



ALASKA STATE PENSION INVESTMENT BOARD

Public Employees' Retirement System

Invested Assets

June 30, 2005 and 2004

(With Independent Auditors' Report Thereon)

ALASKA STATE PENSION INVESTMENT BOARD

Public Employees' Retirement System

Invested Assets

June 30, 2005 and 2004

Table of Contents

	<u>Page</u>
Independent Auditors' Report	1
Schedules of Invested Assets	2
Schedules of Investment Income and Changes in Invested Assets	3
Notes to Schedules.....	4



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Independent Auditors' Report

Alaska State Pension Investment Board and
State of Alaska, Department of Revenue
Division of Treasury:

We have audited the accompanying schedules of invested assets of the Public Employees' Retirement System as of June 30, 2005 and 2004 and of investment income and changes in invested assets of the Public Employees' Retirement System for the years then ended (schedules). These schedules are the responsibility of the Division of Treasury's management. Our responsibility is to express an opinion on these schedules based on our audits.

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

The accompanying schedules were prepared to present the invested assets of the Public Employees' Retirement System, which is established under the State of Alaska Public Employees Retirement System (PERS). The schedules are not intended to present the financial status of PERS.

In our opinion, the schedules referred to above present fairly, in all material respects, the invested assets of the Public Employees' Retirement System as of June 30, 2005 and 2004, and the investment income and changes in invested assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

August 25, 2005

ALASKA STATE PENSION INVESTMENT BOARD

PUBLIC EMPLOYEES' RETIREMENT SYSTEM

SCHEDULES OF INVESTED ASSETS

June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Investments (at Fair Value) (Notes 4, 7)		
Cash and Cash Equivalents		
Short-term Fixed Income Pool (Note 3)	\$ 653,551	\$ 510,556
Securities Lending Collateral (Note 7)	659,801,022	993,267,894
Total Cash and Cash Equivalents	<u>660,454,573</u>	<u>993,778,450</u>
Marketable Debt Securities (Note 3)		
Domestic Fixed Income Pool	1,910,374,412	2,209,350,038
International Fixed Income Pool	319,300,896	297,481,250
High Yield Pool	138,443,544	-
Total Marketable Debt Securities	<u>2,368,118,852</u>	<u>2,506,831,288</u>
Equity Securities (Note 3)		
Domestic Equity Pool	3,296,280,295	3,298,973,034
International Equity Pool	1,337,642,720	1,364,094,145
Emerging Markets Equity Pool	134,075,977	99,177,084
Private Equity Pool	379,843,136	269,232,951
Absolute Return Pool	210,613,031	-
Total Equity Securities	<u>5,358,455,159</u>	<u>5,031,477,214</u>
Other Investments Pool (Note 3)	<u>31,763,002</u>	<u>8,160,418</u>
Real Estate Investments		
Real Estate Pool (Note 3)	827,537,553	628,393,630
Mortgages (Note 2)	10,335	118,650
Total Real Estate Investments	<u>827,547,888</u>	<u>628,512,280</u>
Total Invested Assets	<u>9,246,339,474</u>	<u>9,168,759,650</u>
Securities Lending Collateral Payable (Note 7)	<u>659,801,022</u>	<u>993,267,894</u>
Net Invested Assets	<u>\$ 8,586,538,452</u>	<u>\$ 8,175,491,756</u>

See accompanying notes to schedules

ALASKA STATE PENSION INVESTMENT BOARD
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

**SCHEDULES OF INVESTMENT INCOME
AND CHANGES IN INVESTED ASSETS**

Years ended June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Investment Income		
Short-term Fixed Income Pool	\$ 72,448	\$ 33,119
Securites Lending (net of \$13,221,426 and \$7,447,729 expense)	1,535,860	1,849,021
Domestic Fixed Income Pool	141,266,215	15,632,101
International Fixed Income Pool	29,657,869	20,737,849
High Yield Pool	2,159,769	-
Domestic Equity Pool	149,825,900	572,605,034
International Equity Pool	175,658,609	352,309,287
Emerging Markets Equity Pool	35,141,474	24,963,546
Private Equity Pool	54,974,867	47,088,265
Absolute Return Pool	5,115,692	-
Other Investments Pool	1,084,939	38,756
Real Estate Pool	114,263,074	48,438,019
Mortgages	<u>22,004</u>	<u>12,976</u>
Total Investment Income	710,778,720	1,083,707,973
Total Invested Assets, Beginning of Year	8,175,491,756	7,389,406,007
Net Withdrawals	<u>(299,732,024)</u>	<u>(297,622,224)</u>
Total Invested Assets, End of Year	<u>\$ 8,586,538,452</u>	<u>\$ 8,175,491,756</u>

