

New York City  
Police Department  
Police Officers' Variable  
Supplements Fund

Financial Statements as of and for the  
Years Ended June 30, 2012 and 2011, and  
Independent Auditors' Report

**NEW YORK CITY POLICE DEPARTMENT  
POLICE OFFICERS'  
VARIABLE SUPPLEMENTS FUND**

**TABLE OF CONTENTS**

---

	<b>Page</b>
INDEPENDENT AUDITORS' REPORT	1
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)	2-7
FINANCIAL STATEMENTS FOR THE YEARS ENDED JUNE 30, 2012 AND 2011:	
Statements of Plan Net Assets	8
Statements of Changes in Plan Net Assets	9
Notes to Financial Statements	10-23

## INDEPENDENT AUDITORS' REPORT

To the Board of Trustees of the  
New York City Police Department Police Officers'  
Variable Supplements Fund

We have audited the accompanying statements of plan net assets of New York City Police Department Police Officers' Variable Supplements Fund (the "Plan") as of June 30, 2012 and 2011, and the related statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of the Plan's management. 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements 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 Plan's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 net assets of the Plan as of June 30, 2012 and 2011, and the changes in plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 2 through 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

*Deloitte & Touche LLP*

October 26, 2012

# NEW YORK CITY POLICE DEPARTMENT POLICE OFFICERS' VARIABLE SUPPLEMENTS FUND

## MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) JUNE 30, 2012 AND 2011

---

The narrative discussion and analysis of the financial activities of the New York City Police Officers' Variable Supplements Fund (POVSF, the "Fund" or the "Plan") for the fiscal years ended June 30, 2012 and 2011 is presented by management as an introduction to the basic financial statements. It is meant to assist the reader in understanding the Fund's financial statements by providing an overall review of financial activities during the year and the effects of significant changes, as well as a comparison with the prior year's activities and results.

### OVERVIEW OF BASIC FINANCIAL STATEMENTS

The following discussion and analysis is intended to serve as an introduction to the Plan's basic financial statements. The basic financial statements are:

- **The Statement of Plan Net Assets** — presents the financial position of the Plan at fiscal year-end. It indicates the assets available for payment of future benefits and any current liabilities that are owed as of the statement date. Investments are shown at fair value. All other assets and liabilities are determined on an accrual basis.
- **The Statement of Changes in Plan Net Assets** — presents the result of activities during the year. All changes affecting the assets and the liabilities of the Plan are reflected on an accrual basis when the activity occurred, regardless of the timing of the related cash flow. In that regard, changes in the fair values of investments are included in the year's activity as net appreciation (depreciation) in fair value of investments.
- **The Notes to Financial Statements** — provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes present information about the Plan's accounting policies, significant account balances and activities, material risks, obligations, contingencies, and subsequent events, if any.

The financial statements are prepared in accordance with Governmental Accounting Standards Board Pronouncements (GASB).

### FINANCIAL HIGHLIGHTS

- The Fund's total assets exceeded its liabilities by \$475.2 million and \$611.1 million as of June 30, 2012 and 2011, respectively.
- In fiscal year 2012, the Fund's Net Assets Held in Trust for Benefits decreased by \$135.8 million or 22.2% compared to fiscal year 2011 and increased by \$9.7 million or 1.6% compared to fiscal year 2010. Plan Net Assets Held in Trust for Benefits decreased in fiscal year 2012 due to the decrease in fair value of investments.

- Benefit payments totaled \$142.8 million for fiscal year 2012 compared to \$136.5 million for fiscal year 2011. This reflects an increase of 5%, which is primarily due to the increase in the number of the retirees. Benefit Payments in the amount of \$136.5 million paid in fiscal year 2011 represented an increase of 8% from year 2010.

## PLAN NET ASSETS

The Statements of Plan Net Assets for fiscal years 2012 and 2011 showed total assets exceeded total liabilities by \$475.2 million and \$611.1 million, respectively. This represents total Fund Net Assets Held in Trust for Benefits. This amount is available to cover the Fund's obligation to pay benefits to the Fund's members.

This year the Fund's Net Assets Held in Trust for Benefits decreased by \$135.8 million or 22.2% compared to fiscal year 2011. Last year, the Fund increased by \$9.7 million or 1.6% compared to fiscal year 2010.

The Fund's 2012 outstanding liabilities of \$164 million decreased by 8% compared to fiscal year 2011. The Fund's 2011 outstanding liabilities of \$177 million increased by 1% compared to fiscal year 2010. Total liabilities consist of outstanding securities lending transactions of 25% and 37%, accrued benefits payable 42% and 39% and payable for investment securities purchased of 32% and 24% for fiscal years 2012 and 2011, respectively.

