7.5% versus the benchmark's 7.2%.

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.

At the close of fiscal year 2006, the S&P Small Cap Index pool represented 0.2% of total investments. This compares to 0.3% for fiscal year 2005. The following summarizes the System's 2.2% ownership share of the S&P Small Cap Index pool at September 30, 2006:

S&P Small Cap Index Pool (in thousands)

Short Term Pooled Investments	\$	18
Equities		552
Fixed Income Securities		1,116
Market Value of Equity Contracts		225
Accrued dividends and interest		4
Total	\$	<u>1,915</u>

International Equity Pool - Passive

The objective of the International Equity 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 for the fiscal year was 17.5% compared to the Citigroup BMI-EPAC return of 18.5%.

INVESTMENT SECTION

Report on Investment Activity (Continued)

Core passive exposure to international equity returns is achieved primarily by investing in a combination of fixed income LIBOR notes, short-term fixed income investments, and equity swap agreements on foreign stock indices in developed markets. Interest on the dedicated notes and short-term fixed income investments 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 portfolio management flexibility, and a country fund portfolio with targeted capitalization was added in September of 2002 to improve exposure to the smallest companies in the BMI index.

The combination of notes, dedicated short-term investments and equity swap agreements was valued at \$108.5 million on September 30, 2006. That valuation included a net unrealized gain of \$29.7 million on equity index exposures and an unrealized gain of \$55 thousand on LIBOR note investments held. The combined Swap agreements, notes and short-term investments together continue to perform like a stock index fund that realizes all gains and losses on a rolling three year basis. During fiscal year 2006, \$16.0 million of gains on equity exposures were realized, \$1.1 million of interest in excess of obligations on completed swaps was recognized, and \$15 thousand of losses on LIBOR notes were realized.

At the close of fiscal year 2006, the International Equity – Passive pool represented 10.6% of total investments. This compares to 11.8% for fiscal year 2005. The following summarizes the System's 2.2% ownership share of the International Equity Pool - Passive at September 30, 2006:

International Equity Pool - Passive (in thousands)

Short Term Pooled Investments	\$	25,115
Equities		16,571
Fixed Income Securities		55,593
Market Value of Equity Contracts		29,337
Accrued dividends and interest		448
Total	\$	<u>127,064</u>

International Equity Pool - Active

The 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. That benchmark is impacted by foreign currency exchange rate changes.

In fiscal year 2005, the System invested in AllianceBernstein International Style Blend, a mix of Large Cap Growth and Value, and in fiscal year 2006 achieved a total rate of return of 18.8% vs. Citigroup Broad Market Index World ex. U.S. of 19.3%. During fiscal year 2006, investments were made in the following funds: The Wellington Trust Company International Research Equity Fund, which for a nine month period achieved a total rate of return of 15.4% and the State Street Global Asset International Alpha Select Pool which achieved a total rate of return of 17.0%. For the same nine month period the benchmark S&P Citigroup Broad Market Index World ex. U.S. achieved a return of 13.9%.

INVESTMENT SECTION

Report on Investment Activity (Continued)

At the close of fiscal year 2006, the International Equity - Active pool represented 1.7% of total investments. This compares to 0.6% for fiscal year 2005. The following summarizes the System's ownership share and composition of the pool at September 30, 2006:

International Equity Pool - Active			
(in thousands)			
	AllianceBernstein	Wellington	SSGA
	<u>International</u>	<u>International</u>	<u>International</u>
Total Investment	\$ 7,846	\$ 5,864	\$ 7,147
Ownership Percentage	2.2%	2.1%	2.1%

Alternative Investments Pool

The Alternative Investments pool objective is to meet or exceed the S&P 500 plus 300 basis points for all private equity investments 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, 2006:

Buyout Funds	56.5 %
Special Situation Funds	13.1
Venture Capital Funds	11.8
Fund of Funds	11.3
Mezzanine Funds	4.1
Hedge Funds	1.8
Short Term Investments	<u>1.4</u>
Total	<u><u>100.0 %</u></u>

The Alternative Investments pool had a return of 26.3% for the fiscal year ended September 30, 2006, versus the S&P 500 Index plus 300 basis points of 13.9%.

Credit Suisse Asset Management (CSAM) managed the stock distributions of the Alternative Investments. The CSAM pool return for the fiscal year ending September 30, 2006, was (19.8%).

At the close of fiscal year 2006, the Alternative Investments pool represented 12.7% of total investments and Credit Suisse Asset Management represented 0.01% of total investments. This compares to 11.6% for Alternative and 0.1% for CSAM for fiscal year 2005.

INVESTMENT SECTION

Report on Investment Activity (Continued)

The following summarizes the System's ownership share and composition of the Alternative Investments pool and Credit Suisse Asset Management at September 30, 2006:

Alternative Investments Pool (in thousands)

	<u>Alternative</u>	<u>CSAM</u>
Short Term Pooled Investments	\$ 2,067	\$ -
Equities	150,023	14
Settlement Proceeds Receivable	-	83
Total	<u>\$ 152,090</u>	<u>\$ 97</u>
Ownership Percentage	2.2%	1.8%

Real Estate Pool

The Real Estate pool seeks favorable 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 diversifies its holdings by:

- Geographic region - The pool is broadly diversified geographically. Emphasis is placed upon U.S. real estate investments, but may also include foreign real estate investments that are not expected to exceed ten percent of the 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 as summarized in the table below.

Multi-family apartments	24.5 %
Commercial office buildings	22.1
Hotels	15.1
Retail shopping centers	15.1
Industrial warehouse buildings	9.8
Senior Living	4.2
Short Term Investments	3.6
Land	2.9
For Sale Housing	2.7
Total	<u>100.0 %</u>

INVESTMENT SECTION

Report on Investment Activity (Continued)

The Real Estate pool generated a return of 18.9% for fiscal year 2006, while the benchmark return was 16.3%. The benchmark is the National Council of Real Estate Investment Fiduciaries Property Index less 130 basis points. The Real Estate pool benefited from a robust real estate market. During the year the pool had strong appreciation and also realized strong gains on asset sales.

At the close of fiscal year 2006, the Real Estate pool represented 8.4% of total investments. This compares to 8.1% for fiscal year 2005. The following summarizes the System's 2.3% ownership share of the Real Estate pool at September 30, 2006:

Real Estate Pool (in thousands)

Short Term Pooled Investments	\$	3,601
Equities		97,032
Total	\$	<u>100,633</u>

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, 2006, the Government Bond pool returned 4.3% which compared favorably to the Lehman Brothers Government Index of 3.3%.