See accompanying notes to schedules

Public Employees' Retirement System

Invested Assets

Notes to Schedules

June 30, 2005 and 2004

(1) THE ACCOUNTING ENTITY

The Public Employees' Retirement System Invested Assets (PERS Invested Assets) is the investment portfolio of the State of Alaska Public Employees' Retirement System (PERS). PERS is a multiple employer, joint contributory, agent-defined benefit system established for the payment of retirement, disability and death benefits to, or on behalf of, qualified employees of the State of Alaska (State) or a political subdivision within the State. These schedules are those of PERS Invested Assets and not PERS taken as a whole. Fiduciary responsibility for PERS Invested Assets resides with the Alaska State Pension Investment Board (Board), pursuant to Alaska Statutes 37.10.210-390.

Alaska Statutes 39.35.080 and 37.10.071 provide that investments shall be made with the judgment and care under circumstances then prevailing that an institutional investor of ordinary professional prudence, discretion and intelligence exercises in managing large investment portfolios.

The Department of Revenue, Treasury Division (Treasury) provides staff for the Board. Treasury has created a pooled environment by which it manages the investments the Board has fiduciary responsibility for. Actual investing is performed by investment officers in Treasury or by contracted external investment managers. The Board has developed investment guidelines, policies and procedures for Treasury staff and external investment managers to adhere to when managing investments. Specifically, the Securities Lending Collateral, External Domestic Fixed Income Pool, International Fixed Income Pool, High Yield Pool, Domestic Equity Pool, International Equity Pool, Emerging Markets Equity Pool, Private Equity Pool, Absolute Return Pool, Other Investments Pool and, with the exception of real estate investment trust holdings, the Real Estate Pool are managed by external management companies. Treasury manages the Alaska Retirement Fixed Income Pool, real estate investment trust holdings and cash holdings of certain external managers in addition to acting as oversight manager for all externally managed investments.

The Short-term Fixed Income Pool is a State pool managed by Treasury.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The schedules are prepared using the accrual basis of accounting for investment income. Assets are reported at fair value in accordance with Governmental Accounting Standards Board (GASB) Statement No. 31. Investment purchases and sales are recorded on a trade-date basis. Net withdrawals represent contributions from employers and employees, net of benefits paid to PERS participants as well as administrative and investment management expenses. Contributions, benefits paid and all expenses are recorded on a cash basis.

Valuation

Marketable debt securities are valued each business day using prices obtained from a pricing service when such prices are available; otherwise, such securities are valued at the mid-point between the bid and asked price or at prices for securities of comparable maturity, quality and type.

Domestic and international equity securities are valued each business day using prices obtained from a pricing service or prices quoted by one or more independent brokers.

Emerging markets securities are valued at their current market or fair values on the last business day of each month by the Trustee.

Private equity securities are valued quarterly by the general partners and investment sponsors. The private equity oversight manager is held to a standard of reasonable care in verifying that the valuations reasonably reflect the underlying fair value of the investments.

Public Employees' Retirement System

Invested Assets

Notes to Schedules

June 30, 2005 and 2004

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Valuation (Cont.)

Absolute return investments are valued monthly by the general partners. The fund administrators are held to a standard of reasonable care in verifying that the valuations reasonably reflect the underlying fair value of the investments.

The energy related investment in the Other Investments Pool is valued quarterly by the general partner. The agricultural investments are valued quarterly by investment managers. Valuations are based on market conditions and knowledge of industry trends. Agricultural holdings are appraised once every three years, in conjunction with the purchase anniversary date, by independent appraisers.

With the exception of real estate investment trust holdings, real estate investments are valued quarterly by investment managers based on market conditions and their knowledge of industry trends. Separate account real estate investments are appraised once every three years, in conjunction with the property's purchase anniversary date, by independent appraisers. Real estate investment trust holdings are valued each business day using prices obtained from a pricing service.

Securities expressed in terms of foreign currencies are translated into U.S. dollars at the prevailing exchange rates. Forward currency contracts are valued at the mid-point of representative quoted bid and asked prices.

Mortgage loans are valued at their principal balance (cost) less an allowance for loan loss, the net result of which approximates fair value. At June 30, 2005 and 2004, the allowance for loan loss totaled \$5,221, and \$16,221 respectively, and is considered by management to be sufficient to cover any losses to the mortgage loan portfolio.

Income Allocation

Income in the fixed income and domestic and international equity pools is allocated to pool participants daily on a pro rata basis.

