

New York City Police  
Department Police Superior  
Officers' Variable Supplements  
Fund

Financial Statements for the Years  
Ended June 30, 2007 and 2006, and  
Independent Auditors' Report

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

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## INDEPENDENT AUDITORS' REPORT

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

We have audited the accompanying statements of Plan net assets of New York City Police Department Police Superior Officers' Variable Supplements Fund (the "Plan") as of June 30, 2007 and 2006, 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, such financial statements present fairly, in all material respects, the Plan net assets as of June 30, 2007 and 2006, 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.

Management's Discussion and Analysis is not a required part of the financial statements, but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit this information and express no opinion on it.

*Deloitte + Touche LLP*

October 30, 2007

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

## MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) YEARS ENDED JUNE 30, 2007 AND 2006

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The narrative discussion and analysis of the financial activities of New York City Police Superior Officers' Variable Supplements Fund (the "Fund" or the "Plan") for the fiscal years ended June 30, 2007 and 2006 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. This discussion and analysis is intended to be read in conjunction with the Plan's financial statements.

### 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 assets and liabilities are determined on an accrual basis.
- **The Statement of Changes in Plan Net Assets** — presents the results of activities during the year. All changes affecting the assets and liabilities of the Plan are reflected on an accrual basis when the activity occurred, regardless of the timing of the related cash flows. In that regard, changes in the fair values of investments are included in the year's activity as net appreciation 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 ("GASB") Pronouncements.

### FINANCIAL HIGHLIGHTS

- The Fund's total assets exceeded its liabilities by \$1.2 billion as of June 30, 2007 and by \$1.1 billion as of June 30, 2006.
- The Plan Net Assets Held in Trust for Benefits at June 30, 2007, increased by \$69.3 million or 6% compared to fiscal year 2006 and increased by \$7.6 million or 1% compared to fiscal year 2005.
- Benefit payments in fiscal year 2007 totaled \$140.3 million; an increase of 17% over the prior year. For fiscal year 2006, a total of \$ 120.3 million was paid, representing an increase of 13% over fiscal year 2005.

## FINANCIAL ANALYSIS

The Statements of Plan Net Assets for fiscal year 2007 and 2006 showed total assets exceeded total liabilities by \$1.2 billion and \$1.1 billion, respectively. The amounts represent total Plan Net Assets Held in Trust for Benefits; available to cover the Fund's primary obligation to pay benefits to the beneficiaries. Compared with the previous fiscal years; the Plan Net Assets Held in Trust for Benefits as of June 30, 2007 increased by \$69.3 million or 6% and as of June 30, 2006 by \$7.6 million or 1%. The Fund's Investment Portfolio increased by 7% during fiscal year 2007 and by 1% during fiscal year 2006. Overall, the Investment Portfolio performed better in the current years compared to trends in the prior years due to an upward trend in the economy.

The Fund's outstanding liabilities of \$372 million increased by 4.5% compared to fiscal year 2006. Last year the outstanding liabilities totaled \$356 million, an increase of 1.5% compared to fiscal year 2005. Total liabilities as of June 30, 2007 consist of outstanding securities lending transactions of 65%, accrued benefits payable of 17%, and payable for investment securities purchased of 18%.

**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 which resulted in a net increase of \$69.3 million and a net increase of \$7.6 million for fiscal years ended June 30, 2007 and 2006, respectively. The changes consisted of investment earnings of \$209.6 million and benefit payments of \$140.3 million in 2007, investment earnings of \$127.9 million and benefit payments of \$120.3 million for 2006 and for fiscal year 2005, investment earnings totaled \$118.7 million and benefit payments \$106.4 million.

**Deductions** — Deductions from the Fund consist mainly of benefit payments to members. All administrative and investment expenses are paid by the City of New York (the "City"). For fiscal year 2007 deductions totaled \$140.3 million compared to \$120.3 million in fiscal year 2006, which is an increase of \$20.0 million or 17% in 2007 compared to 2006. In addition, benefit payments increased this year primarily as a result of an increase in the number of retirees added to this plan and the increase in benefit payments.

