State of Rhode Island

Employees' Retirement System

FISCAL YEAR ENDED JUNE 30, 2012

Dennis E. Hoyle, CPA
Auditor General

State of Rhode Island and Providence Plantations
General Assembly
Office of the Auditor General

Office of the Auditor General
State of Rhode Island and Providence Plantations - General Assembly
Dennis E. Hoyle, CPA - Auditor General
oag.ri.gov
86 Weybosset Street • Providence, RI • 02903-2800
tel: 401.222.2435 • fax: 401.222.2111

December 11, 2012

JOINT COMMITTEE ON LEGISLATIVE SERVICES:

SPEAKER Gordon D. Fox, Chairman

Senator M. Teresa Paiva Weed
Senator Dennis L. Algiere
Representative Nicholas A. Mattiello
Representative Brian C. Newberry

We have completed our audit of the financial statements of the Employees' Retirement System of the State of Rhode Island for the fiscal year ended June 30, 2012 in accordance with Chapter 36-8-19 of the Rhode Island General Laws.

Our report is contained herein as outlined in the Table of Contents.

Sincerely,

Dennis E. Hoyle, CPA
Auditor General

EMPLOYEES' RETIREMENT SYSTEM OF THE STATE OF RHODE ISLAND

FISCAL YEAR ENDED JUNE 30, 2012

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INDEPENDENT AUDITOR'S REPORT

JOINT COMMITTEE ON LEGISLATIVE SERVICES, GENERAL ASSEMBLY
STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS:

RETIREMENT BOARD OF THE EMPLOYEES' RETIREMENT SYSTEM OF THE
STATE OF RHODE ISLAND:

We have audited the accompanying basic financial statements of the plans which comprise the Employees' Retirement System of the State of Rhode Island (the System) as of June 30, 2012 and for the year then ended, as listed in the table of contents. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 1, the financial statements present only the Pension Trust Funds of the State of Rhode Island and Providence Plantations (the State) and do not purport to, and do not, present fairly the financial position of the State, as of June 30, 2012, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the fiduciary net assets of the plans within the System as of June 30, 2012, and the changes in fiduciary net assets for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As more fully described in Notes 2 and 6 to the financial statements, on November 18, 2011 the Rhode Island General Assembly enacted comprehensive pension reform legislation that significantly modified benefit provisions including cost of living adjustments, implemented a defined contribution plan to supplement the modified defined benefit plans, and reamortized the unfunded actuarial accrued liability. The pension reform legislation had the objectives of enhancing retirement security for plan members by reducing the unfunded liability thereby improving the funded status of the plans within the System, and stabilizing projected increases in required employer contributions.

Joint Committee on Legislative Services
Retirement Board of the Employees' Retirement System of the State of Rhode Island
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As more fully described in Notes 3 and 4 to the financial statements, approximately 26% of the holdings in the pooled investment trust are hedge funds, private equity and real estate investments. Because the fair value of these investments were not all determined based on quoted market prices, the fair values may differ from the values that would have been determined had a ready market for these investments existed.

As more fully described in Note 10 to the financial statements, various lawsuits have been filed challenging pension reforms legislatively enacted in 2009 and 2010 as well as the more recent pension reforms enacted on November 18, 2011.

In accordance with *Government Auditing Standards*, we will issue our report dated December 3, 2012 on our consideration of the System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 8 and the Schedules of Funding Progress and the Schedules of Contributions from the Employers and Other Contributing Entity on pages 39 and 40 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 inquires, 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.

Dennis E. Hoyle, CPA
Auditor General

December 3, 2012

Management's Discussion and Analysis

Management of the Employees' Retirement System of the State of Rhode Island (the System) provides this Management's Discussion and Analysis of their financial performance for the readers of the System's financial statements. This narrative provides an overview of the System's financial activity for the fiscal year ended June 30, 2012. This analysis is to be considered in conjunction with the financial statements to provide an objective analysis of the System's financial activities based on the status of the System and issues currently facing management.

Understanding the Employees' Retirement System Financial Statements

The System administers defined benefit pension plans for state employees, teachers, state police, judges and participating municipal employees. State employees and teachers are combined in one plan while state police, judges and municipal employees each have separate plans. The *Statements of Fiduciary Net Assets* provide a snapshot of the financial position of the System at June 30, 2012. The *Statements of Changes in Fiduciary Net Assets* summarize the additions and deductions that occurred during the fiscal year. The *Notes to the Financial Statements* provide additional information that is essential to a full understanding of the financial statements. The *Required Supplementary Information* consists of schedules and related notes, which demonstrate the System's progress in accumulating funds to meet future pension benefits for members of the System.