Rates continued to be volatile during the year. Ten-year treasuries started the year at 4.32%, rose to 5.25%, then declined and ended at 4.63%. The yield curve shifted upward and continued to flatten from five to thirty years. From three months to three years the curve inverted.

The following summarizes the security type breakdown of the pool as of September 30, 2006:

U.S. Agency	61.8 %
GNMA	18.2
U.S. Guaranteed	8.7
U.S. Treasury	4.9
TIPS	4.3
Short Term Investments/Accruals	2.1
Total	<u>100.0 %</u>

INVESTMENT SECTION

Report on Investment Activity (Continued)

At the close of fiscal year 2006, the Government Bond pool represented 8.3% of total investments. This compares to 8.2% for fiscal year 2005. The following summarizes the System's 2.2% ownership share of the Government Bond pool at September 30, 2006:

Government Bond Pool (in thousands)

Short Term Pooled Investments	\$	1,235
Fixed Income Securities		97,767
Accrued dividends		878
Total	\$	<u>99,880</u>

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, 2006, the Corporate Bond pool returned 3.6% compared to the Lehman Brothers Credit Index of 3.4%. The pool's performance improved as the year progressed due to the decline in rates later in the year.

The following summarizes the security type breakdown of the pool as of September 30, 2006:

Financials	29.4 %
Short Term Investments/Accruals	15.6
Healthcare	12.3
Industrials	10.3
Consumer Discretionary	9.0
Consumer Staples	8.8
Utilities	5.1
Other	4.9
Materials	2.6
Information Technology	2.0
Total	<u>100.0 %</u>

INVESTMENT SECTION

Report on Investment Activity (Continued)

At the close of fiscal year 2006, the Corporate Bond pool represented 5.8% of total investments. This compares to 8.6% for fiscal year 2005. The following summarizes the System's 2.1% ownership share of the Corporate Bond pool at September 30, 2006:

Corporate Bond Pool (in thousands)

Short Term Pooled Investments	\$	10,196
Fixed Income Securities		58,962
Accrued dividends		680
Total	\$	69,838

Fixed Income Core Pools

Five Fixed Income Core managers were selected in fiscal year 2006, and they began managing assets for the System beginning March 31, 2006. Their investment objective is to generate a rate of return exceeding the Lehman Aggregate Index net of fees.

The System hired Delaware Investments, Dodge & Cox, Dupont Capital Management, Fidelity Management Trust, and Metropolitan West Asset Management.

The Fixed Income Core pools combined rate of return from inception to fiscal year end was 3.6%.

At the close of fiscal year 2006, the Fixed Income Core pools represented 1.0% of total investments. The following summarizes the System's ownership share and composition of the five Fixed Income Core pools at September 30, 2006:

Fixed Income Core Pools (in thousands)

	Delaware Fixed Income Core	Dodge & Cox Fixed Income Core	Dupont Fixed Income Core	Fidelity Fixed Income Core	Metro West Fixed Income Core
Total Investment	\$ 2,271	\$ 2,260	\$ 1,135	\$ 3,417	\$ 2,272
Ownership Percentage	2.2%	2.2%	2.2%	2.2%	2.2%

Corporate Fixed Income Manager Pools

Four Corporate Fixed Income managers were selected in fiscal year 2006, and they began managing assets for the System beginning September 15, 2006. Their investment objective is to generate a rate of return exceeding the Lehman Credit Index net of fees.

The System hired AllianceBernstein, Prudential Financial, Western Asset, and Taplin, Canida & Habacht.

INVESTMENT SECTION

The Corporate Fixed Income Manager pools combined rate of return from inception to fiscal year end was 0.7%.

Report on Investment Activity (Continued)

At the close of fiscal year 2006, the Corporate Fixed Income Manager pools represented 0.9% of total investments. The following summarizes the System's ownership share and composition of the four Corporate Fixed Income Manager pools at September 30, 2006:

	Corporate Fixed Income Manager Pools			
	(in thousands)			
	Alliance Bernstein Corporate	Prudential Financial Corporate	Western Asset Corporate	Taplin, Canida & Habacht Corporate
Total Investment	\$ 2,197	\$ 3,853	\$ 2,201	\$ 2,734
Ownership Percentage	2.2%	2.2%	2.2%	2.2%

Short Term Investment 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 4.7% versus the benchmark's 4.4%.

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, 2006, 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 2006, the Short Term Investment pool represented 2.1% of total investments. This compares to 2.7% for fiscal year 2005. The System's ownership share of the Short Term Investment pool at September 30, 2006 was \$25,907,367 composed of fixed income securities and equity in common cash.

Tactical Asset Allocation Pool

A Tactical Asset Allocation (TAA) Pool was established in June 2006 to allow the System more flexibility in achieving its investment goals. The TAA can be used to capitalize on shorter-term windows of investment opportunities without disturbing the return/risk profiles of the longer-term strategies of the underlying investment pools.

The Tactical Asset Allocation pool return from inception to fiscal year end was 7.5%.

INVESTMENT SECTION

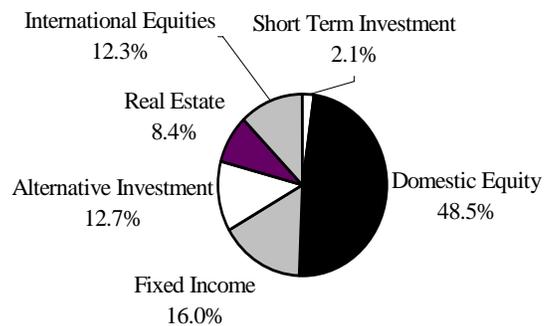
Report on Investment Activity (Continued)

At the close of fiscal year 2006, the Tactical Asset Allocation pool represented 0.6% of total investments. The following summarizes the System's 2.2% ownership share of the Tactical Asset Allocation pool at September 30, 2006:

Tactical Asset Allocation Pool (in thousands)

Net Equities	\$ 723
Fixed Income Securities	<u>6,241</u>
Total	<u><u>\$ 6,964</u></u>