### Funding and Plan Benefits

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

For fiscal years 2007, 2006 and 2005 there were no transfers from POLICE to the fund.

Eligible retirees were entitled to a benefit of \$12,000 for calendar year 2007 payable during December 2007. This benefit rate increases by \$500 per year to \$12,000 per year by calendar year 2007. These benefits are reduced for certain supplementations and Cost-of-Living Adjustments from POLICE.

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 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 (see note 4).

Effective fiscal year 2000, the Actuary recommended revisions to calculation of the HIR. This change in methodology makes the HIR for POLICE consistent with Chapter 255 of the Laws of 2000 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 distortions, the Actuary proposed to determine the HIR for fiscal year 2000 and later by taking an average of the monthly yields of 10-year Treasury notes as published in Federal Reserve Statistical Release 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 HIR for fiscal years 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 Funds. The primary objectives of the Fund are to provide benefits for its members and provide for growth in membership and also be prepared for inflation. Investments are made with the objective to minimize risks and maintain a high competitive return. Diversification has increased investment results and provided security for the assets of the Fund. 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 sale of securities are reflected on the trade date. No investment in any one security represents 5% or more of the 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 ten-year period ended June 30 2007, the Fund had an annualized return of 8.1%. Investments in assets that are expected to produce higher returns are also subject to greater volatility and may also produce negative returns. Fiscal year 2007 has been a good year for investors. Investments in stock markets within and outside the United States have generally gained value. For example, the Russell 3000 index, a broad measure of the U.S. stock market, gained 20.1% during this period, and the Europe, Australia and Far East (EAFE) Index, the most commonly used measure of performance in developed international markets, gained 27.0%. Less-developed international markets gained 45.5%. Lower-rated bonds ended the year with a gain of 27.4% in value. The returns of the Fund have been consistent with broad market trend; the asset allocation followed by the Fund produced a combined return of a gain of 18.8%. For the three-year period ended June 30, 2007 the combined gain was 13.5% and for the five-year period it was a gain of 12.0%

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 these investments is 160 days. The Fund earned an average yield of 5.50% which compares with the average of 5.47% on three-month Treasury Bills and 5.12% for a representative institutional money market Fund. The Fund earned \$190,000 in its short-term accounts during FY2007.

Assets are invested long-term for the benefit of the participants and their beneficiaries. All investments are managed by registered investment advisors, pursuant to applicable law and to guidelines issued by the Comptroller. The Fund utilizes nineteen domestic equity managers, eleven domestic fixed-income managers, seventeen international equity managers and two treasury inflation-protected security investment managers. Assets are allocated in accordance with plans 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 New York City Police Superior Officers' Variable Supplements Fund 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 Department Police Superior Officers' Variable Supplements Fund, 233 Broadway, 25<sup>th</sup> Floor, New York, NY 10279.

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

**STATEMENTS OF PLAN NET ASSETS  
JUNE 30, 2007 AND 2006**

	<b>2007</b>	<b>2006</b>
<b>ASSETS:</b>		
Cash	\$ 527	\$ 105,945
Receivables:		
Investments securities sold	10,829,225	23,577,751
Accrued interest and dividends	3,964,928	3,868,096
Total receivables	<u>14,794,153</u>	<u>27,445,847</u>
Investments — at fair value (Notes 2 and 3):		
Commercial Paper	3,446,435	
Other short term investments	7,196,353	13,263,403
Discount notes	1,498,610	2,695,695
Debt securities:		
U.S. Government	179,678,479	153,199,077
Corporate	172,132,008	161,436,835
Foreign	4,481,123	4,893,151
Equity securities	560,984,512	485,207,111
Mutual funds:		
International equity	331,435,612	348,692,036
Treasury inflation-protected securities	34,223,884	32,904,962
Collateral from securities lending transactions (Note 2)	241,119,102	235,897,498
Total investments	<u>1,536,196,118</u>	<u>1,438,189,768</u>
Total assets	<u>1,550,990,796</u>	<u>1,465,741,560</u>
<b>LIABILITIES:</b>		
Accounts payable and accrued liabilities	824,055	22,902
Payable for investment securities purchased	65,618,715	62,857,550
Accrued benefits payable (Note 2)	64,701,618	57,529,794
Securities lending transactions (Note 2)	241,119,102	235,897,498
Total liabilities	<u>372,263,490</u>	<u>356,307,744</u>
<b>PLAN NET ASSETS HELD IN TRUST FOR BENEFITS</b>	<u>\$1,178,727,306</u>	<u>\$1,109,433,816</u>

See notes to financial statements.