The Fund Investment Portfolio decreased by 20.5% during fiscal year 2012 due to a downturn in the economy, and increased by 3.5% during fiscal year 2011 due to a positive net income from investment.

### Plan Net Assets June 30, 2012, 2011, and 2010 (in thousands)

	2012	2011	2010
Cash	\$ 295	\$ 6	\$ 4,095
Receivables	31,258	9,601	20,135
Investments, at fair value	566,050	712,343	688,946
Collateral from Securities Lending Transactions	<u>41,372</u>	<u>66,363</u>	<u>63,161</u>
Total Assets	<u>638,975</u>	<u>788,313</u>	<u>776,337</u>
Accounts Payable and Other Liabilities	122,367	110,890	111,821
Payables for Securities Lending Transactions	<u>41,372</u>	<u>66,363</u>	<u>63,161</u>
Total Liabilities	<u>163,739</u>	<u>177,253</u>	<u>174,982</u>
Plan Net Assets Held in Trust for Benefits	<u>\$ 475,236</u>	<u>\$ 611,060</u>	<u>\$ 601,355</u>

The Plan's receivables and payables related to Investment Securities are primarily generated through the timing of the difference between the trade and settlement dates for investment securities purchased or sold.

**Investment Summary**

**Fair Value**

(in thousands)

	2012	2011	2010
Short-term Investments/Discount Notes	\$ 44,270	\$ 19,253	\$ 24,718
Debt Securities	133,599	218,070	207,684
Equity Securities	307,050	349,172	296,110
Mutual Fund: International Equity	81,131	115,449	146,334
Mutual Fund: Treasury Inflation-Protected Securities	-	10,399	14,100
Collateral from Securities Lending Transactions	<u>41,372</u>	<u>66,363</u>	<u>63,161</u>
 Total Investments	 <u>\$ 607,422</u>	 <u>\$ 778,706</u>	 <u>\$ 752,107</u>

**CHANGES IN PLAN NET ASSETS**

**Additions** — The overall activities of the Fund shown in the Statements of Changes in Plan Net Assets are reflected in the difference between total additions and total deductions resulting in a net decrease of \$135.8 million for the fiscal year 2012 and increase of \$9.7 million for the fiscal year 2011. The following items represent the components of this difference: net investment income \$7.0 million and benefit payments of \$142.8 million for 2012, and net investment income \$146.2 million and benefit payments of \$136.5 million for 2011.

**Deductions** — All administrative and investment expenses are paid by The City of New York and not charged to the Fund. For fiscal year 2012 deductions totaled \$142.8 million and \$136.5 million was paid in fiscal year 2011. This shows an increase of \$6.3 million or 5% this year compared to the prior fiscal year and an increase of \$10.3 million or 8% in 2011 compared to 2010. In addition, benefit payments increased substantially this year primarily as a result of an increase in the number of retirees paid.

**Changes in Plan Net Assets**  
**Years Ended June 30, 2012, 2011, and 2010**  
(in thousands)

	2012	2011	2010
ADDITIONS:			
Investment income (loss):			
Interest income	\$ 5,771	\$ 9,552	\$ 10,968
Dividend income	9,284	9,907	10,031
Net appreciation (depreciation) in fair value of investments	<u>(8,446)</u>	<u>126,209</u>	<u>77,632</u>
Total investment income (loss)	6,609	145,668	98,631
Less investment (income)/expense	<u>11</u>	<u>(147)</u>	<u>4</u>
Net income (loss)	<u>6,598</u>	<u>145,815</u>	<u>98,627</u>
Securities lending transactions:			
Securities lending income	409	475	603
Securities lending fees	<u>(27)</u>	<u>(58)</u>	<u>(92)</u>
Net securities lending income	<u>382</u>	<u>417</u>	<u>511</u>
Net investment income (loss)	<u>6,980</u>	<u>146,232</u>	<u>99,138</u>
DEDUCTIONS — Benefits payments (Note 1)	<u>142,804</u>	<u>136,527</u>	<u>126,202</u>
NET INCREASE (DECREASE) IN PLAN NET ASSETS	(135,824)	9,705	(27,064)
PLAN NET ASSETS HELD IN TRUST FOR BENEFITS:			
BEGINNING OF YEAR	<u>611,060</u>	<u>601,355</u>	<u>628,419</u>
END OF YEAR	<u>\$ 475,236</u>	<u>\$ 611,060</u>	<u>\$ 601,355</u>

**FUNDING AND PLAN BENEFITS**

The New York City Police Pension Fund (POLICE) is the source of funding for the Fund.

For Fiscal Years 2012, 2011 and 2010 there were no transfers from POLICE to the Fund.