Asset Allocation – Security Type



INVESTMENT SECTION

Investment Results for the Period Ending September 30, 2006

<u>Investment Category</u>	<u>Current Year</u>	<u>Annualized Rate of Return¹</u>		
		<u>3 Years</u>	<u>5 Years</u>	<u>10 Years</u>
Total Portfolio	12.9 %	12.7 %	8.1 %	8.7 %
Total Domestic Equity	10.8	12.0	7.5	9.1
S&P 1500 Index	10.3	12.8	7.7	9.0
Large Cap Value Pool	15.8	15.9		
Large Cap Growth Pool	7.2	7.5		
Mid Cap Pool	7.1			
Small Cap Pool	8.3	12.5		
S&P 500 Index Pool	10.8	12.3		
S&P MidCap Index Pool	6.9	15.4		
S&P Small Cap Index Pool	7.5	17.5		
International Equity Pool - Passive	17.5	21.3	12.8	8.2
S&P Citigroup BMI - EPAC 50/50	18.5	22.3	13.4	7.8
International Equity Pool - Active	19.7			
Alternative Investments Pool	26.3	23.6	9.7	12.0
S&P 500 Index plus 300 Basis Points	13.9	15.4	10.3	12.1
Credit Suisse Asset Management (Stock Distributions)	(19.8)	(8.2)		
Real Estate Pool	18.9	13.7	11.1	11.4
NCREIF Property Blended Index ²	16.3	15.4	11.6	11.7
Total Fixed Income	4.0	3.4	4.6	6.2
Lehman Brothers Government/Credit	3.3	3.1	5.0	6.5
Government Bond Pool	4.3	3.6		
Corporate Bond Pool	3.6	3.3		
Short Term Investment Pool	4.7	2.7	2.4	4.1
30 Day Treasury Bill	4.4	2.6	2.2	3.5

¹Calculations used a time-weighted rate of return based on the market rate of return in accordance with industry standards.

²As of 10/1/05, index is NCREIF less 130 bp. History prior to 10/1/05 reflects NCREIF less 75 bp.

INVESTMENT SECTION

Largest Assets Held

Largest Stock Holdings (By Market Value)¹ September 30, 2006

Rank	Shares	Stocks	Market Value
1	268,536	Exxon Mobil Corporation	\$ 18,018,749
2	438,106	General Electric Corporation	15,465,130
3	271,556	Citigroup Incorporated	13,488,174
4	218,678	Bank of America Corporation	11,714,589
5	384,028	Microsoft Corporation	10,495,494
6	355,566	Pfizer Incorporated	10,083,841
7	135,423	American International Group	8,973,096
8	137,246	Procter and Gamble Corporation	8,506,477
9	129,283	Johnson and Johnson	8,395,644
10	178,611	JP Morgan Chase & Co	8,387,551

Largest Bond Holdings (By Market Value)¹ September 30, 2006

Rank	Par Amount	Description	Market Value
1	\$ 6,478,845	Canadian Imperial Bank 0% Coupon Due 6-14-2007	\$ 6,240,812
2	4,891,203	U.S. Treasury Strip 0% Coupon Due 11-15-2011	4,861,415
3	4,386,282	Bank Nova Scotia 5.38188% FRN Due 10-12-2007	4,386,449
4	4,093,958	Treasury Inflation Index Due 7-15-14	4,328,928
5	4,302,666	US Bank NA 5.37% FRN Due 4-5-2007	4,306,491
6	3,289,712	Household Finance Corporation 5.47375% FRN Due 10-22-2007	3,298,327
7	3,150,351	Wells Fargo & Company 5.42375% FRN Due 9-28-2007	3,153,303
8	3,150,351	Canadian Imperial Bank 5.42% FRN Due 1-5-2007	3,150,389
9	2,851,083	Citigroup Global Markets 5.555% FRN Due 1-30-2007	2,852,261
10	2,412,455	JP Morgan Chase & Co 5.50% FRN Due 1-5-2007	2,413,809

¹ A complete list of holdings is available from the Michigan Department of Treasury.

The Plan's assets are commingled in various pooled accounts. Amounts, par value, and number of shares represent the System's pro-rata share based on its ownership of the investment pools.

INVESTMENT SECTION

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 26.5% of the total investment portfolio is managed by fully discretionary outside advisors. The Michigan Department of Treasury's cost of operations applicable to the retirement system for the fiscal year end amounted to \$226 thousand or two and six tenths basis points (.026%) of the market value of the Asset under Management by the State Treasurer.

Act 380 of the Public Acts of 1965 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 (in thousands)	Fees (in thousands)	Basis Points *
State Treasurer	\$ 883,237	\$ 226	2.6
Outside Advisors -			
Fixed Income	22,338	5	
Mid Cap Equity	25,221	97	38.4
Small Cap Equity	11,966	80	67.0
International Equity	36,649	60	16.4
Alternative	150,022	1,208	80.5
Real Estate	72,030	64	8.9
Total	\$ 1,201,463	\$ 1,740	213.8

Other Investment Services Fees:

Custody & Research Fees	\$ 1,175,556	\$ 48
Security Lending Fees	182,643	40

* Outside Advisors Fees are netted against income for Fixed Income, Small Cap, Mid Cap Equity, 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 150 basis points. Alternative and Real Estate fees, in most cases, are included in the net income of the partnership and are not reflected in the Schedule of Fees.