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

**STATEMENTS OF CHANGES IN PLAN NET ASSETS  
YEARS ENDED JUNE 30, 2007 AND 2006**

	<b>2007</b>	<b>2006</b>
ADDITIONS:		
Investment income (Note 2):		
Interest income	\$ 20,052,234	\$ 19,347,467
Dividend income	12,957,009	11,458,538
Net appreciation in fair value of investments	<u>176,082,403</u>	<u>96,474,880</u>
Total investment income	209,091,646	127,280,885
Less investment expenses	<u>19,262</u>	<u>22,540</u>
Net income	<u>209,072,384</u>	<u>127,258,345</u>
Securities lending transactions:		
Securities lending income	13,566,209	9,248,155
Securities lending fees	<u>(13,034,027)</u>	<u>(8,641,794)</u>
Net securities lending income	<u>532,182</u>	<u>606,361</u>
Net investment income	<u>209,604,566</u>	<u>127,864,706</u>
DEDUCTIONS — Benefit payments (Note 1)	<u>140,311,078</u>	<u>120,299,764</u>
INCREASE IN PLAN NET ASSETS	<u>69,293,488</u>	<u>7,564,942</u>
PLAN NET ASSETS HELD IN TRUST FOR BENEFITS:		
Beginning of year	<u>1,109,433,816</u>	<u>1,101,868,874</u>
End of year	<u>\$1,178,727,304</u>	<u>\$1,109,433,816</u>

See notes to financial statements.

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

**NOTES TO FINANCIAL STATEMENTS  
YEARS ENDED JUNE 30, 2007 AND 2006**

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**1. PLAN DESCRIPTION**

The New York City (the "City") Police Pension Fund administers the Police Superior Officers' Variable Supplements Fund (the "Fund" or the "Plan") and the Police Officers' Variable Supplements Fund ("POVSF"). 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 Superior Officers (including Sergeants or higher and Detectives). To be eligible to receive Fund benefits, Police Superior 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 forfeited 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 POVSF 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, 2006 and 2005, the dates of the Fund's most recent actuarial valuations, the Fund's membership consisted of:

	<b>2006</b>	<b>2005</b>
Retirees currently receiving payments	13,981	13,175
Active members*	<u>12,409</u>	<u>12,536</u>
Total	<u>26,390</u>	<u>25,711</u>

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

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

- a. A Police Superior Officer hired before July 1, 1988, who retires from service as a Police Superior Officer on or after October 1, 1988, receives a defined schedule of benefits starting at an annual rate of \$5,000 payable during December 1993 for the Calendar Year 1993 payment.

The 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 1993, the benefit for the first year of retirement is a proportion of the annual scheduled amount as described above for 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, increasing by \$500 each year until a maximum of \$12,000 is payable in the twentieth and later years of retirement. This was later modified by Chapter 444 of the Laws of 2001 ("Chapter 444/01") as discussed below.

Chapter 503 of the Laws of 1995 ("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.

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 Supplementation benefits or automatic Cost-of-Living Adjustments ("COLA") payable from POLICE for retirees of the Fund under legislation enacted after 1993 will reduce benefits payable from the Fund until the later of: (a) age 62, or (b) Calendar Year 2007 (the twentieth year of retirement in the case of new members on and after July 1, 1988).

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

Chapter 444/01 provided that Police Superior Officers who became members of the Fund on and after July 1, 1988, will receive the maximum \$12,000 benefit beginning Calendar Year 2008.

Chapter 390 of the Laws of 1998 ("Chapter 390/98") provided 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") provided Supplementation benefits from POLICE for certain retirees who retired before Calendar Year 1997 effective September 2000. In addition, Chapter 125/00 provided future COLA increases from POLICE beginning September 2001 and on each subsequent September to eligible retirees.