Plan benefits are paid once a year, in December, according to a schedule which, in general, increases annually by \$500 up to a maximum of \$12,000. Tier A members, those hired before July 1, 1988, and Tier B members, those hired after June 30, 1988, are under different schedules. Tier A eligible Police Officer retirees began receiving the maximum scheduled benefit of \$12,000 in December 2007. Tier B eligible Police Officer retirees began receiving the maximum \$12,000 benefit in December 2008.

All data pertaining to benefits and other information concerning the Fund is discussed in detail in the notes to the financial statements.

The Administrative Code of The City of New York (ACNY) provides that POLICE transfer to the Fund an amount equal to certain excess earnings on equity investments, limited to the unfunded Accumulated Benefit Obligation (ABO) of the Fund. Excess earnings are defined as the amount by which earnings on equity investments of POLICE exceed what those earnings would have been had such Funds been invested at a yield comparable to that available from Fixed-Income Securities (Hypothetical Fixed Income Security Earnings) less any cumulative deficiencies. The Fund also receives credit for investment earnings on Fund assets.

The calculation of the Hypothetical Fixed Income Security Earnings requires the determination of the Hypothetical Interest Rate (HIR), which is computed by the Comptroller (Note 4).

Effective Fiscal Year 2000, the Actuary recommended revision to the calculation of the HIR. This change in methodology would make HIR for POLICE consistent with Chapter 255 of the Laws of 2000 (Chapter 255/00) that modified the methodology for the HIR used for developing the Transferable Earnings Payable from the New York City Employees' Retirement System (NYCERS) to certain Variable Supplements Funds.

Specifically, in recognition that 30-year U.S. Treasury Securities may become less plentiful in the future and subject to market distortion, the Actuary proposed to determine the HIR for Fiscal Year 2000 and later by taking an average of the monthly yields of 10-year U.S. Treasury Notes as published in Federal Reserve Statistical Bulletin H.15 and increasing it by 15%.

At its March 14, 2001 meeting, the Board of Trustees of POLICE adopted this revised methodology for use in connection with the calculation of the HIR for Fiscal Year 2000 and later.

## **INVESTMENTS**

The Board of Trustees of the Fund, in accordance with existing laws, has the authority to determine the manner in which the assets of the Funds are invested. Investments are made by the New York City Comptroller, who acts as custodian of the assets. The primary object of the Fund is to provide benefits for its members and provide for growth in membership and also be prepared for inflation. Investments are made with the objective of minimizing risks and maintaining a high competitive return. Diversification has increased investment results and provided security for the assets of the retirement system. The Comptroller of The City of New York utilizes several investment advisors to manage long-term debt and equity portfolios. Advisors must obtain prior approval before each purchase or sale of a particular security. Investments are valued at fair value. Purchase and sales of Securities are reflected on the trade date. No investment in any one security represents 5% or more of Plan Net Assets Held in Trust for Benefits.

The Fund is expected to earn a higher long-term rate of return than short-term cash accounts, due to the long-term nature of its liabilities and the diversification of its investment holdings. For the five-year period ended June 30, 2012, the Fund had an annualized return of 2.24%. Investments in assets that are expected to produce higher returns are also subject to greater volatility and may also produce negative returns. Fiscal year 2012 has been a fairly good year for investors. Investments in stock markets within and outside the United States have slightly gained value. For example, the Russell 3000 index, a broad measure of the U.S. stock market, gain 3.84% during this period, and the Europe, Australia and Far East ("EAFE") Index, the most commonly used measure of performance in developed international markets, loss 13.83%. The returns of the Fund have been consistent with these broad market trends and as a result, the asset allocation followed by the Fund produced a combined return of a gain of 2.11%. For the three-year period ended June 30, 2012 the combined return was a gain of 12.67%, and for the five-year period it was a gain of 2.24%.

Cash temporarily idle during the year is subject to conservative investment restrictions, and was invested in obligations of the U.S. Treasury and U.S. agency securities, commercial paper, medium term notes, and repurchase agreements. The average maturity of the investments is 83 days. The Fund earned an average yield of 0.60% which compares with the average yield of 0.088% on three-month Treasury Bills and 0.32% for a representative institutional money market Fund.

Assets are invested long-term for the benefit of the Fund's participants and their beneficiaries. All investments are managed by registered investments advisors, pursuant to applicable laws and to guidelines issued by the Comptroller. Collectively the investments utilize one domestic equity manager, three domestic fixed-income managers, three international equity managers and one emerging markets manager. Assets are allocated in accordance with plan policy adopted periodically by the Fund's Board of Trustees. The percentage in each category is determined based on a study indicating the probable rates of return and levels of risk for various assets' allocations. The actual allocation may vary from this policy mix as market values shift and as investments are added or terminated.