Schedule of Investment Commissions

	Fiscal Year Ended September 30, 2006						
	Actual	Actual	Average	Estimated	Estimated	Estimated	Estimated
	Commissions	Number of	Commission	Trade	Research	Trade	Research
	Paid ⁽¹⁾	Shares	Rate	Costs	Costs	Costs	Costs
	Traded ⁽¹⁾	Per Share	Per Share	Per Share	Per Share	Per Share	Per Share
Investment Brokerage Firms:							
ADP Clearing & Outsourcing Services, Inc	\$ 13	254	\$ 0.05	\$ 0.02	\$ 0.03	\$ 5	\$ 8
Baird, Robert W., Company Inc	28	561	0.05	0.03	0.02	17	11
Banc/America Secur. LLC Montgomery Div	1,721	51,350	0.03	0.01	0.02	514	1,207
Bear Stearns & Co Inc	27,245	1,132,585	0.02	0.01	0.01	11,326	15,920
Bridge Treading	4,842	133,702	0.04	0.02	0.02	2,674	2,167
Broadcort Capital	1,637	50,587	0.03	0.02	0.01	1,012	625
BNY Brokerage Inc	27	532	0.05	0.03	0.02	16	11
B-Trande Service LLC	51	2,571	0.02	0.01	0.01	26	26
Cantor Fitzgerald & Co.	8,463	280,146	0.03	0.01	0.02	2,801	5,662
CIBC World Markets Corp	388	7,766	0.05	0.02	0.03	155	233
Citigroup Global Markets Inc	35,387	1,190,786	0.03	0.01	0.02	11,908	23,480
Credit Suisse First Boston Corporation	10,936	340,785	0.03	0.01	0.02	3,408	7,528
Deutsche Bank Securities Inc	4,934	141,780	0.03	0.01	0.02	1,418	3,517
Friedman Billings Ramsey	37	739	0.05	0.03	0.02	22	15
Fulcrum Global Partners	126	2,518	0.05	0.03	0.02	76	50
Goldman Sachs	17,717	596,809	0.03	0.01	0.02	5,968	11,749
Griswold Company	9,035	457,699	0.02	0.01	0.01	4,577	4,458
Howard Weil Division Legg Mason	582	14,543	0.04	0.02	0.02	291	291
Investment Technology Group Inc.	269	13,457	0.02	0.01	0.01	135	135
Instinet	80	4,014	0.02	0.01	0.01	40	40
ISI Group Inc	5,554	149,107	0.04	0.02	0.02	2,982	2,571
Janney Montgomery, Scott Inc	8	167	0.05	0.03	0.02	5	3
J P Morgan Securities Inc	10,741	293,546	0.04	0.02	0.02	5,871	4,870
Jefferies Company Inc	118	2,830	0.04	0.02	0.02	57	62
Labranche Financial (MARA)	22	1,090	0.02	0.01	0.01	11	11
Leerink Swann & Co	1,980	51,712	0.04	0.02	0.02	1,034	946
Lehman Brothers Inc	24,531	763,285	0.03	0.01	0.02	7,633	16,898
Liquidnetinc	145	7,274	0.02	0.01	0.01	73	73
Merrill Lynch, Pierce, Fenner & Smith, Inc	15,619	486,362	0.03	0.01	0.02	4,864	10,755
Midwest Research Securities	144	2,881	0.05	0.02	0.03	58	86
Mischler Financial Group, Inc	833	22,449	0.04	0.02	0.02	449	384
Morgan Keegan Co Inc	43	854	0.05	0.02	0.03	17	26
Morgan Stanley Co Inc	21,511	662,753	0.03	0.01	0.02	6,628	14,884
OTA Research	3,380	94,136	0.04	0.02	0.02	1,883	1,497
Pershing LLC	12	622	0.02	0.01	0.01	6	6
Prudential Equity Group	13,033	397,420	0.03	0.01	0.02	3,974	9,059
Raymond James and Associates Inc	173	4,321	0.04	0.02	0.02	86	86
SG Americas Securities LLC	229	4,846	0.05	0.03	0.02	145	84
S.G. Cowen & Co., LLC	6,610	189,400	0.03	0.01	0.02	1,894	4,716
Sanford Bernstein Co LLC	7,934	244,755	0.03	0.01	0.02	2,448	5,487
Stifel Nicolaus & Co LLC	172	3,448	0.05	0.03	0.02	103	69
Suntrust Capital Markets Inc	58	1,673	0.03	0.02	0.01	33	25
Thomas Weisel Partners	208	4,625	0.04	0.02	0.02	93	116
US Bancorp Piper Jaffray Inc	19	386	0.05	0.03	0.02	12	8
UBS Securities LLC	17,745	579,528	0.03	0.01	0.02	5,795	11,950
Wachovia Capital Markets, LLC	82	2,057	0.04	0.02	0.02	41	41
Wayne Company	732	18,291	0.04	0.02	0.02	366	366
Weeden & Co	56	1,114	0.05	0.03	0.02	33	22
WR Hambrecht & Co	2	38	0.05	0.03	0.02	1	1
	<u>\$ 255,212</u>	<u>8,414,154</u>	<u>\$ 0.03</u> ²	<u>\$ 0.02</u>	<u>\$ 0.01</u>	<u>\$ 92,984</u>	<u>\$ 162,235</u>

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

2 The average commission per share for all brokerage firms.

INVESTMENT SECTION

Investment Summary

Fiscal Year Ended September 30, 2006

	<u>Market Value (a)</u>	<u>Percent of Total Market Value</u>	<u>Investment & Interest Income (b)</u>	<u>Percent of Investment & Interest Income</u>
Fixed Income Pools	\$ 192,055,307	16.0%	\$ 7,496,917	5.3%
Domestic Equity Pools	582,758,980	48.5%	56,732,354	39.9%
Real Estate Pool	100,633,124	8.4%	17,165,248	12.1%
Alternative Investment Pools	152,186,251	12.7%	34,464,991	24.3%
International Equities Pools	147,922,103	12.3%	24,866,448	17.5%
Short Term Investment Pools	<u>25,907,367</u>	<u>2.1%</u>	<u>1,239,479</u>	<u>0.9%</u>
Total	<u>\$ 1,201,463,132</u>	<u>100.0%</u>	<u>\$ 141,965,437</u>	<u>100.0%</u>

(a) Market value excludes \$187,448,116 in cash collateral for security lending for fiscal year 2006.

(b) Total Investment & Interest Income excludes net security lending income of \$165,057.

INVESTMENT SECTION

Investment Summary (Continued)

Fiscal Year Ended September 30, 2005

	Market Value (a)	Percent of Total Market Value	Investment & Interest Income (b)	Percent of Investment & Interest
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 Pool	131,611,717	11.7%	26,602,825	20.1%
International Equities Pool	138,919,735	12.4%	30,381,768	22.9%
Short Term Investment Pools	30,743,229	2.7%	845,753	0.6%
Total	\$ 1,120,793,927	100.0%	\$ 132,494,702	100.0%

(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.

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ACTUARIAL SECTION

Actuary's Certification
Summary of Actuarial Assumptions and Methods
Schedule of Active Member Valuation Data
Retirant and Beneficiary Data
Prioritized Solvency Test
Analysis of Financial Experience
Summary of Plan Provisions

ACTUARIAL SECTION

Actuary's Certification



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

December 7, 2006

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, 2005 included a total of 4,574 members of MSPRS. The actuarial value of MSPRS's assets amounted to approximately \$1,090.3 million on September 30, 2005.

The assumptions used in the 2005 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, 2005 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 2005 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,

A handwritten signature in black ink that reads "Michael Karlin".