Income, in the Emerging Markets, Private Equity, Absolute Return, Other Investments, and Real Estate Pools is allocated to pool participants monthly on a pro rata basis.

Reclassifications

Certain reclassifications not affecting net changes in invested assets have been made to 2004 amounts in order to conform to the 2005 presentation.

(3) POOLED INVESTMENTS

Short-term Fixed Income Pool

PERS Invested Assets include participation in the State's internally managed Short-term Fixed Income Pool which was established March 15, 1993, with a start up and maintained share price of \$1. Treasury staff determines the allocation between permissible securities. Each participant owns shares in the pool, the number of which fluctuates daily with contributions and withdrawals. Participant shares also change at the beginning of each month when income is paid. At June 30, 2005 and 2004, PERS Invested Assets included a 0.03% direct ownership in the Short-term Fixed Income Pool which included interest receivable of \$8,927 and \$5,103 respectively. PERS Invested Assets included a 3.35% and 7.17% indirect ownership in the Short-term Fixed Income Pool at June 30, 2005 and 2004, respectively.

Public Employees' Retirement System

Invested Assets

Notes to Schedules

June 30, 2005 and 2004

(3) POOLED INVESTMENTS (Cont.)

Domestic Fixed Income Pool

The Domestic Fixed Income Pool is comprised of an internally managed and an externally managed pool.

Retirement Fixed Income Pool

PERS Invested Assets include participation in the Board's internally managed Retirement Fixed Income Pool which was established March 1, 1996, with a start up share price of \$1,000. The share price at June 30, 2005, was \$1,848. Treasury staff determines the allocation between permissible securities. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2005 and 2004, PERS Invested Assets included a 67.32% and 67.03% ownership in the Retirement Fixed Income Pool, respectively.

External Domestic Fixed Income Pool

PERS Invested Assets include participation in the Board's externally managed Domestic Fixed Income Pool which was established June 25, 1999, with a start up share price of \$1,000. The share price at June 30, 2005, was \$1,546. Each manager independently determines the allocation between permissible securities. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2005 and 2004, PERS Invested Assets included a 66.86% and 66.73% ownership in the External Domestic Fixed Income Pool, respectively.

International Fixed Income Pool

PERS Invested Assets include participation in the Board's externally managed International Fixed Income Pool which was established March 3, 1997, with a start up share price of \$1,000. The share price at June 30, 2005, was \$1,790. The manager independently determines the allocation between permissible securities. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2005 and 2004, PERS Invested Assets included a 67.81% and 67.32% ownership in the International Fixed Income Pool, respectively.

High Yield Pool

PERS Invested Assets include participation in the Board's externally managed High Yield Pool which was established April 15, 2005, with a start up share price of \$1,000. The share price at June 30, 2005, was \$1,016. The manager independently determines the allocation between permissible securities. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2005, PERS Invested Assets included a 68.14% ownership in the High Yield Pool.

Domestic Equity Pool

Effective July 1, 2005, the Domestic Equity Pool was replaced with an External Large Cap Domestic Equity Pool and an External Small Cap Domestic Equity Pool. At June 30, 2004, PERS Invested Assets included a 67.20% ownership in the Domestic Equity Pool.

Public Employees' Retirement System

Invested Assets

Notes to Schedules

June 30, 2005 and 2004

(3) POOLED INVESTMENTS (Cont.)

Large Cap Domestic Equity Pool

PERS Invested Assets include participation in the Board's externally managed Large Cap Domestic Equity Pool which was established July 1, 2004, with a start up share price of \$1,000. The share price at June 30, 2005, was \$1,050. Each manager independently determines the allocation between permissible securities. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2005, PERS Invested Assets included a 67.63% ownership in the Large Cap Domestic Equity Pool.

Small Cap Domestic Equity Pool

PERS Invested Assets include participation in the Board's externally managed Small Cap Domestic Equity Pool which was established July 1, 2004, with a start up share price of \$1,000. The share price at June 30, 2005, was \$1,019. Each manager independently determines the allocation between permissible securities. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2005, PERS Invested Assets included a 67.70% ownership in the Small Cap Domestic Equity Pool.

International Equity Pool

PERS Invested Assets include participation in the Board's externally managed International Equity Pool which was established January 1, 1992, with a start up share price of \$1,000. The share price at June 30, 2005, was \$2,622. Each manager independently determines the allocation between permissible securities. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2005 and 2004, PERS Invested Assets included a 68.00% and 67.46% ownership in the International Equity Pool, respectively.

