



ALASKA RETIREMENT MANAGEMENT BOARD

Military Retirement System

Invested Assets

June 30, 2009

(With Independent Auditors' Report Thereon)

ALASKA RETIREMENT MANAGEMENT BOARD

Military Retirement System

Invested Assets

June 30, 2009

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Independent Auditors' Report

Alaska Retirement Management Board and
State of Alaska, Department of Revenue
Division of Treasury:

We have audited the accompanying schedules of invested assets of the Military Retirement System as of June 30, 2009 and of investment income (loss) and changes in invested assets of the Military Retirement System for the year 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 audit.

We conducted our audit 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 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 audit provides a reasonable basis for our opinion.

The accompanying Schedules were prepared to present the invested assets of the Military Retirement System, which is established under the State of Alaska National Guard and Naval Militia Retirement System (NG & NMRS). The Schedules are not intended to present the financial status of NG & NMRS.

In our opinion, the Schedules referred to above present fairly, in all material respects, the invested assets of the Military Retirement System as of June 30, 2009 and the investment income (loss) and changes in invested assets for the year then ended in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

October 9, 2009

ALASKA RETIREMENT MANAGEMENT BOARD

MILITARY RETIREMENT SYSTEM

SCHEDULE OF INVESTED ASSETS

July 30, 2009

Investments (at Fair Value)

Cash and Cash Equivalents	
Short-term Fixed Income Pool	\$ <u>2,152</u>
Total Cash and Cash Equivalents	<u>2,152</u>
Marketable Debt Securities	
Alaska Retirement Fixed Income Pool	<u>13,954,357</u>
Equity Securities	
Domestic Equity Pool	8,433,391
International Equity Pool	<u>3,117,222</u>
Total Equity Securities	<u>11,550,613</u>
Total Invested Assets	<u><u>25,507,122</u></u>

ALASKA RETIREMENT MANAGEMENT BOARD

MILITARY RETIREMENT SYSTEM

**SCHEDULE OF INVESTMENT INCOME (LOSS)
AND CHANGES IN INVESTED ASSETS**

Year ended June 30, 2009

Investment Income (Loss)

Short-term Fixed Income Pool	\$	4,017
Alaska Retirement Fixed Income Pool		417,952
Domestic Equity Pool		(2,169,616)
International Equity Pool		<u>(773,604)</u>
Total Investment Income (Loss)		(2,521,251)
Total Invested Assets, Beginning of Year		27,261,582
Contributions		2,473,300
Withdrawals		<u>(1,706,509)</u>
Net Contributions		<u>766,791</u>
Total Invested Assets, End of Year	\$	<u><u>25,507,122</u></u>

Military Retirement System

Invested Assets

Notes to Schedules
June 30, 2009

(1) THE ACCOUNTING ENTITY

The Military Retirement System Invested Assets (MRS Invested Assets) is the investment portfolio of the State of Alaska National Guard and Naval Militia Retirement System (NG & NMRS). NG & NMRS is a single-employer defined benefit system established for the payment of retirement, disability and death benefits to, or on behalf of, qualified members of the Alaska National Guard, Alaska Naval Militia and Alaska Air Guard. These Schedules are those of MRS Invested Assets and not NG & NMRS taken as a whole. Fiduciary responsibility for MRS Invested Assets resides with the Alaska Retirement Management Board (Board), pursuant to Alaska Statutes 37.10.210-390.

Alaska Statute 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 MRS 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 Domestic Equity Pool and the International Equity Pool are managed by external management companies. Treasury manages the Alaska Retirement Fixed Income Pool, and cash holdings of certain external domestic equity 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 that holds investments on behalf of MRS and other pension and state funds.

(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. Investment purchases and sales are recorded on a trade-date basis. Net contributions represent contributions from employers and employees, net of benefits paid to NG & NMRS participants as well as administrative and investment management expenses. Contributions, benefits paid and all expenses are recorded on a cash basis.

Valuation

Fixed income 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 most current sale price or based on a valuation provided by investment managers.

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 on the last business day of each month by the investment managers.

Income Allocation

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

Military Retirement System

Invested Assets

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June 30, 2009

(3) INVESTMENTS

Short-term Fixed Income Pool

MRS 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, 2009 MRS Invested Assets included a 0.0006% direct ownership in the Short-term Fixed Income Pool which included interest receivable of \$51. MRS Invested Assets included a 0.02% indirect ownership through ownership by other investment pools which invest in the Short-term Fixed Income Pool at June 30, 2009.