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

6031224v1/03603.001

Benefits, Compensation and HR Consulting ATLANTA BOSTON CALGARY CHICAGO CLEVELAND DENVER HARTFORD HOUSTON LOS ANGELES
MINNEAPOLIS NEW ORLEANS NEW YORK PHILADELPHIA PHOENIX PRINCETON RALEIGH SAN FRANCISCO TORONTO WASHINGTON, D.C.



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MEXICO CITY OSLO PARIS

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 healthy life 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 declining 50 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.
10. A 5-year experience investigation, covering the period from September 30, 1997 through September 30, 2002 was completed in April 2004. The purpose of the study was to analyze the actual experience of the System versus that anticipated by the actuarial assumptions then in use. The combined effect of the recommended changes in assumptions was an increase in actuarial accrued liabilities of approximately 0.1% and an 8.3% decrease in computed employer contributions. Adopted 2004.
11. Gabriel Roeder Smith & Company was awarded the actuarial and consulting services contract beginning October 4, 2006.

ACTUARIAL SECTION

Summary of Actuarial Assumptions and Methods (Continued)

SCHEDULE 1

Percent of Eligible Active Members Retiring Within Next Year

<u>Retirement Ages</u>	<u>Not Electing DROP</u>	<u>Electing DROP</u>	
First year eligible to retire			
49 and under	50 %	100 %	
After first year eligible to retire			
46 and under	35	100	
47	25	100	
48-49	25	100	
All Members		Over 25 Years	Under 25 Years
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

<u>Sample Ages</u>	<u>Years of Service</u>	<u>Percent of Active Members Withdrawing Within Next Year (Men and Women)</u>	<u>Percent of Active Members Becoming Disabled Within Next Year</u>		<u>Percent Increase In Pay During Next Year*</u>
			<u>Duty</u>	<u>Non-duty</u>	
All	0	6.50 %			93.50 %
	1	5.00			21.50
20	2 & Over	2.00	0.25 %	0.00 %	9.90
25	"	2.00	0.25	0.00	9.40
30	"	1.50	0.25	0.01	6.61
35	"	0.60	0.25	0.02	5.26
40	"	0.35	0.25	0.07	4.54
45	"	0.35	0.25	0.14	4.28
50	"	0.35	0.25	0.21	4.22
55	"		0.25	0.30	4.02
60 & Over	"		0.25	0.28	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 SECTION

Actuarial Valuation Data

Valuation Date <u>Sept. 30</u>	<u>Number</u>	<u>Reported Annual Payroll</u>	<u>Average Annual Pay</u>	<u>% Increase</u>	<u>Average Age</u>	<u>Average Service</u>
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	1,831	119,721,613	65,386	6.7	38.1	10.6
2005	1,708	117,648,748	68,881	5.3	38.3	12.0

Excludes DROP program participants who are still actively employed.

Retirant and Beneficiary Data Rolls End of Year

Year Ended <u>Sept. 30</u>	<u>Number</u>			<u>Average Monthly Benefit</u>			<u>Average Age</u>		
	<u>Pensioners</u>	<u>Widows</u>	<u>Children</u>	<u>Pensioners</u>	<u>Widows</u>	<u>Children</u>	<u>Pensioners</u>	<u>Widows</u>	<u>Children</u>
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
2005	2,182	379	8	2,747	1,562	511	63.1	74.2	11.5

ACTUARIAL SECTION

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.

(\$ in thousands)

Valuation Date	Actuarial Accrued Liability (AAL)			Valuation Assets	Portion of (AAL) Covered by Assets			
	(1)	(2)	(3)		(1)	(2)	(3)	(4) ³
	Active Member Contributions	Retirants and Beneficiaries	Active and Inactive Members (Employer Financed Portion)					
Sept. 30								
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
2005	295	909,741	390,307	1,090,327	100	100	46.2	83.8

¹ Revised asset valuation method.

² Change in assumptions and benefit provisions.

³ Percent funded on a total valuation asset and total actuarial accrued liability basis.

⁴ Change in assumptions and benefit provisions.

Analysis of Financial Experience

Gains/(Losses) in Accrued Liabilities During Year Ended September 30, 2005 Resulting from Differences Between Assumed Experience & Actual Experience

<u>Type of Activity</u>	<u>Gain/(Loss)</u>
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.	\$ (7,011,993)
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.	61,244
3. Pay Increases. If there are smaller pay increases than assumed, there is a gain. If greater increases, a loss.	3,330,444
4. Investment Income. If there is greater investment income than assumed, there is a gain. If less income, a loss.	(61,573,035)
5. Death After Retirement. If retirants live longer than assumed, there is a loss. If not as long, a gain.	(1,053)
6. New entrants/rehires. New entrants into the System will generally result in an actuarial loss. This does not apply to plans closed to new entrants.	(37,295)
7. Other. Miscellaneous gains and losses resulting from data adjustments, timing of financial transactions, etc.	<u>2,537,168</u>
8. Composite Gain (or Loss) During Year	<u><u>\$ (62,694,520)</u></u>

ACTUARIAL SECTION

Summary of Plan Provisions

Our actuarial valuation of the System as of September 30, 2005, 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 Credit 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 Revenues by Source
Schedule of Expenses by Type
Schedule of Changes in Net Assets
Schedule of Benefit and Refund Deductions by Type
Schedule of Retired Members by Type of Benefit
Schedule of Average Benefit Payments
Ten Year History of Membership

STATISTICAL SECTION

This part of the System's comprehensive annual financial report presents detailed information as a context for understanding what the information in the financial statements, note disclosures, and required supplementary information says about the System's overall financial health.