Emerging Markets Equity Pool

PERS Invested Assets include participation in the Board's externally managed Emerging Markets Equity Pool which was established May 2, 1994, with a start up share price of \$1,000. The share price at June 30, 2005, was \$1,944. The pool participates in two externally managed commingled investment funds through ownership of equity shares. The commingled funds, comprised of various institutional investors, invest in the securities markets of developing countries. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2005 and 2004, PERS Invested Assets included a 65.00% ownership in the Emerging Markets Equity Pool.

Public Employees' Retirement System

Invested Assets

Notes to Schedules June 30, 2005 and 2004

(3) POOLED INVESTMENTS (Cont.)

Private Equity Pool

PERS Invested Assets include participation in the Board's externally managed Private Equity Pool which was established April 24, 1998, with a start up share price of \$1,000. The share price at June 30, 2005, was \$1,365. Underlying assets in the pool are comprised of venture capital, buyouts, restructuring and special situation investments through limited partnership agreements. Each manager independently determines the limited partnerships to invest in. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2005 and 2004, PERS Invested Assets included a 68.15% and 67.68% ownership in the Private Equity Pool, respectively.

Absolute Return Pool

PERS Invested Assets include participation in the Board's externally managed Absolute Return Pool which was established October 31, 2004, with a start up share price of \$1,000. The share price at June 30, 2005, was \$1,027. Underlying assets in the pool are comprised of hedge fund limited partnership agreements. Each manager independently determines the limited partnerships to invest in. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2005, PERS Invested Assets included a 68.15% ownership in the Absolute Return Pool.

Other Investments Pool

PERS Invested Assets include participation in the Board's externally managed Other Investments Pool which was established March 18, 2004, with a start up share price of \$1,000. The share price at June 30, 2005, was \$1,065. Underlying assets in the pool are comprised of a limited partnership interest in an energy related venture capital operating company and two agricultural entities. Each manager independently determines which permissible investments are made. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2005 and 2004, PERS Invested Assets included a 68.15% and 67.68% ownership in the Other Investments Pool.

Real Estate Pool

PERS Invested Assets include participation in the Board's externally managed Real Estate Pool which was established June 27, 1997, with a start up share price of \$1,000. The share price at June 30, 2005, was \$2,104. Underlying assets in the pool are comprised of separate accounts, commingled accounts, limited partnerships, and real estate investment trust holdings. With the exception of investments in real estate investment trusts, each manager independently determines which permissible investments are made. Treasury staff determine the permissible real estate investment trusts to invest in. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2005 and 2004, PERS Invested Assets included a 67.70% and 67.54% ownership in the Real Estate Pool, respectively.

Public Employees' Retirement System Invested Assets

Notes to Schedules June 30, 2005 and 2004

(4) DEPOSIT AND INVESTMENT RISK

At June 30, 2005, PERS Invested Assets included the following:

	Fair Value (in thousands)					
	Fixed Income Pools					Total
	Short-term	Domestic	International	High Yield	Other	
Deposits	\$ -	\$ -	\$ 6,587	\$ -	\$ 3,052	\$ 9,639
Overnight Sweep Account	88	935	-	37,348	-	38,371
Money Market Fund	-	-	-	-	659,801	659,801
Short-term Investment Fund	-	-	2,220	-	22,460	24,680
Commercial Paper	4,920	9,216	-	-	-	14,136
U. S. Treasury Bills	3,852	-	-	-	-	3,852
U. S. Treasury Notes	3,346	101,314	-	-	-	104,660
U. S. Treasury Bonds	-	123,573	-	-	-	123,573
U. S. Treasury Strips	-	25,160	-	-	-	25,160
U.S. Government Agency						
Discount Notes	851	7,245	-	-	-	8,096
U.S. Government Agency	-	125,170	-	-	-	125,170
Municipal Bonds	-	969	-	-	-	969
Foreign Government Bonds	-	-	212,977	-	-	212,977
Mortgage-backed	9,721	917,260	-	-	-	926,981
Other Asset-backed	27,264	112,094	-	272	-	139,630
Corporate Bonds	12,365	429,452	99,155	94,720	-	635,692
Convertible Bonds	-	-	-	1,445	-	1,445
Yankees:						
Government	-	9,502	-	-	-	9,502
Corporate	474	6,915	-	2,917	-	10,306
Domestic Equity Pool:						
Limited Partnership	-	-	-	-	177,777	177,777
Equity	-	-	-	-	3,074,626	3,074,626
International Equity Pool:						
Convertible Bonds	-	-	-	-	313	313
Equity	-	-	-	-	1,311,369	1,311,369
Emerging Markets Equity Pool	-	-	-	-	134,076	134,076
Private Equity Pool:						
Limited Partnerships	-	-	-	-	379,843	379,843
Absolute Return Pool:						
Limited Partnerships	-	-	-	-	210,613	210,613
Other Investments Pool:						
Limited Partnerships	-	-	-	-	15,097	15,097
Agricultural Holdings	-	-	-	-	16,666	16,666
Real Estate Pool:						
Real Estate	-	-	-	-	473,584	473,584
Commingled Funds	-	-	-	-	172,117	172,117
Limited Partnerships	-	-	-	-	104,288	104,288
Real estate investment trusts	-	-	-	-	76,249	76,249
Mortgages	-	-	-	-	10	10
Net Other Assets (Liabilities)	637	16,443	(1,638)	1,742	7,887	25,071
Ownership by Other Pools	(62,864)	25,126	-	-	37,738	-
PERS Invested Assets	\$ 654	\$ 1,910,374	\$ 319,301	\$ 138,444	\$ 6,877,566	\$ 9,246,339