**Security Lending Transactions** — The Board of Trustees permits the Fund to lend its securities to brokers, dealers and others with an agreement to return the collateral for the same securities in the future. In return, it receives collateral in the form of cash, treasury and US Government Securities at 100% to 105% of the principal, plus accrued interest for reinvestment.

**Contact Information** — This financial report is designed to provide our members and their beneficiaries and others with a general overview of the Fund's finances and show accountability for money it receives. Questions concerning any data provided in this report or request for additional information should be directed to the Chief Accountant, New York City Police Officers' Variable Supplements Fund, 233 Broadway 25<sup>th</sup> Floor, New York, NY 10279.

\* \* \* \* \*

**NEW YORK CITY POLICE DEPARTMENT  
POLICE OFFICERS'  
VARIABLE SUPPLEMENTS FUND**

**STATEMENTS OF PLAN NET ASSETS  
JUNE 30, 2012 AND 2011**

	<b>2012</b>	<b>2011</b>
<b>ASSETS:</b>		
Cash	\$ 295,471	\$ 5,713
Receivables:		
Receivables from investment securities sold	29,978,877	7,467,967
Accrued interest and dividends receivable	<u>1,278,631</u>	<u>2,133,515</u>
Total receivables	<u>31,257,508</u>	<u>9,601,482</u>
Investments — at fair value (Notes 2 and 3):		
Securities purchased under agreements to resell	27,505,218	-
Short-term investments	15,064,561	18,551,974
Discount notes	1,699,765	699,952
Debt securities:		
U.S. government	91,477,605	132,443,130
Corporate	41,456,757	84,992,300
Foreign	664,492	634,705
Equity securities	307,050,513	349,172,371
Mutual fund:		
International equity	81,130,842	115,449,000
Treasury inflation-protected securities	-	10,399,379
Collateral from securities lending transactions (Note 2)	<u>41,372,276</u>	<u>66,363,163</u>
Total investments	<u>607,422,029</u>	<u>778,705,974</u>
Total assets	<u>638,975,008</u>	<u>788,313,169</u>
<b>LIABILITIES:</b>		
Accounts payable	8,156	848
Payable for investment securities purchased	52,806,760	43,179,159
Accrued benefits payable (Note 2)	69,552,277	67,709,924
Securities lending transactions (Note 2)	<u>41,372,276</u>	<u>66,363,163</u>
Total liabilities	<u>163,739,469</u>	<u>177,253,094</u>
<b>PLAN NET ASSETS HELD IN TRUST FOR BENEFITS</b>	<u>\$475,235,539</u>	<u>\$611,060,075</u>

See notes to financial statements.

**NEW YORK CITY POLICE DEPARTMENT  
POLICE OFFICERS'  
VARIABLE SUPPLEMENTS FUND**

**STATEMENTS OF CHANGES IN PLAN NET ASSETS  
YEARS ENDED JUNE 30, 2012 AND 2011**

	<b>2012</b>	<b>2011</b>
ADDITIONS:		
Investment income (Note 2):		
Interest income	\$ 5,770,788	\$ 9,552,020
Dividend income	9,284,215	9,907,045
Net appreciation in fair value of investments	<u>(8,446,168)</u>	<u>126,208,164</u>
Total investment income	6,608,835	145,667,229
Less investment (income)/expense	<u>11,195</u>	<u>(147,402)</u>
Net income	<u>6,597,640</u>	<u>145,814,631</u>
Securities lending transactions:		
Securities lending income	409,892	474,681
Securities lending fees	<u>(27,454)</u>	<u>(57,611)</u>
Net securities lending income	<u>382,438</u>	<u>417,070</u>
Net investment income	<u>6,980,078</u>	<u>146,231,701</u>
DEDUCTIONS — Benefit payments (Note 1)	<u>142,804,614</u>	<u>136,526,849</u>
NET INCREASE (DECREASE) IN PLAN NET ASSETS	(135,824,536)	9,704,852
PLAN NET ASSETS HELD IN TRUST FOR BENEFITS:		
Beginning of year	<u>611,060,075</u>	<u>601,355,223</u>
End of year	<u>\$475,235,539</u>	<u>\$611,060,075</u>

See notes to financial statements.