Contents

Financial Trends

These schedules contain trend information to help the reader understand how the System's financial performance and fiscal health has changed over time. The schedules are presented for the last ten fiscal years. Schedules included are:

- Schedule of Pension Plan Revenues by Source
- Schedule of Health Plan Revenues by Source
- Schedule of Pension Plan Expenses by Type
- Schedule of Health Plan Expenses by Type
- Schedule of Changes in Net Assets – Pension Plan
- Schedule of Changes in Net Assets – Health Plan
- Schedule of Benefit and Refund Deductions by Type

Operating Information

These schedules contain contextual information to assist the reader's understanding of how the System's financial information relates to the combination of participating members and the benefits it provides. The schedules are presented for the last ten fiscal years, except where noted. Schedules included are:

- Schedule of Retired Members by Type of Pension Benefit
- Schedule of Retired Members by Type of Health Benefit
- Schedule of Average Benefit Payments—Pension
- Schedule of Average Benefit Payments—Health
- Schedule of Average Benefit Payments—Dental
- Schedule of Average Benefit Payments—Vision
- Ten Year History of Membership

STATISTICAL SECTION

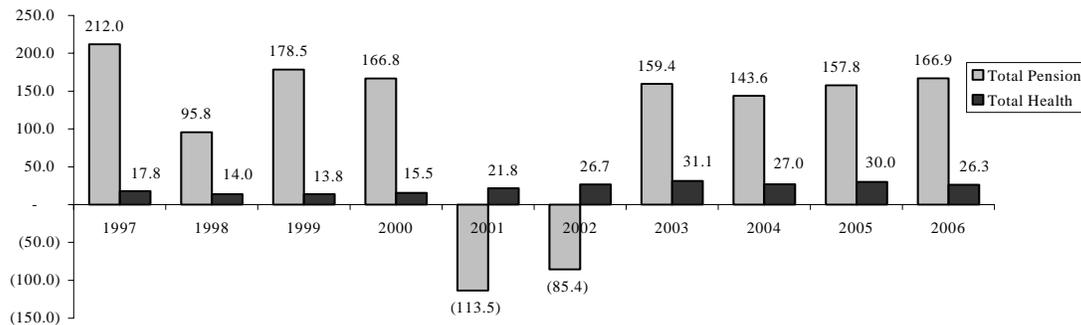
Schedule of Pension Plan Revenues by Source

Fiscal Year Ended Sept. 30	Member Contributions	Employer Contributions		Net Investment & Other Income	Total
		Dollars	% of Annual Covered Payroll		
1997	\$ 67,914	\$ 34,785,548	31.6 %	\$ 177,128,779	\$ 211,982,241
1998	38,727	20,003,807	18.5	75,726,277	95,768,811
1999	7,679	21,609,520	18.5	156,896,728	178,513,927
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	20.7	118,817,294	143,639,493
2005	112,303	26,607,572	22.6	131,111,123	157,830,998
2006	252,805	26,103,923	N/A	140,565,537	166,922,265

Schedule of Health Plan Revenues by Source

Fiscal Year Ended Sept. 30	Member Contributions	Employer Contributions		Net Investment & Other Income	Total
		Dollars	% of Annual Covered Payroll		
1997	\$ 644,885	\$ 17,066,083	15.5 %	\$ 107,113	\$ 17,818,081
1998	884,009	13,119,577	12.1		14,003,586
1999	992,839	12,838,366	11.0		13,831,205
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	21.2		26,999,152
2005	1,566,646	28,488,384	24.2		30,055,030
2006	1,254,352	25,021,287	N/A	4,319	26,279,958

Total Revenue
Year Ended September 30
(in millions)



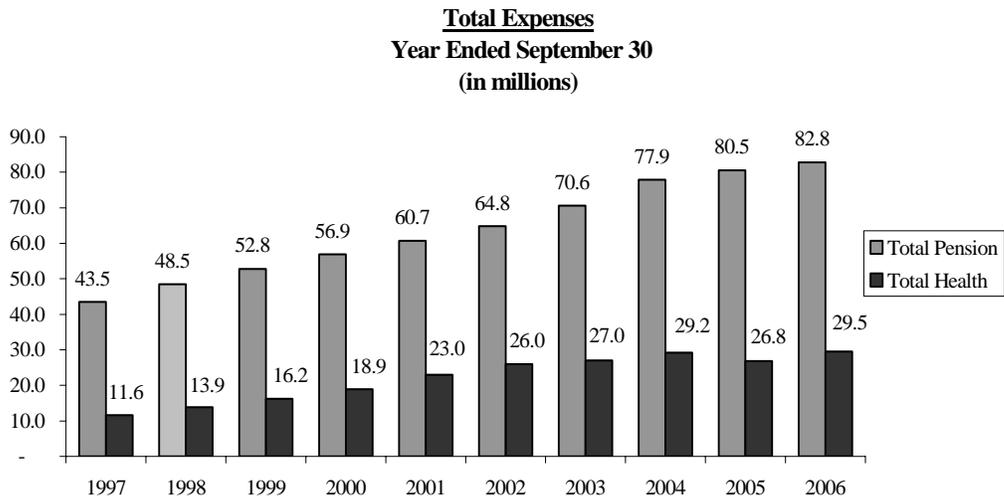
STATISTICAL SECTION

Schedule of Pension Plan Expenses by Type

<u>Fiscal Year Ended Sept. 30</u>	<u>Benefit Payments</u>	<u>Refunds and Transfers</u>	<u>Administrative and Other Expenses</u>	<u>Total</u>
1997	\$ 43,318,234		\$ 202,828	\$ 43,521,062
1998	48,227,332		225,327	48,452,659
1999	52,486,589	\$ 4,694	322,997	52,814,280
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
2006	82,316,931	142,979	343,205	82,803,115

Schedule of Health Plan Expenses by Type

<u>Fiscal Year Ended Sept. 30</u>	<u>Benefit Payments</u>	<u>Refunds and Transfers</u>	<u>Administrative and Other Expenses</u>	<u>Total</u>
1997	\$ 11,594,161			\$ 11,594,161
1998	13,856,103			13,856,103
1999	16,206,544			16,206,544
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
2006	29,492,740			29,492,740



STATISTICAL SECTION

Schedule of Changes in Net Assets-Pension Plan

Last Ten Years

(in thousands)

	Fiscal Year									
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Member contributions	\$ 68	\$ 39	\$ 8	\$ 17	\$ 197	\$ 113	\$ 78	\$ 30	\$ 112	\$ 253
Employer contributions	34,786	20,004	21,610	22,107	24,064	22,456	25,932	24,792	26,608	26,104
Net investment income	177,128	75,726	156,896	144,658	(137,798)	(108,017)	133,377	118,817	131,111	140,565
Total Additions	\$ 211,982	\$ 95,769	\$ 178,514	\$ 166,782	\$ (113,537)	\$ (85,448)	\$ 159,387	\$ 143,639	\$ 157,831	\$ 166,922
Pension benefits	\$ 43,318	\$ 48,228	\$ 52,486	\$ 56,693	\$ 60,407	\$ 64,418	\$ 70,152	\$ 77,592	\$ 80,170	\$ 82,317
Health care benefits	-	-	-	-	-	-	-	-	-	-
Refunds of member contributions	-	-	5	-	-	-	-	1	-	143
Administrative expenses	203	225	323	159	299	353	424	317	294	343
Total Deductions	\$ 43,521	\$ 48,453	\$ 52,814	\$ 56,852	\$ 60,706	\$ 64,771	\$ 70,576	\$ 77,910	\$ 80,464	\$ 82,803
Changes in net assets	\$ 168,461	\$ 47,316	\$ 125,700	\$ 109,930	\$ (174,243)	\$ (150,219)	\$ 88,811	\$ 65,729	\$ 77,367	\$ 84,119