Public Employees' Retirement System

Invested Assets

Notes to Schedules

June 30, 2005 and 2004

(4) DEPOSIT AND INVESTMENT RISK (Cont.)

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

Short-term Fixed Income Pool

As a means of limiting its exposure to fair value losses arising from increasing interest rates, Treasury's investment policy limits individual fixed rate securities to fourteen months in maturity or fourteen months expected average life. Floating rate securities are limited to three years in maturity or three years expected average life. Treasury utilizes the actual maturity date for commercial paper and twelve-month prepay speeds for other securities. At June 30, 2005, the expected average life of individual fixed rate securities ranged from one day to ten months and the expected average life of floating rate securities ranged from less than one year to three years.

Other Fixed Income Pools

Through the Board's investment policy, Treasury manages the exposure to fair value losses arising from increasing interest rates by limiting the effective duration of the domestic fixed income portfolio to $\pm 20\%$ of the Lehman Brothers Aggregate Bond Index. The effective duration for the Lehman Brothers Aggregate Bond Index at June 30, 2005, was 4.16 years.

Through the Board's investment policy, Treasury manages the exposure to fair value losses arising from increasing interest rates by limiting the effective duration of the international fixed income portfolio to $\pm 25\%$ of the Citigroup Non-U.S. World Government Bond Index. The effective duration for the Citigroup Non-U.S. World Government Bond Index at June 30, 2005, was 6.09 years.

Through the Board's investment policy, Treasury manages the exposure to fair value losses arising from increasing interest rates by limiting the effective duration of the high yield portfolio to $\pm 20\%$ of the Merrill Lynch U.S. High Yield Master II Index. The effective duration for the Merrill Lynch U.S. High Yield Master II Index at June 30, 2005, was 4.58 years. The High Yield Pool was funded April 15, 2005. Investment managers were in the transition period at year end working towards fully investing allocated funds. Funds not invested at year end have no duration causing the pool's duration to be lower than the policy limit.

Duration is a measure of interest rate risk. It measures a security's sensitivity to a 100-basis point change in interest rates. The duration of a pool is the average fair value weighted duration of each security in the pool taking into account all related cash flows.

Treasury uses industry-standard analytical software developed by The Yield Book Inc. to calculate effective duration. The software takes into account various possible future interest rates, historical and estimated prepayment rates, options and other variable cash flows for purposes of the effective duration calculation.

Public Employees' Retirement System Invested Assets

Notes to Schedules June 30, 2005 and 2004

(4) DEPOSIT AND INVESTMENT RISK (Cont.)

Interest Rate Risk (cont.)

At June 30, 2005, the effective duration of the fixed income pools, by investment type, was as follows:

	<u>Effective Duration (in years)</u>		
	<u>Domestic</u>	<u>International</u>	<u>High Yield</u>
U.S. Treasury Notes	3.27	-	-
U.S. Treasury Bonds	10.10	-	-
U.S. Treasury Strips	17.29	-	-
U.S. Government Agency	5.69	-	-
Municipal Bonds	13.95	-	-
Foreign Government Bonds	-	5.59	-
Mortgage-backed	2.50	-	-
Other Asset-backed	1.19	-	5.28
Corporate Bonds	5.27	4.17	3.59
Convertible Bonds	-	-	4.54
Yankees			
Government	6.98	-	-
Corporate	7.68	-	4.43
Portfolio Effective Duration	3.99	5.00	2.64

Credit Risk

Credit risk is the risk that an issuer or other counter party to an investment will not fulfill its obligations.