Alaska Retirement Fixed Income Pool

MRS Invested Assets include participation in the Board's internally managed Alaska Retirement Fixed Income Pool which was established March 1, 1996, with a startup share price of \$1,000. The share price at June 30, 2009 was \$2,163. 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, 2009 MRS Invested Assets included a 0.96% ownership in the Alaska Retirement Fixed Income Pool.

Domestic Equity Pool

The Domestic Equity Pool is comprised of an External Large Cap Domestic Equity Pool and an External Small Cap Domestic Equity Pool.

Large Cap Domestic Equity Pool

MRS 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, 2009, was \$870. 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, 2009 MRS Invested Assets included a 0.24% ownership in the Large Cap Domestic Equity Pool.

Small Cap Domestic Equity Pool

MRS 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, 2009, was \$844. 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, 2009 MRS Invested Assets included a 0.06% ownership in the Small Cap Domestic Equity Pool.

Military Retirement System

Invested Assets

Notes to Schedules

June 30, 2009

(3) INVESTMENTS (Cont.)

International Equity Pool

MRS 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, 2009, was \$2,703. 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, 2009 MRS Invested Assets included a 0.16% ownership in the International Equity Pool.

(4) DEPOSIT AND INVESTMENT RISK

At June 30, 2009, MRS Invested Assets included the following:

	Fair Value (in thousands)			
	Fixed Income Pools		Other	Total
	Short-term	Retirement		
Deposits	\$ 2	\$ (1)	\$ 19	\$ 20
Short-term Investment Fund	-	-	41	41
Commercial Paper	46	-	-	46
U. S. Treasury Bills	260	-	-	260
U. S. Treasury Notes	-	2,348	-	2,348
U. S. Treasury Bonds	-	198	-	198
U.S. Government Agency	20	281	-	301
Mortgage-backed	29	7,093	-	7,122
Other Asset-backed	91	100	-	191
Corporate Bonds	247	2,782	-	3,029
Yankees:				
Government	-	162	-	162
Corporate	53	629	-	682
Domestic Equity Pool:				
Limited Partnership	-	-	507	507
Treasury Bills	-	-	6	6
Equity	-	-	7,842	7,842
International Equity Pool:				
Convertible Bonds	-	-	2	2
Equity	-	-	2,998	2,998
Mutual Funds	-	-	52	52
Net Other Assets (Liabilities)	(2)	(304)	6	(300)
Other Pool Ownership	(744)	666	78	-
Total Invested Assets	<u>\$ 2</u>	<u>\$ 13,954</u>	<u>\$ 11,551</u>	<u>\$ 25,507</u>

Military Retirement System

Invested Assets

Notes to Schedules
June 30, 2009

(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, 2009, the expected average life of fixed income securities ranged from eight days to less than three months.

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.

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 Retirement 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, 2009, was 4.68 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 Enhanced Cash Income portfolio to one year.

At June 30, 2009, the effective duration of the defined benefit fixed income pools, by investment type, was as follows:

	Effective Duration (in years)
	Retirement Fixed Income Pool
Corporate Bonds	4.96
Mortgage-Backed	3.50
Other Asset-Backed	1.72
U.S. Treasury Bonds	14.18
U.S. Treasury Notes	4.95
US. Government and Agency Securities	5.48
Yankees:	
Corporate	4.48
Government	10.52
Portfolio Effective Duration	4.16

Military Retirement System

Invested Assets

Notes to Schedules
June 30, 2009

(4) DEPOSIT AND INVESTMENT RISK (Cont.)

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:

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 P1 or equivalent. Asset-backed and non-agency mortgage securities must be rated A3 or equivalent. The A3 rating is defined as the median rating of the following three rating agencies: 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.

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

Retirement Fixed Income:

Commercial paper must carry a rating of at least P-1 by Moody's and A-1 by Standard and Poor's.

Corporate debt securities must be investment grade.

Corporate, asset-backed and non-agency mortgage securities must be investment grade. Investment grade is defined as the median rating of Standard & Poor's, 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.

No more than 40% of the portfolio's assets may be invested in investment grade corporate debt.

No more than 15% of the portfolio's assets may be invested in BBB+ to BBB- rated debt by Standard and Poor's Corporation or the equivalent by Moody's or Fitch.

Domestic and International Equity:

Corporate debt obligations must carry a rating of at least A or better by Moody's, Standard & Poor's or Fitch rating services.

Commercial paper must bear the highest rating assigned by Moody's, Standard & Poor's, or Fitch rating services.

Military Retirement System

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June 30, 2009

(4) DEPOSIT AND INVESTMENT RISK (Cont.)