Financial Highlights for the Fiscal Year Ended June 30, 2012

- The System's fiduciary net assets decreased by $204 million from $7.5 billion at June 30, 2011 to $7.3 billion at June 30, 2012.

- Total pension benefits paid to members were $881 million, an increase of $35 million or 4.0% compared to the fiscal year ended June 30, 2011.

- Total employee and employer contributions into the System's plans increased $62.1 million compared to the prior year. Contributions to all plans from both employers and employees at June 30, 2012 were $582.7 million.

- The System's net gain from investing activities was $115.6 million for the fiscal year ended June 30, 2012.

- The Rhode Island General Assembly enacted comprehensive pension reform legislation that modified benefit provisions, reamortized the unfunded accrued actuarial liability as of June 30, 2010 and implemented a defined contribution plan to supplement the benefits provided under the ERS and MERS plans.

Management's Discussion and Analysis

Assets, Liabilities and Fiduciary Net Assets – All Plans
(in millions)

	June 30, 2012	June 30, 2011
Assets:		
Cash and cash equivalents	$ 3.1	$ 3.5
Investments	7,225.0	7,440.1
Contributions and other receivables	60.7	46.6
Property and equipment	.5	2.3
Total assets	7,289.3	7,492.5
Liabilities:		
Accounts payable and other liabilities	4.8	3.6
Total liabilities	4.8	3.6
Net assets:	$ 7,284.5	$ 7,488.9

Summary of Changes in Fiduciary Net Assets – All Plans
(in millions)

	Year Ended June 30, 2012	Year Ended June 30, 2011
Additions:		
Contributions	$ 582.7	$ 520.6
Net investment gain (loss)	115.6	1,256.8
Miscellaneous revenue		
Total Additions	698.3	1,777.4
Deductions:		
Benefits	881.1	846.0
Refunds of contributions	12.9	11.2
Administrative expenses	8.7	8.4
Total Deductions	902.7	865.6
Increase (Decrease) in Net Assets:	(204.4)	911.8
Net Assets:		
Beginning of year	7,488.9	6,577.1
End of year	$ 7,284.5	$ 7,488.9

Management's Discussion and Analysis

Investments

The State Investment Commission (SIC) establishes long-term asset allocation policy and monitors investment performance of the plan. An asset/liability (A/L) study is conducted every two to three years to identify an optimal diversified investment portfolio that maximizes return within an acceptable level of risk. As long-term investors, the SIC is committed to its strategic asset allocation that has been developed as part of a comprehensive A/L study which incorporates capital market return expectations, risks and correlations associated with each asset class as well as the unique profile and objectives of the System. As a defined benefit plan, the System generally has a much longer time horizon than individual investors and is better positioned to withstand short-term volatility of the capital markets.