**NEW YORK CITY POLICE DEPARTMENT  
POLICE OFFICERS'  
VARIABLE SUPPLEMENTS FUND**

**NOTES TO FINANCIAL STATEMENTS  
YEARS ENDED JUNE 30, 2012 AND 2011**

---

**1. PLAN DESCRIPTION**

The New York City ("The City") Police Pension Fund administers both the Police Officers' Variable Supplements Fund (POVSF, the "Fund" or the "Plan") and the Police Superior Officers' Variable Supplements Fund (PSOVSF). The Fund operates pursuant to the provisions of Title 13, Chapter 2 of the Administrative Code of The City of New York (ACNY) and provides supplemental benefits to retired Police Officers. To be eligible to receive Fund benefits, Police Officers must retire, on or after October 1, 1968, and be receiving a service retirement benefit from the New York City Police Pension Fund (POLICE).

Except for service retirement, Fund benefits are forfeitable upon separation from service.

The Fund is included in the Pension and Other Employee Benefit Trust Funds section of The City's Comprehensive Annual Financial Report (CAFR).

The PSOVSF is maintained as a separate fund and is not included in these financial statements.

Under current law, the Fund is not to be construed as constituting a pension or retirement system. Instead, it provides defined supplemental payments, other than pension or retirement system allowances, in accordance with applicable statutory provisions. While The City guarantees these payments, the New York State Legislature has reserved to itself and the State of New York (the "State") the right and power to amend, modify, or repeal the Fund and the payments it provides.

At June 30, 2011 and June 30, 2010, the dates of the Fund's most recent actuarial valuations, the Fund's membership consisted of:

	<b>2011</b>	<b>2010</b>
Retirees currently receiving payments	11,462	11,004
Active members*	<u>21,320</u>	<u>21,905</u>
Total	<u>32,782</u>	<u>32,909</u>

\* Represents the number of actively employed Police Officers as of the June 30 valuation dates.

The Fund provides a guaranteed schedule of supplemental benefits for Police Officers who retire (or have retired) as Police Officers on service retirement with at least 20 years of service as follows:

- a. For those who retired prior to July 1, 1988, the annual benefit was \$2,500 in Calendar Year 1988. For those who retired during Calendar Year 1988, the annual \$2,500 benefit payment was prorated. The annual benefit increases \$500 each year thereafter to a maximum of \$12,000 in the Calendar Year 2007 and thereafter.

For those who were members of POLICE prior to July 1, 1988 and who retire after Calendar Year 1988, the annual benefit payment is the scheduled amount described above prorated in the year of retirement and the full amount thereafter.

- b. For those who become members of POLICE on or after July 1, 1988, the annual supplemental benefit is \$2,500 for the first twelve months of retirement, which increases by \$500 each year until a maximum of \$12,000 is payable in the twentieth and later years of retirement. This was modified by Chapter 503 of the Laws of 1995 (Chapter 503/95) as discussed below.

Chapter 503/95 amended the ACNY in relation to the transfer of assets, liabilities and administration of certain pension funds in the New York City Police Department. In addition, this law permits certain active employees with prior service credit before entering POLICE to utilize their original dates of hire for determining benefits from the Fund. It also provides that police officers who became members of POLICE on or after July 1, 1988 will receive the maximum \$12,000 benefit beginning Calendar Year 2008 and thereafter.

Chapter 216 of the Laws of 2002 (Chapter 216/02) provides that participants of the Fund who retire from POLICE on and after January 1, 2002 with more than 20 years of service are entitled to an additional one-time special lump sum payment in the first year following retirement equal to the cumulative Fund benefits that would have been paid after January 1, 2002 had they retired at the completion of their 20th year of service (VSF DROP).

In the past, the New York State Legislature, in recognition of inflation, has increased retirement benefits to retirees of its public pension systems. Any increase in the amounts of ad-hoc cost-of-living increases ("Supplementation") or automatic Cost-of-Living Adjustments (COLA) payable from POLICE for retirees of the Fund under legislation enacted after 1988 will reduce benefits payable from the Fund until the later of: (a) age 62, or (b) Calendar Year 2007 (the twentieth year of retirement or Calendar Year 2008, if earlier, in the case of new members on and after July 1, 1988).

Chapter 119 of the Laws of 1995 (Chapter 119/95) provides additional benefits for Supplementation payable from POLICE on and after December 1, 1996 for certain retirees of POLICE effective as enacted by The City Council on October 25, 1995.

Chapter 390 of the Laws of 1998 (Chapter 390/98) provides additional benefits for Supplementation payable from POLICE on and after September 1, 1998 (with a second increase commencing September 1, 1999).

Chapter 125 of the Laws of 2000 (Chapter 125/00) provides Supplementation benefits from POLICE for certain retirees who retired before Calendar Year 1997 effective September 2000. In addition, Chapter 125/00 provides future COLA increases from POLICE beginning September 2001 and on each subsequent September to eligible retirees.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Basis of Accounting** — The Fund is accounted for on an accrual basis where the measurement focus is on the flow of economic resources. Revenues are recognized in the accounting period in which they are earned and expenses are recognized in the period incurred.