Credit Risk (Cont.)

At June 30, 2009, MRS 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):

	Fixed Income Pools			
	Rating	Short-term		Retirement
Commercial Paper	A-1	1.10	%	-
Commercial Paper	Not Rated	5.05		-
U. S. Treasury Notes	AAA	-		16.82
U. S. Treasury Bills	AAA	34.70		-
U. S. Treasury Bonds	AAA	-		1.42
U.S. Government Agency	AAA	2.69		1.84
U.S. Government Agency	Not Rated	-		0.17
Mortgage-backed	AAA	3.46		44.60
Mortgage-backed	A	0.11		-
Mortgage-backed	BBB	0.18		-
Mortgage-backed	Not Rated	0.30		6.22
Other Asset-backed	AAA	10.87		0.47
Other Asset-backed	AA	0.85		0.13
Other Asset-backed	A	0.35		0.03
Other Asset-backed	BBB	-		0.08
Corporate Bonds	AAA	19.33		1.18
Corporate Bonds	AA	6.16		2.48
Corporate Bonds	A	7.64		9.15
Corporate Bonds	BBB	-		6.25
Corporate Bonds	BB	-		0.02
Corporate Bonds	Not Rated	-		0.86
Yankees:				
Government	AAA	-		0.46
Government	BBB	-		0.24
Government	Not Rated	-		0.46
Corporate	AAA	1.61		0.76
Corporate	AA	4.29		0.43
Corporate	A	1.24		2.13
Corporate	BBB	-		1.09
Corporate	Not Rated	-		0.10
No Credit Exposure		0.07		2.61
		<u>100.00</u>	%	<u>100.00</u>
				%

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June 30, 2009

(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, 2009, MRS Invested Assets had the following uncollateralized and uninsured deposits:

	<u>Amount</u>
International Equity Pool	\$ <u>12,993</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 Equity Pool is to permit MRS to hold up to fifteen percent of total investments in international equity.

At June 30, 2009, MRS investment in the International Equity Pool had exposure to foreign currency risk with the following deposits:

<u>Currency</u>	<u>International Equity Pool</u>
Australian Dollar	\$ 100
Canadian Dollar	60
Danish Krone	1,541
Euro	6,621
Hong Kong Dollar	175
Japanese Yen	3,652
New Taiwan Dollar	69
New Zealand Dollar	38
Norwegian Krone	114
Pound Sterling	596
Singapore Dollar	1
Swedish Krona	18
Swiss Franc	1
Yuan Renminbi	7
	\$ <u>12,993</u>

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June 30, 2009

(4) DEPOSIT AND INVESTMENT RISK (Cont.)

Foreign Currency Risk (cont.)

At June 30, 2009, MRS investment in the International Equity Pool had exposure to foreign currency risk with the following investments:

<u>Currency</u>	<u>Amount</u>
	<u>Equity</u>
Australian Dollar	\$ 47,692
Brazilian Real	19,057
Canadian Dollar	50,756
Danish Krone	22,400
Euro	1,009,059
Hong Kong Dollar	108,018
Indonesian Rupah	1,671
Japanese Yen	719,727
Mexican Peso	1,671
New Taiwan Dollar	17,837
New Zeland Dollar	3,504
Norwegian Krone	7,341
Pound Sterling	518,458
Singapore Dollar	21,639
South African Rand	6,259
South Korean Won	9,963
Swedish Krona	40,465
Swiss Franc	219,615
	<u>\$ 2,825,132</u>

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. This provision does not apply to securities backed by the full faith and credit of the United States Government.

The Board's policy with regard to concentration of credit risk for the Retirement 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.

At June 30, 2009, MRS invested assets included \$4 million in Federal National Mortgage Association securities, which represented 16% of total MRS invested assets. Federal National Mortgage Association securities are not classified as corporate bonds.

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June 30, 2009

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

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

Net Realized (Loss) on Foreign currency	\$	(55,056)
Net Unrealized Gain on Foreign currency		62
Net Realized Gain on Foreign Exchange Contracts		867

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. At June 30, the International Equity Pool had one foreign currency forward which matured in 22 days. JMRS had net unrealized loss with respect this contract, calculated using forward rates at June 30, as follows:

Contract Purchases	\$	45,562
Less: Fair Value		<u>45,211</u>
Net Unrealized Loss on Contracts	\$	<u>(351)</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, 2009, MRS Invested Asset's share of the unfunded commitment totaled \$111,611. This commitment can be withdrawn annually in December with ninety days notice.