Chapter 152 of the Laws of 2006 ("Chapter 152/06") provided for those changes in actuarial assumptions and methods proposed by the Actuary, including the continuation of the Actuarial Interest Rate ("AIR") assumption of 8% per annum, for determining employer contributions to POLICE.

Chapter 216 of the Laws of 2002 ("Chapter 216/02") provided that participants of the Fund who retire from POLICE on and after January 1, 2002, with 20 or more 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").

## 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 (the “STIF”) (a money market fund) and the International Investment Funds (the “IIF”). The IIF’s are private 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 approximated 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 plan net assets held in trust for benefits.

**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 Board of Trustees policies permit the Fund to lend its 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 agencies 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 credit risk exposure to borrowers because the amounts the Fund owes the borrowers exceed the amounts the borrowers owe 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 90 days. The underlying fixed income securities which comprise these pools have an average maturity of ten years.

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 lent 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 will be reported in the Statements of Plan 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.

### 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 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 (“BONY”) 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 \$100,000 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, 2007</b>										
U.S. Government	16.41 %	- %	- %	- %	0.05 %	- %	- %	- %	- %	16.46 %
Corporate Bonds	25.94	7.87	10.94	13.37	8.27	9.89	1.13	-	0.74	78.15
Yankee Bonds	-	-	0.81	0.66	0.51	-	-	-	-	1.98
Short Term:										
Commercial Paper	-	-	-	-	-	-	-	-	-	-
Pooled Fund	-	-	-	-	-	-	-	2.73	-	2.73
Certificate of Deposit	-	-	-	-	-	-	-	-	-	-
U.S. Treasuries	-	-	-	-	-	-	-	0.68	-	0.68
U.S. Agencies	-	-	-	-	-	-	-	-	-	-
Percent of Rated Portfolio	<u>42.35 %</u>	<u>7.87 %</u>	<u>11.75 %</u>	<u>14.03 %</u>	<u>8.83 %</u>	<u>9.89 %</u>	<u>1.13 %</u>	<u>3.41 %</u>	<u>0.74 %</u>	<u>100.00 %</u>
<b>June 30, 2006</b>										
U.S. Government	17.30 %	- %	- %	- %	- %	- %	- %	- %	- %	17.30 %
Corporate Bonds	23.84	6.32	13.51	11.17	8.60	8.57	0.39	-	0.90	73.30
Yankee Bonds	-	0.11	0.56	1.02	0.56	-	-	-	-	2.25
Short Term:										
Pooled Funds	-	-	-	-	-	-	-	-	5.93	5.93
U.S. Treasuries	0.86	-	-	-	-	-	-	-	-	0.86
U.S. Agencies	-	-	-	-	-	-	-	0.36	-	0.36
Percent of Rated Portfolio	<u>42.00 %</u>	<u>6.43 %</u>	<u>14.07 %</u>	<u>12.19 %</u>	<u>9.16 %</u>	<u>8.57 %</u>	<u>0.39 %</u>	<u>0.36 %</u>	<u>6.83 %</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.

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 changes in interest rates will adversely affect the fair value of the investment. Duration limits are used to control the portfolios exposure to interest rate changes. Duration is limited to a range of -1 to .75 years. 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 length of investment maturities (in years) are as follows:

**Years to Maturity  
Investment Type  
June 30, 2007**

	<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	49.38 %	0.01 %	37.66 %	8.77 %	2.94 %
Corporate Bonds	47.36	12.70	19.32	10.74	4.60
Yankee Bonds	1.20	-	0.58	0.17	0.45
Short Term:					
Commercial Paper					
Pooled Fund	1.65	1.65	-	-	-
Certificate of Deposit					
U.S. Treasuries	0.41	0.41	-	-	-
U.S. Agencies	-	-	-	-	-
Percent of Rated Portfolio	<u>100.00 %</u>	<u>14.77 %</u>	<u>57.56 %</u>	<u>19.68 %</u>	<u>7.99 %</u>