Schedule of Changes in Net Assets-Health Plan

Last Ten Years

(in thousands)

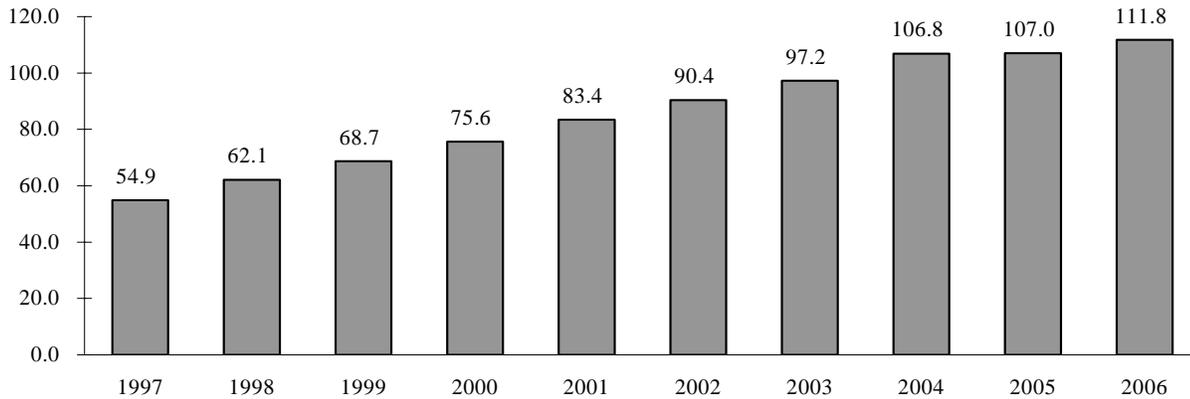
	Fiscal Year									
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Member contributions	\$ 645	\$ 884	\$ 993	\$ 1,098	\$ 1,265	\$ 1,380	\$ 1,501	\$ 1,572	\$ 1,567	\$ 1,255
Employer contributions	17,066	13,120	12,838	14,422	20,582	25,271	29,621	25,427	28,488	25,021
DC savings subaccount	-	-	-	-	-	-	-	-	-	-
Net investment income	107	-	-	-	-	-	-	-	-	4
Total Additions	\$ 17,818	\$ 14,004	\$ 13,831	\$ 15,520	\$ 21,847	\$ 26,651	\$ 31,122	\$ 26,999	\$ 30,055	\$ 26,280
Pension benefits	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Health care benefits	11,594	13,856	16,206	18,938	23,024	26,030	27,036	29,195	26,842	29,493
Refunds of member contributions	-	-	-	-	-	-	-	-	-	-
Administrative expenses	-	-	-	-	-	-	-	-	-	-
Total Deductions	\$ 11,594	\$ 13,856	\$ 16,206	\$ 18,938	\$ 23,024	\$ 26,030	\$ 27,036	\$ 29,195	\$ 26,842	\$ 29,493
Changes in net assets	\$ 6,224	\$ 148	\$ (2,375)	\$ (3,418)	\$ (1,177)	\$ 621	\$ 4,086	\$ (2,196)	\$ 3,213	\$ (3,213)

STATISTICAL SECTION

Schedule of Benefit and Refund Deductions by Type

Fiscal Year Ended Sept. 30	Regular Benefits	Disability Benefits	Survivor Benefits	Funeral Benefits	Health Benefits	Total	Refunds
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	\$ 4,694
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	6
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	1,434
2005	75,606,407	4,563,201			26,842,248	107,011,856	358
2006	71,830,448	3,993,123	\$ 6,493,361		29,492,740	111,809,672	142,979

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



STATISTICAL SECTION

Schedule of Retired Members by Type of Pension Benefit

September 30, 2005

<u>Amount Monthly Benefit</u>	<u>Number of Retirees</u>	<u>Type of Retirement *</u>						<u>Option **</u>
		<u>1</u>	<u>2</u>	<u>3</u>	<u>4</u>	<u>5</u>	<u>6</u>	<u>Life</u>
\$ 001 - 400	36	26	1	2	1	4	2	36
401 - 800	140	114	7	4	5	0	10	140
801 - 1,200	301	138	115	19	4	16	9	301
1,201 - 1,600	297	176	71	31	9	5	5	297
1,601 - 2,000	211	154	27	13	6	4	7	211
2,001 - 2,400	147	107	17	10	7	2	4	147
2,401 - 2,800	326	262	28	26	7	1	2	326
2,801 - 3,200	497	457	16	16	3	2	3	497
3,201 - 3,600	417	406	4	5	0	0	2	417
3,601 - 4,000	230	224	2	4	0	0	0	230
Over 4,000	<u>124</u>	<u>122</u>	<u>1</u>	<u>1</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>124</u>
Totals	<u><u>2,726</u></u>	<u><u>2,186</u></u>	<u><u>289</u></u>	<u><u>131</u></u>	<u><u>42</u></u>	<u><u>34</u></u>	<u><u>44</u></u>	<u><u>2,726</u></u>

* Type of Retirement

- 1 - Normal retirement for age & service
- 2 - Survivor payment - normal or early retirement
- 3 - Duty disability retirement (incl. survivors)
- 4 - Non-duty disability retirement (incl. survivors)
- 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

STATISTICAL SECTION

Schedule of Retired Members by Type of Health Benefit September 30, 2005

Amount of Monthly Benefit	Eligible Retirees	Type of Other Post - Employment Benefits		
		Health	Dental	Vision
\$ 1 - 400	36	6	7	7
401 - 800	140	57	54	56
801 - 1,200	301	222	214	213
1,201 - 1,600	297	255	249	249
1,601 - 2,000	211	195	188	190
Over 2,000	1,741	1,684	1,690	1,691
Totals	2,726	2,419	2,402	2,406

*Participating member totals displayed in this schedule and the information presented in Note 1 of this report may differ. These variances are the result of a mid-year data conversion.