**Method Used to Value Investments** — Investments are valued at fair value. Trading securities are stated at the last reported sales price on a national securities exchange on the last business day of the fiscal year. Securities purchased pursuant to agreements to resell are carried at the contract price, exclusive of interest, at which the securities will be resold. Fair value is defined as the quoted market value on the last trading day of the period, except for the Short-Term Investment Fund (“STIF”) (a money market fund) and the International Investment Funds (“IIF”). The IIF’s are privately traded funds, which are managed by various investment managers on behalf of the Plan. Plan management determines fair value of the IIF’s based on information provided by the various investment managers. Management records the STIF at cost, which approximates fair value.

Purchases and sales of securities are reflected on the trade date. Gains or losses on sales of securities are based on the average cost of securities.

Dividend income is recorded on the ex-dividend date. Interest income is recorded as earned on an accrual basis.

No investment in any one security represents 5% or more of the Fund’s net assets held in trust for benefits.

The Plan does not possess an investment risk policy statement nor does it actively manage Plan assets to specified risk targets. Rather, investment risk management is an inherent function of our asset allocation process. Plan assets are diversified over a broad range of asset classes and encompass multiple investment strategies aimed at limiting concentration risk.

**Contributions** — POLICE is the source of funding for the Fund. Section 13-232 of the ACNY states, among other things, how amounts transferred into the Fund shall be computed.

**Income Taxes** — Income earned by the Fund is not subject to Federal income tax.

**Accrued Benefits Payable** — Accrued benefits payable represent either: (1) benefits due and unpaid from the preceding payment date of December 15; or (2) benefits deemed incurred and unpaid (an accrual for a portion of the current Calendar Year benefit) for the Fiscal Year-end of June 30.

**Securities Lending Transactions** — State Statutes and the Fund Board of Trustees policies permit the Fund to lend its securities (the underlying securities) to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. The Fund’s custodian lends the following types of securities: short-term securities; common stock; long-term corporate bonds; U.S. Government and U.S. Government agency bonds; asset-backed securities; and international equities and bonds held in collective investment funds. In return, it receives collateral in the form of cash and treasury and U.S. Government agency securities at 100% to 105% of the principal plus accrued interest for reinvestment. At year-end, the Fund had no custodian credit risk exposure to borrowers because the amounts the Fund owed the borrowers exceeded the amounts the borrowers owed the Fund. The contracts with the fund custodian require borrowers to indemnify the Fund if the borrowers fail to return the securities and if the collateral is inadequate to replace the securities loaned or fail to pay the Fund for income distributions by the securities’ issuers while the securities are on loan. All securities loans can be terminated on demand within a period specified in each agreement by either the Fund or the borrowers. Cash collateral is invested in the lending agents’ short-term investment pools, which have a weighted average maturity of 83 days.

The securities lending program in which the Fund participates only allows pledging or selling securities in the case of borrower default. Accordingly, the Fund is fully indemnified against any loss of value between the securities loaned and the securities held as collateral.

Governmental Accounting Standards Board (“GASB”) Statement No. 28, *Accounting and Financial Reporting for Securities Lending Transactions*, requires that securities loaned as assets be reported in the statements of plan net assets. Cash received as collateral on securities lending transactions and investments made with that cash are reported as assets. Securities received as collateral are also reported as assets if the government entity has the ability to pledge or sell them without a borrower default. Liabilities resulting from these transactions are reported in the statements of fund net assets. Accordingly, the Fund recorded the investments purchased with the cash collateral as collateral from securities lending transactions with a corresponding liability as securities lending transactions. Securities on loan are carried at market value. The value as of June 30, 2012 and 2011 is \$43.7 million and \$69.1 million, respectively.

**New Accounting Standard Adopted** — In fiscal year 2011, the Plan adopted one new statement on financial accounting standards issued by the Governmental Accounting Standards Board (“GASB”). GASB Statement No. 59, *Financial Instruments Omnibus* updates and improves existing standards regarding financial reporting and disclosure requirements of certain financial instruments and external investment pools for which significant issues have been identified in practice. The Plan has determined that GASB Statement No. 59 had no impact on the Plan’s financial statements as a result of the implementation.