June 30, 2006

	<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	45.71 %	0.01 %	0.99 %	7.89 %	36.82 %
Corporate Bonds	48.12	0.82	26.99	7.85	12.46
Yankee Bonds	1.47	0.10	0.45	0.17	0.75
Short Term:					
Pooled Funds	3.90	3.90	-	-	-
U.S. Treasuries	0.56	0.56	-	-	-
U.S. Agencies	0.24	0.24	-	-	-
Percent of Rated Portfolio	<u>100.00 %</u>	<u>5.63 %</u>	<u>28.43 %</u>	<u>15.91 %</u>	<u>50.03 %</u>

**Securities Lending Transactions —**

*Credit Risk* — The quality ratings of investments held as collateral for Securities Lending as of June 30, 2007 and 2006, are as follows (in thousands):

Investment Type and Fair Value of Securities Lending Transactions	S&P Quality Ratings									
	AAA	AA	A	BBB	BB	B	CCC & Below	Short Term	Not Rated	Total
<b>June 30, 2007</b>										
U.S. Government	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Corporate Bonds	19,757	19,212	12,556	-	-	-	-	26,947	755	79,227
Yankee Bonds	-	-	-	-	-	-	-	3,700	-	3,700
Short term:										
Commercial Paper	-	-	-	-	-	-	-	7,170	-	7,170
Pooled Funds	30,122	-	-	-	-	-	-	-	-	30,122
Repurchase Agreements	-	-	-	-	-	-	-	1,090	43,380	44,470
Certificates of Deposits	-	14,932	2,126	-	-	-	-	23,820	-	40,878
Bank Notes	3,472	12,163	9,805	-	-	-	-	7,276	-	32,716
Other	20	78	-	-	-	-	-	2,738	-	2,836
<b>Total</b>	<b>\$53,371</b>	<b>\$46,385</b>	<b>\$24,487</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$72,741</b>	<b>\$ 44,135</b>	<b>\$ 241,119</b>
Percent of securities lending portfolio	22.13%	19.24%	10.16%	- %	- %	- %	- %	30.17%	18.30%	100.00%
<b>June 30, 2006</b>										
U.S. Government	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Corporate Bonds	18,736	18,233	40,602	-	-	-	-	10,627	1,498	89,696
Yankee Bonds	-	-	-	-	-	-	-	3,264	-	3,264
Short term:										
Commercial Paper	-	-	-	-	-	-	-	9,284	-	9,284
Pooled Funds	28,654	-	-	-	-	-	-	-	-	28,654
Repurchase Agreements	-	-	-	-	-	-	-	3,043	32,192	35,235
Certificates of Deposits	-	32,656	5,791	-	-	-	-	621	-	39,068
Bank Notes	163	18,162	7,514	-	-	-	-	2,603	-	28,442
Other	-	543	284	-	-	-	-	1,427	-	2,254
<b>Total</b>	<b>\$47,553</b>	<b>\$69,594</b>	<b>\$54,191</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$30,869</b>	<b>\$ 33,690</b>	<b>\$ 235,897</b>
Percent of securities lending portfolio	20.16%	29.50%	22.97%	- %	- %	- %	- %	13.09%	14.28%	100.00%

**Interest Rate Risk** — The lengths of investment maturities (in years) of the collateral for Securities Lending as of June 30, 2007 and 2006, are as follows (in thousands):

**June 30, 2007**

Securities Lending Years to Maturities	Fair Value	Investment Maturities			
		Less than one year	One to five years	Six to ten years	More than ten years
U.S. Government	\$ -	\$ -	\$ -	\$ -	\$ -
Corporate Bonds	79,226	23,235	55,991	-	-
Yankee Bonds	3,700	1,513	2,187	-	-
Short-term:					
Commercial Paper	7,170	7,170	-	-	-
Pooled Funds	30,122	30,122	-	-	-
Repurchase Agreements	44,471	44,471	-	-	-
Certificates of Deposits	40,877	23,820	17,057	-	-
Bank Notes	32,716	6,625	26,091	-	-
Other	2,837	2,181	656	-	-
<b>Total</b>	<b>\$ 241,119</b>	<b>\$ 139,137</b>	<b>\$ 101,982</b>	<b>\$ -</b>	<b>\$ -</b>
Percent of securities lending portfolio	100.00%	57.70%	42.30%	- %	- %