STATISTICAL SECTION

Schedule of Average Benefit Payments - Pension

Last Ten Years

Payment Periods	Credited Service (Years)							Total
	0-5	5-10	10-15	15-20	20-25	25-30	30+	
Period 10/1/95 to 9/30/96								
Average Monthly Benefit	\$ 757	\$ 952	\$ 775	\$ 959	\$ 1,255	\$ 1,814	\$ 2,180	\$ 1,709
Average Final Average Salary	3,752	18,858	20,419	20,860	25,543	33,351	41,832	31,620
Number of Active Retirants	82	20	61	64	98	1,383	207	1,915
Period 10/1/96 to 9/30/97								
Average Monthly Benefit	\$ 750	\$ 1,112	\$ 789	\$ 1,016	\$ 1,324	\$ 1,971	\$ 2,295	\$ 1,840
Average Final Average Salary	2,411	18,858	21,369	21,482	25,967	34,903	42,786	32,846
Number of Active Retirants	86	20	70	67	98	1,463	214	2,018
Period 10/1/97 to 9/30/98								
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 10/1/98 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
Period 10/1/04 to 9/30/05:								
Average Monthly Benefit	\$ 881	\$ 1,692	\$ 1,023	\$ 1,494	\$ 1,688	\$ 2,704	\$ 2,955	\$ 2,466
Average Final Average Salary	1,150	34,621	28,069	31,362	30,799	46,663	51,067	42,364
Number of Active Retirants	171	32	103	79	105	1,955	281	2,726

Source: The Segal Company

STATISTICAL SECTION

Schedule of Average Benefit Payments - Health

September 30, 2005

Retirement Effective Dates

	Years Credited Service							Total
	0 - 5	5 - 10	10 - 15	15 - 20	20 - 25	25 - 30	30 +	
Period 10/1/04 to 9/30/05								
Average Monthly Benefit	1,403	1,866	1,121	1,512	2,511	2,770	2,974	2,611
Average FAC	17,124	33,041	27,280	31,346	43,452	48,672	53,253	46,154
Number of Active Retirants	9	26	79	70	714	1,253	268	2,419 *

*Participating member totals displayed in this schedule and the information presented in Note 1 of this report may differ. These variances are the result of a mid-year data conversion.

Schedule of Average Benefit Payments - Dental

September 30, 2005

Retirement Effective Dates

	Years Credited Service							Total
	0 - 5	5 - 10	10 - 15	15 - 20	20 - 25	25 - 30	30 +	
Period 10/1/04 to 9/30/05								
Average Monthly Benefit	1,403	1,866	1,126	1,512	2,535	2,783	2,979	2,627
Average FAC	17,124	33,041	27,185	31,346	44,039	48,958	53,354	46,504
Number of Active Retirants	9	26	77	70	703	1,250	267	2,402 *

*Participating member totals displayed in this schedule and the information presented in Note 1 of this report may differ. These variances are the result of a mid-year data conversion.

Schedule of Average Benefit Payments - Vision

September 30, 2006

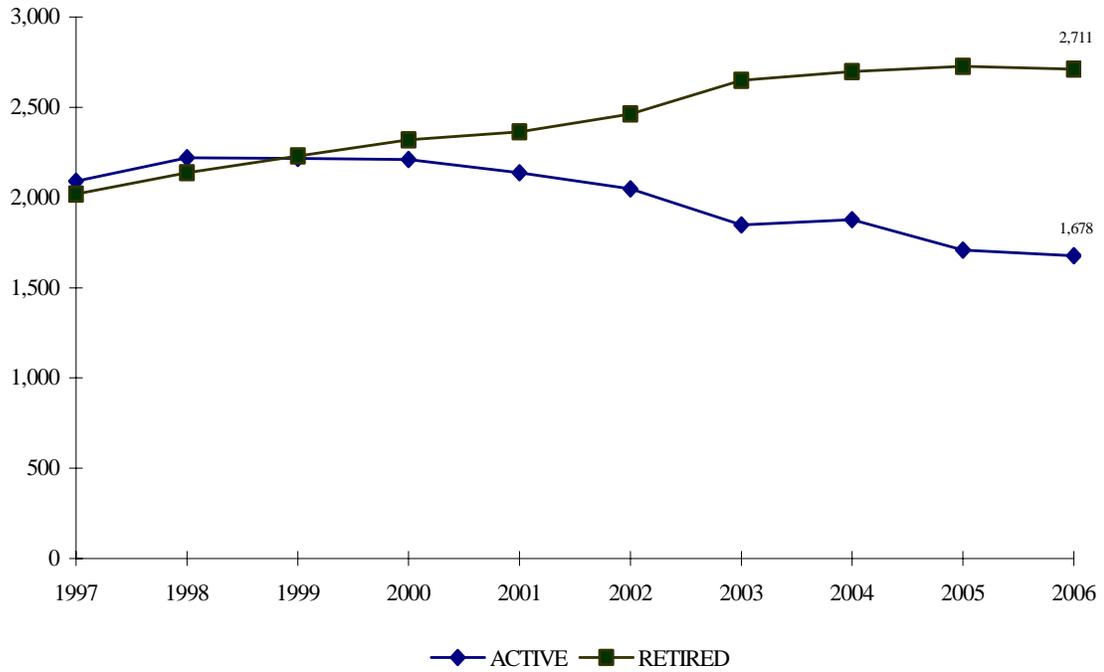
Retirement Effective Dates

	Years Credited Service							Total
	0 - 5	5 - 10	10 - 15	15 - 20	20 - 25	25 - 30	30 +	
Period 10/1/04 to 9/30/05								
Average Monthly Benefit	1,403	1,866	1,114	1,499	2,534	2,783	2,979	2,625
Average FAC	17,124	33,041	27,540	30,941	44,016	48,971	53,354	46,491
Number of Active Retirants	9	26	78	71	703	1,252	267	2,406 *

*Participating member totals displayed in this schedule and the information presented in Note 1 of this report may differ. These variances are the result of a mid-year data conversion.

STATISTICAL SECTION

Ten Year History of Membership Fiscal Year Ended September 30



Source: The Segal Company

ACKNOWLEDGMENTS

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 2005-2006 report included:

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