Treasury's investment policy has the following limitations with regard to credit risk:

With the exception of the sweep account, Short-term Fixed Income Pool investments are limited to instruments with a long-term credit rating of at least A3 or equivalent and instruments with a short-term credit rating of at least A1 or equivalent. For securities with long-term credit ratings, they may be purchased if the median rating of Standard & Poor's Corporation, Moody's and Fitch is A3 or equivalent. Asset-backed and non-agency mortgage securities may be purchased if only rated by one of the rating agencies mentioned above if they are rated AAA. Unexpected daily cash surpluses that arise in this pool are invested overnight in the custodian's repurchase agreement sweep account. Treasury does not have a policy to limit credit risk associated with the sweep account.

The Board's investment policy has the following limitations with regard to credit risk:

Domestic Fixed Income:

- Commercial paper must carry a rating of at least A1 or equivalent;
- Corporate debt securities must be investment grade;

Public Employees' Retirement System

Invested Assets

Notes to Schedules

June 30, 2005 and 2004

(4) DEPOSIT AND INVESTMENT RISK (Cont.)

Credit Risk (Cont.)

Domestic Fixed Income (cont.):

Corporate, asset-backed and non-agency mortgage securities must be investment grade. Investment grade is defined as the median rating of Standard & Poor's Corporation, Moody's and Fitch. Asset-backed and non-agency mortgage securities may be purchased if only rated by one of these agencies if they are rated AAA. Corporate bonds may be purchased if rated by two of these agencies.

International Fixed Income:

Corporate debt and asset-backed securities must be investment grade.

Domestic and International Equity:

Corporate debt obligations must carry a rating of at least A or equivalent.

High Yield

No more than ten percent of the portfolio's assets may be invested in securities rated A3 or higher.

No more than twenty-five percent of the portfolio's assets may be invested in securities rated below B3.

No more than five percent of the portfolio's assets may be invested in unrated securities.

The lower of any Standard & Poor's Corporation, Moody's or Fitch rating will be used for limits on securities rated below B3 and the higher rating will be used for limits on securities rated A3 or higher.

Daily cash surpluses that arise in this pool are invested in the custodian's repurchase agreement sweep account. This account is secured by U.S. Government or Agency securities. As such, the Board does not consider this investment subject to the credit risk limitations above.

Public Employees' Retirement System Invested Assets

Notes to Schedules June 30, 2005 and 2004

(4) DEPOSIT AND INVESTMENT RISK (Cont.)

Credit Risk (Cont.)

At June 30, 2005, PERS Invested Assets consisted of securities with credit quality ratings issued by nationally recognized statistical rating organizations as follows (using Standard & Poor's Corporation rating scale):

	Rating ¹	Fixed Income Pool				Inter- national Equity
		Short- term	Domestic	Internat- ional	High Yield	
Overnight Sweep Account	Not Rated	-	-	-	27%	-
Short-term Investment Account	Not Rated	-	-	1%	-	1%
Commercial Paper	A	8%	1%	-	-	-
U. S. Government Agency Discount Notes	Not Rated	1%	-	-	-	-
U. S. Government Agency Foreign Government	Not Rated	-	6%	-	-	-
Foreign Government	AAA	-	-	53%	-	-
Foreign Government	AA	-	-	9%	-	-
Foreign Government	A	-	-	5%	-	-
Mortgage-backed	AAA	15%	13%	-	-	-
Mortgage-backed (Agency)	Not Rated	-	34%	-	-	-
Other Asset-backed	AAA	39%	6%	-	-	-
Other Asset-backed	A	3%	-	-	-	-
Corporate Bonds	AAA	1%	3%	24%	-	-
Corporate Bonds	AA	11%	3%	7%	-	-
Corporate Bonds	A	9%	7%	-	-	-
Corporate Bonds	BBB	-	10%	-	1%	-
Corporate Bonds	BB	-	-	-	17%	-
Corporate Bonds	B	-	-	-	43%	-
Corporate Bonds	CCC	-	-	-	8%	-
Convertible Bonds	B	-	-	-	1%	-
Yankees:						
Government	BBB	-	1%	-	-	-
Corporate	A	1%	-	-	-	-
Corporate	BB	-	-	-	1%	-
Corporate	B	-	-	-	1%	-
No credit exposure		12%	16%	1%	1%	99%
		<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>

¹Rating modifiers are not disclosed.

Securities lending collateral was invested in a registered 2(a)-7 money market fund that was not rated.

Public Employees' Retirement System

Invested Assets

Notes to Schedules

June 30, 2005 and 2004

(4) DEPOSIT AND INVESTMENT RISK (Cont.)