**June 30, 2006**

Securities Lending Years to Maturities	Fair Value	Less than one year	One to five years	Six to ten years	More than ten years
Corporate Bonds	89,696	10,267	79,429	-	-
Yankee Bonds	3,264	1,092	2,172	-	-
Short-term:					
Commercial Paper	9,284	9,284	-	-	-
Pooled Funds	28,654	28,654	-	-	-
Repurchase Agreements	35,235	35,235	-	-	-
Certificates of Deposits	39,068	621	38,447	-	-
Bank Notes	28,442	190	28,252	-	-
Other	2,254	2,176	78	-	-
<b>Total</b>	<b>\$ 235,897</b>	<b>\$ 87,519</b>	<b>\$ 148,378</b>	<b>\$ -</b>	<b>\$ -</b>

**4. FUNDING**

The 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.

For Fiscal Year 2007, the excess earnings of POLICE, inclusive of prior year’s cumulative deficiencies, are estimated to be equal to zero and, therefore, no transfer will be due from POLICE to the Fund as of June 30, 2007.

For Fiscal Year 2006, the excess earnings of POLICE, inclusive of prior year's cumulative deficiencies, were estimated to be equal to zero and, therefore, no transfer was due from POLICE to the Fund as of June 30, 2006.

In addition, Chapter 479 of the Laws of 1993 states that if the assets of the Fund are less than the amount required to pay the retirees' guaranteed scheduled annual supplemental benefit payments, then the City is required by law to fund the difference. However, it is not anticipated that the City will be required to contribute directly to the Fund.

The amount shown below as the ABO is the measure of the present value of supplemental benefits estimated to be payable in the future as a result of employee service-to-date. The ABO is calculated as the actuarial present value of credited projected benefits, prorated on service and is intended to help users assess the funded status of the Fund on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due and make comparisons among variable supplements funds.

Actuarial valuations of the Fund are performed annually as of June 30.

A comparison of the ABO as calculated by the Actuary with the Plan net assets held in trust for benefits as calculated by the Actuary as of June 30, 2006 and 2005, follows (in millions):

	<u>Amount</u>	
	<u>2006</u>	<u>2005</u>
Accumulated benefit obligation for:		
Retirees currently receiving benefits	\$ 1,527.7	\$ 1,392.2
Active members	<u>856.1</u>	<u>860.9</u>
Total accumulated benefit obligation*, **	2,383.8	2,253.1
Plan net assets held in trust for benefits***	<u>1,109.4</u>	<u>1,101.9</u>
Unfunded accumulated benefit obligation	<u>\$ 1,274.4</u>	<u>\$ 1,151.2</u>

\* The June 30, 2006 and 2005, ABOs decreased by approximately \$60.4 million and \$87.5 million, respectively, compared to those projected prior to the enactment of Chapters 119/95, 390/98 and 125/00.

\*\* These total ABOs have been reduced by accrued benefits payable. This basis of reporting the total ABO is consistent with that used to report Plan net assets held in trust for benefits in these financial statements, but may differ from the bases used for other purposes.

\*\*\* See Note 2 for valuation of investments in the calculation of Plan net assets held in trust for benefits.

The June 30, 2006 actuarial valuation, used to determine the ABO, is based on the same actuarial assumptions and methods as were used in the actuarial valuation as of June 30, 2005.

For purposes of the June 30, 2006 and 2005, actuarial valuations of the Fund, Chapter 125/00 has been taken into account in the determination of the unfunded ABO relative to the Supplementation benefit

increases that began Fiscal Year 2001 and to the automatic COLA provided for Fiscal Year 2002 and each future year (see Note 1).

Sections 13-270 and 13-280 of the ACNY provide that the Boards of Trustees of the POVSF and the Fund shall adopt, upon the recommendation of the Actuary, actuarial assumptions as to interest rate, mortality of beneficiaries and estimated number of active members of POLICE in service as of each June 30 who will retire for service with 20 or more years of service as Police Officers and Police Superior Officers, for use in making annual valuations of liabilities.