**New Accounting Standard Issued but Not Yet Effective-** In June of 2012, GASB issued Statement No. 67, *Financial Reporting for Pension Plans*. This Statement establishes financial reporting standards for state and local governmental pension plans, defined benefit pension plans and defined contribution pension plans that are administered through trusts or equivalent arrangements in which: (1) contributions from employers and nonemployer contributing entities to the pension plan and earnings on those contributions are irrevocable (2) pension plan assets are dedicated to providing pensions to plan members in accordance with the benefit terms and (3) pension plan assets are legally protected from the creditors of employers, nonemployer contributing entities, and the pension plan administrator. If the plan is a defined benefit pension plan, plan assets also are legally protected from creditors of the plan members. For defined benefit pension plans, this statement establishes standards of financial reporting for separately issued financial reports and specifies the required approach to measuring the pension liability of employers and nonemployer contributing entities for benefits provided through the pension plan (the net pension liability), about which information is required to be presented. Distinctions are made regarding the particular requirements depending upon the type of pension plan administered. This Statement replaces the requirements of Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and Statement No. 50, *Pension Disclosures*, as they relate to pension plans that are administered through trusts or equivalent arrangements that meet certain criteria. The requirements of Statements 25 and Statement No. 50 remain applicable to pension plans that are not administered through trusts covered by the scope of this Statement and to defined contribution plans that provide postemployment benefits other than pensions. The provisions of Statement No. 67 are effective for financial statements for fiscal years beginning after June 15, 2013. Earlier application is encouraged. The Plan has not completed the process of evaluating the impact of Statement No. 67 on its financial statements.

### 3. INVESTMENTS AND DEPOSITS

The Comptroller of The City of New York (the “Comptroller”) acts as an investment advisor to the Plan. In addition, the Plan employs an independent investment consultant as an investment advisor. The Plan

utilizes several investment managers to manage the long-term debt and equity portfolios. The managers are regularly reviewed, with regard to both their investment performance and for their adherence to investment guidelines.

**Concentration of Credit Risk** — The criteria for Plan investments are as follows:

The Plan does not have any investments in any one entity that represent 5% or more of plan net assets.

The legal requirements for Plan investments are as follows:

Fixed income, equity and other investments may be made as permitted by New York State RSSL §§ 176-178(a) and Banking Law § 235, the New York City Administrative Code, and the Legal Investments for New York Savings Banks list as published by The New York State Banking Department, subject to Note 3(b).

Investments up to 25% of total pension fund assets may be made in instruments not expressly permitted by the State RSSL.

Bank of New York Mellon (“BNYM”) is the primary custodian for substantially all of the securities of the Plan.

Cash deposits are insured by the Federal Deposit Insurance Corporation for up to \$250,000 per Plan member and are, therefore, fully insured.

**Credit Risk** — Portfolios other than U.S. Government and related portfolios have credit rating limitations. Investment Grade portfolios are limited to mostly ratings of BBB and above except that they are also permitted a 10% maximum exposure to BB & B rated securities. While Non Investment grade managers are primarily invested in BB & B rated securities, they can also invest up to 7% of their portfolio in securities rated CCC. Non-rated securities are considered to be non-investment grade. The quality ratings of investments, by percentage of the rated portfolio, as described by nationally recognized statistical rating organizations are as follows:

Investment Type *	S&P Quality Ratings									
	AAA	AA	A	BBB	BB	B	CCC& Below	Short Term	Not Rated	Total
<b>June 30, 2012</b>										
U.S. Government	- %	- %	- %	- %	- %	- %	- %	- %	- %	- %
Corporate bonds	0.29	4.24	19.47	19.83	1.60	0.05	0.81	-	2.66	48.95
Yankee bonds	-	0.31	-	0.29	-	-	-	-	0.19	0.79
Short-term:										
Commercial paper	-	-	-	-	-	-	-	32.48	-	32.48
Pooled fund	-	-	-	-	-	-	-	-	17.78	17.78
U.S. Treasuries	-	-	-	-	-	-	-	-	-	-
U.S. Agencies	-	-	-	-	-	-	-	-	-	-
Percent of rated portfolio	<u>0.29 %</u>	<u>4.55 %</u>	<u>19.47 %</u>	<u>20.12 %</u>	<u>1.60 %</u>	<u>0.05 %</u>	<u>0.81 %</u>	<u>32.48 %</u>	<u>20.63 %</u>	<u>100.00 %</u>
<b>June 30, 2011</b>										
U.S. Government	- %	- %	- %	- %	- %	- %	- %	- %	- %	- %
Corporate bonds	2.82	5.20	19.97	24.60	12.86	11.51	3.07	-	1.55	81.58
Yankee bonds	0.11	-	-	0.22	-	-	-	-	0.31	0.64
Short-term:										
Commercial paper	-	-	-	-	-	-	-	6.23	-	6.23
Pooled fund	-	-	-	-	-	-	-	-	11.55	11.55
U.S. Treasuries	-	-	-	-	-	-	-	-	-	-
U.S. Agencies	-	-	-	-	-	-	-	-	-	-
Percent of rated portfolio	<u>2.93 %</u>	<u>5.20 %</u>	<u>19.97 %</u>	<u>24.82 %</u>	<u>12.86 %</u>	<u>11.51 %</u>	<u>3.07 %</u>	<u>6.23 %</u>	<u>13.41 %</u>	<u>100.00 %</u>

\* U.S. Treasury Bonds, Notes and Treasury-inflation protected securities are obligations of the U.S. Government or explicitly guaranteed by the U.S. government and therefore not considered to have credit risk and are not included above.