Custodial Credit Risk – Deposits

Custodial credit risk is the risk that deposits may not be returned in the event of a bank failure. The Board does not have a policy in relation to custodial credit risk for deposits. At June 30, 2005, PERS Invested Assets had the following uncollateralized and uninsured deposits:

	<u>Amount</u> <u>(in thousands)</u>
International Fixed Income Pool	\$ 6,587
International Equity Pool	2,984
	<u>\$ 9,571</u>

Foreign Currency Risk

Foreign Currency Risk is the risk that changes in exchange rates will adversely impact the fair value of an investment.

The Board's policy with regard to foreign currency risk in the International Fixed Income Pool is to restrict obligations to those issued in the currencies of countries represented in the Citibank Non-U.S. World Government Bond Index. In addition, the Board's asset allocation policy permits PERS to hold up to four percent of total investments in international fixed income.

The Board's policy with regard to foreign currency risk in the International Equity Pool and the Emerging Markets Pool is to permit PERS to hold up to eighteen percent of total investments in these two pools combined.

The Board's policy with regard to foreign currency risk in the Private Equity Pool is to permit PERS to hold up to ten percent of total investments in private equity.

At June 30, 2005, PERS had exposure to foreign currency risk with the following deposits:

<u>Currency</u>	<u>Amount (in thousands)</u>	
	<u>International Fixed</u> <u>Income Pool</u>	<u>International</u> <u>Equity Pool</u>
Australian Dollar	\$ 68	\$ 24
Canadian Dollar	-	21
Danish Krone	-	126
Euro Currency	-	446
Hong Kong Dollar	-	171
Japanese Yen	6,519	1,181
New Zealand Dollar	-	2
Norwegian Krone	-	249
Pound Sterling	-	232
Singapore Dollar	-	3
South Korean Won	-	1
Swiss Franc	-	4
	<u>\$ 6,587</u>	<u>\$ 2,460</u>

Public Employees' Retirement System Invested Assets

Notes to Schedules June 30, 2005 and 2004

(4) DEPOSIT AND INVESTMENT RISK (Cont.)

Foreign Currency Risk (Cont.)

At June 30, 2005, PERS had exposure to foreign currency risk with the following investments:

Currency	Amount (in thousands)				
	International Fixed Income Pool		International Equity Pool		Private Equity Pool
	Foreign Government	Corporate	Convertible Bonds	Equity	Limited Partnerships
Australian Dollar	\$ -	\$ -	\$ -	\$ 21,988	\$ -
Canadian Dollar	-	-	-	20,501	-
Danish Krone	-	-	-	2,859	-
Euro Currency	-	5,954	-	492,397	39,194
Hong Kong Dollar	-	-	-	13,425	-
Japanese Yen	27,956	93,201	-	266,857	-
New Zealand Dollar	-	-	-	4,947	-
Norwegian Krone	-	-	-	12,624	-
Polish Zloty	16,977	-	-	-	-
Pound Sterling	-	-	-	260,786	843
Singapore Dollar	-	-	-	18,458	-
South African Rand	-	-	-	4,696	-
South Korean Won	-	-	-	9,770	-
Swedish Krona	168,044	-	-	11,532	-
Swiss Franc	-	-	313	108,431	-
	<u>\$ 212,977</u>	<u>\$ 99,155</u>	<u>\$ 313</u>	<u>\$ 1,249,270</u>	<u>\$ 40,037</u>

At June 30, 2005, PERS also had exposure to foreign currency risk in the Emerging Markets Equity Pool. This pool represents an investment in commingled investment funds; therefore no disclosure of specific currencies is made.

Concentration of Credit Risk

Treasury's policy with regard to concentration of credit risk for the Short-term Fixed Income Pool is to prohibit the purchase of more than five percent of the portfolio's assets in corporate bonds of any one company or affiliated group.

The Board's policy with regard to concentration of credit risk for the Domestic Fixed Income, International Fixed Income and High Yield Pools is to prohibit the purchase of more than five percent of the portfolio's assets in corporate bonds of any one company or affiliated group.

At June 30, 2005, PERS invested assets included \$589.6 million in Federal National Mortgage Association securities which represented 6% of total PERS invested assets.