The following actuarial assumptions represent the recommendations of the Actuary that were used in the actuarial calculations to determine the ABO as of June 30, 2006 and 2005, respectively:

	June 30, 2006	June 30, 2005
Investment rate of return	8.0% per annum. <sup>(1)</sup>	8.0% per annum. <sup>(1)</sup>
Post-retirement mortality	Tables adopted by POLICE during Fiscal Year 2006.	Tables adopted by POLICE during Fiscal Year 2006.
Active service: withdrawal, death, and disability	Tables adopted by POLICE during Fiscal Year 2006.	Tables adopted by POLICE during Fiscal Year 2006.
Service retirement	Tables adopted by POLICE during Fiscal Year 2006.	Tables adopted by POLICE during Fiscal Year 2006.
Percentage of all active POLICE members estimated to retire for service with 20 or more years of service as Police Superior Officers	50%	50%
Percentage of all active Police Superior Officers estimated to retire for service with 20 or more years of service as Police Superior Officers	100%	100%
Cost-of-Living Adjustments	1.3% per annum. <sup>(1)</sup>	1.3% per annum. <sup>(1)</sup>
Actuarial Asset Valuation Method	Fair Market Value.	Fair Market Value.

<sup>(1)</sup> Developed assuming a long-term Consumer Price Inflation assumption of 2.5% per year.

## 5. INVESTMENT ADVISORS

The Comptroller of the City (the "Comptroller") 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. To be eligible for consideration, investments must meet criteria set forth in governing laws and regulations.

## 6. RELATED PARTIES

Administrative expenses are paid by the City. The Comptroller provides certain administrative services to the Fund. The Actuary is appointed to be the technical advisor to the Fund and the Office of the Actuary provides related actuarial services to the Fund. The City's Corporation Counsel provides legal services to the Fund. The City also provides other administrative services.

The Comptroller has been appointed by law as the custodian for monies and assets of the Plans with revocable discretionary authority. Securities are held by certain banks under custodial agreements with the Comptroller.

## 7. CONTINGENT LIABILITIES

From time to time the Fund has a number of claims pending against it and has been named as defendant in a number of lawsuits. The Fund also has certain other contingent liabilities. Management of the Fund, on the advice of legal counsel, believes that such proceedings and contingencies generally do not have a material effect on the plan net assets or changes in the plan net assets of the Fund. Under the State statutes and City laws that govern the functioning of the Fund, increases in the obligation of the Fund to members and beneficiaries ordinarily result in increases to the future potential obligations of POLICE.

## 8. OTHER ACTUARIAL INFORMATION

**Actuarial Audit** — Pursuant to Section 96 of the New York City Charter, studies of the actuarial assumptions used to value liabilities of the five actuarially-funded New York City Retirement Systems ("NYCRS") are conducted every two years. The most recent study was published by The Segal Company ("Segal") dated November 2006 and analyzed experience for Fiscal Years 2002 through 2005. Segal made recommendations to the actuarial assumptions and methods based on their analysis. The Actuary is reviewing those recommendations.

**Revised Actuarial Assumptions and Methods** — In accordance with the ACNY and with appropriate practice, the Boards of Trustees of the five actuarially-funded NYCRS are to periodically review and adopt actuarial assumptions as proposed by the Actuary for use in the determination of employer contributions.

Based upon a review of an October 2003 experience study by Gabriel, Roeder, Smith & Company ("GRS"), the Actuary issued an August 24, 2005 Report entitled "Proposed Changes in Actuarial Assumptions and Methods for Determining Employer Contributions for Fiscal Years Beginning on and After July 1, 2005 for the New York City Police Pension Fund" ("August 2005 Report"). Where required, the Board of Trustees of POLICE adopted those changes to actuarial assumptions that required Board approval and the State Legislature and the Governor have enacted Chapter 152/06 to provide for those changes to the actuarial assumptions and methods that required legislation, including the AIR assumption of 8.0% per annum.

For the actuarial valuations of the Fund from June 30, 1999 to June 30, 2004, the Actuary used actuarial assumptions that were adopted during Fiscal Year 2000 by the Board of Trustees of POLICE.

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.

\* \* \* \* \*