**Custodial Credit Risk** — Deposits are exposed to custodial credit risk if they are uninsured and uncollateralized. Custodial credit risk is the risk that, in the event of a failure of the counterparty, the Plan will not be able to recover the value of its 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 Plan and are held by either the counterparty or the counterparty's trust department or agent but not in the Plan's name.

Consistent with the Plan's investment policy, the investments are held by the Plan's custodian and registered in the Plan's name.

No investment in any one security represents 5% or more of Plan Assets Held in Trust for Benefits.

All of the Plan's deposits are insured and/or collateralized by securities held by a financial institution separate from the Plan's depository financial institution.

All of the Plan's securities are held by the Plan's custodial bank in the Plan's name.

**Interest Rate Risk** — Interest rate risk is the risk that the fair value of investments could be adversely affected by the change in interest rates. Duration limits are used to control the portfolios exposure to

interest rate changes. In the investment grade core Fixed Income portfolios duration is limited to a range of -1 to .75 years versus the duration of the benchmark indices. Duration range is a measure of the overall portfolio, while statements of the stated maturity reflect the specific maturities of the individual securities held. The Plan has no formal risk policy. The lengths of investment maturities (in years), as shown by the percent of the rated portfolio, are as follows:

**Years to Maturity**

<b>Investment Type June 30, 2012</b>	<b>Investment Maturities</b>				
	<b>Fair Value</b>	<b>Less Than One Year</b>	<b>One to Five Years</b>	<b>Six to Ten Years</b>	<b>More Than Ten Years</b>
U.S. Government	51.43 %	- %	0.67 %	3.96 %	46.80 %
Corporate bonds	23.31	0.86	8.62	6.73	7.10
Yankee bonds	0.37	-	-	0.14	0.23
Short-term:					
Commercial paper	15.46	15.46	-	-	-
Pooled fund	8.47	8.47	-	-	-
U.S. Agencies	0.96	-	-	-	0.96
U.S. Agencies	-	-	-	-	-
Percent of rated portfolio	<u>100.00 %</u>	<u>24.79 %</u>	<u>9.29 %</u>	<u>10.83 %</u>	<u>55.09 %</u>

<b>Investment Type June 30, 2011</b>	<b>Investment Maturities</b>				
	<b>Fair Value</b>	<b>Less Than One Year</b>	<b>One to Five Years</b>	<b>Six to Ten Years</b>	<b>More Than Ten Years</b>
U.S. Government	55.80 %	- %	6.96 %	3.21 %	45.63 %
Corporate bonds	35.89	0.26	12.57	12.24	10.82
Yankee bonds	0.28	0.08	-	0.10	0.10
Short-term:					
Commercial paper	2.74	2.74	-	-	-
Pooled fund	5.08	5.08	-	-	-
U.S. Treasuries	-	-	-	-	-
U.S. Agencies	0.21	0.04	-	-	0.17
Percent of rated portfolio	<u>100.00 %</u>	<u>8.20 %</u>	<u>19.53 %</u>	<u>15.55 %</u>	<u>56.72 %</u>

Where required, the Board of Trustees of POLICE adopted those changes to actuarial assumptions that required Board approval. The State Legislature and the Governor were expected to enact prior to June 30, 2012 and are now expected to enact legislation to provide for those changes to the actuarial assumptions and methods that require legislation, including the AIR assumption of 7.0% per annum, net of expenses.

For the actuarial valuations of the Fund beginning June 30, 2005, the Actuary used actuarial assumptions that were adopted during Fiscal Year 2006 by the Board of Trustees of POLICE.

For actuarial valuations of the Fund beginning June 30, 2011, the Actuary used actuarial assumptions that were adopted during Fiscal Year 2012 by the Board of Trustees of POLICE.

For Fiscal Year 2011 financial reporting purposes, the June 30, 2010 actuarial valuation of the Fund used actuarial assumptions adopted during Fiscal Year 2006 by the Board of Trustees of POLICE. The June 30, 2010 actuarial valuation results for the Fund, based on actuarial assumptions adopted during Fiscal Year 2012 by the Board of Trustees of POLICE, are shown herein for purposes of comparison.

\* \* \* \* \*