Public Employees' Retirement System

Invested Assets

Notes to Schedules

June 30, 2005 and 2004

(5) **FOREIGN EXCHANGE, FOREIGN EXCHANGE CONTRACTS AND OFF-BALANCE SHEET RISK**

The International Fixed Income and International Equity Pool's investment income includes the following at June 30:

	<u>2005</u>	<u>2004</u>
Realized Gain on Foreign Currency	\$ 122,903,509	\$ 87,803,704
Unrealized Gain (Loss) on Foreign Currency	(26,827)	19,401
Realized Gain (Loss) on Foreign Exchange Contracts	(217,279)	82,142

The International Equity Pool includes foreign currency forward contracts to buy and sell specified amounts of foreign currencies at specified rates on specified future dates for the purpose of hedging existing security positions. The maturity periods for these contracts range from eight to one hundred and twenty-four days. PERS had net unrealized gains (losses) with respect to such contracts, calculated using forward rates at June 30, as follows:

	<u>2005</u>	<u>2004</u>
Net Contract Sales	\$ 6,587,214	\$ 4,980,969
Less: Fair Value	<u>6,302,248</u>	<u>5,312,169</u>
Net unrealized gains (losses)	<u>\$ 284,966</u>	<u>\$ (331,200)</u>

The counterparties to the foreign currency forward contracts consist of a diversified group of financial institutions. Credit risk exposure exists to the extent of non-performance by these counterparties; however, the risk of default is considered to be remote. The market risk is limited to the difference between contractual rates and forward rates at the balance sheet date.

(6) **COMMITMENTS AND CONTINGENCIES**

The Board entered into an agreement through an external investment manager to provide capital funding for a domestic equity limited partnership. At June 30, 2005, PERS Invested Asset's share of the unfunded commitment totaled \$104,826,035. This commitment can be withdrawn annually in December with ninety days notice.

The Board entered into agreements through external investment managers to provide capital funding for limited partnerships as it continues to build the private equity portfolio. At June 30, 2005, PERS Invested Asset's share of these unfunded commitments totaled \$482,295,527. Ninety-four percent of this commitment is estimated to be paid through the year 2010. Six percent of this commitment can be withdrawn annually in December with ninety days notice.

The Board entered into an agreement through an external investment manager to provide capital funding for a limited partnership as it continues to build the other investment portfolio. At June 30, 2005, PERS Invested Asset's share of this unfunded commitment totaled \$39,800,301 to be paid through the year 2007.

The Board entered into agreements through external investment managers to provide capital funding for real estate investments as it continues to build the real estate portfolio. At June 30, 2005, PERS Invested Asset's share of these unfunded commitments totaled \$235,140,626 to be paid through the year 2010.

Public Employees' Retirement System

Invested Assets

Notes to Schedules

June 30, 2005 and 2004

(7) SECURITIES LENDING

Alaska Statute 37.10.071 authorizes the Board to lend assets, under an agreement and for a fee, against deposited collateral of equivalent fair value. The Board has entered into an agreement with State Street Corporation (the Bank) to lend equity and domestic fixed income securities. The Bank, acting as the Board's agent under the agreement, transfers securities to broker agents or other entities for collateral in the form of cash or securities and simultaneously agrees to return the collateral for the same securities in the future.

At June 30, 2005 and 2004, the fair value of securities on loan allocable to PERS Invested Assets totaled \$642,524,010 and \$960,292,029, respectively. There is no limit to the amount that can be loaned and the Board is able to sell securities on loan. International equity security loans are collateralized at not less than 105 percent of their fair value. All other security loans are collateralized at not less than 102 percent of their fair value. Loaned securities and collateral is marked to market daily and collateral is received or delivered the following day to maintain collateral levels.

Cash collateral is invested in a registered 2(a)-7 money market fund, which is valued at amortized cost. Maturities of investments in the money market fund generally did not match the maturities of the loaned securities because the lending agreements are terminable at will. Collateral securities may be pledged or sold upon borrower default. Since the Board does not have the ability to pledge or sell collateral securities unless the borrower defaults, they are not recorded on the financial schedules. Securities on loan, cash collateral and cash collateral payable are recorded on the financial schedules. The bank, PERS and the borrower receive a fee from earnings on invested collateral. The bank and PERS share a fee paid by the borrower for loans not collateralized with cash.

There is limited credit risk associated with the lending transactions since the Board is indemnified by the Bank against any loss resulting from counterparty failure or default on a loaned security or its related income distributions. The Bank further indemnifies the Board against loss due to borrower rebates in excess of earnings on cash collateral. Indemnifications are subject to limitation relating to war, civil unrest or revolution, or beyond the reasonable control of the Bank.

For the year ended June 30, 2005 and 2004, there were no losses incurred as a result of securities lending transactions and there were no significant violations of legal or contractual provisions nor failures by any borrowers to return loaned securities.