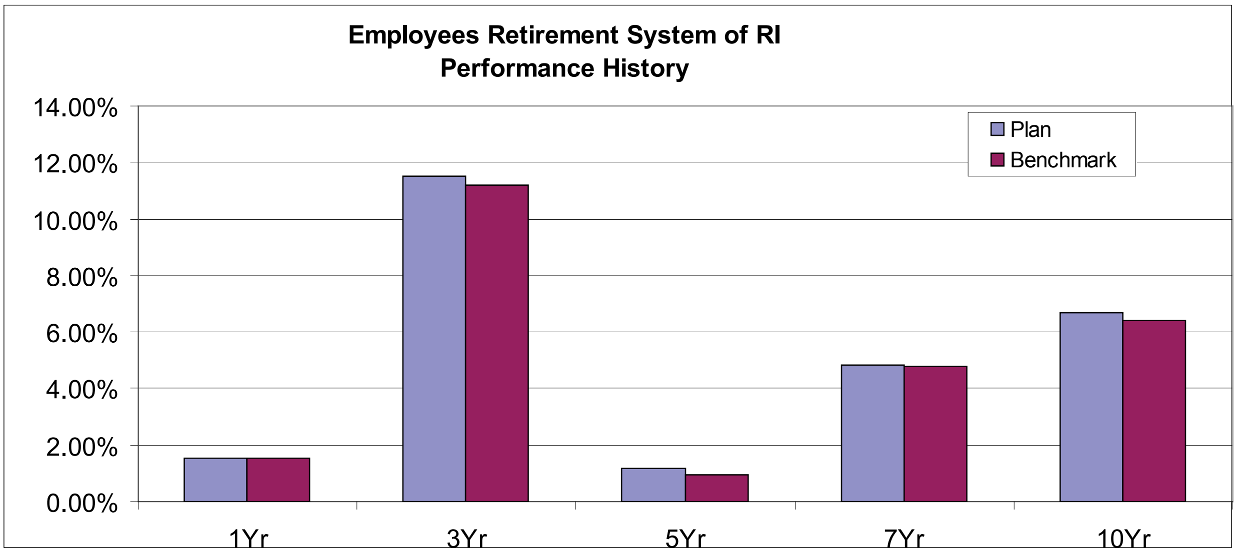
The State Investment Commission adopts and periodically adjusts asset allocation targets in major asset categories – domestic and international equity, fixed income, real return, alternative investments, and real estate. Investment managers are engaged to manage portions of the portfolio and performance is measured in relation to benchmarks adopted for each asset category. A composite benchmark, based on weighted asset allocations, is used to measure manager and overall portfolio performance.

The allocation of assets among stocks, bonds and alternative investments can have a significant impact on investment performance. In light of its long time horizon, the SIC is able to take advantage of historical long-term return opportunities offered by equity and other long-term investments.

Management's Discussion and Analysis

Investment Performance

The System's one-year, time weighted rate of return was 1.55% which was even with the composite benchmark. The three-year average was 11.53% which was 34bps better than the 11.19% benchmark return, and the five-year average was 1.19% which was 22bps better than the .97% benchmark return.



The composite benchmark is weighted based on asset allocation targets. It is currently comprised: 52% MSCI World Free; 20% Barclay's Aggregate; 11% CPI + 4%; 7.5% S&P 500 + 3%; 5% NCREIF Property Index Lagged; and 4.5% 91 day Treasury Bills. The composite benchmark for each of the years shown in the chart reflects the asset allocation targets in place for that fiscal year and the related indices used to measure performance.

The System's actuarial investment return assumption is 7.50%. The actuarial value of assets is determined based on a five-year smoothing methodology.

During the Fiscal Year ended June 30, 2012, the State Investment Commission began using hedge funds as a risk management tool within the pooled investment trust. An overall portfolio allocation to hedge funds was set at 15% - hedge funds are used within various asset allocation categories.

Funded Status

Independent actuarial valuations are conducted of the System each year. As part of this valuation, the progress toward funding pension obligations of the System is measured by comparing the actuarial value of assets to the actuarial accrued liability. This measure is referred to as the funded ratio or funded status.

Management's Discussion and Analysis

The most recent actuarial valuations of the plans within the System were performed as of June 30, 2011. Those actuarial valuations reflect both significant changes in actuarial assumptions as adopted by the Retirement Board and the enactment of the Rhode Island Retirement Security Act on November 18, 2011. The changes in actuarial assumptions are more fully described in note 6 to the financial statements and note 2 to the required supplementary information schedules.

The objectives of the legislation included enhancing retirement security for plan members, improving the funded status of the plans within the System and stabilizing the projected increases in required employer contributions. The pension reform measures included:

- For General State and Municipal Employees and Teachers: changing the structure of the retirement program to a hybrid plan designed with a smaller defined benefit plan and a supplemental defined contribution plan.

- Changing the automatic cost of living adjustments (COLA) from a stated amount or CPI based COLA to a formula contingent on the actual investment performance over time.

- Suspending COLA when the funded ratio is lower than 80%. The ERS, Judicial and State Police Plans will be aggregated to determine if the 80% funded ratio has been met. When the COLA is suspended based on funded status, potential periodic COLA are provided every five years.

- Reamortizing the unfunded actuarial accrued liability to 25 years from the previous 19 year schedule.

- Preserving accumulated benefits earned by members (service credit multiplier) as of June 30, 2012.

- Aligning retirement eligibility ages to those for Social Security with a phased approach for those members who are vested (five years) as of June 30, 2012.

Changes in member benefit provision are effective on July 1, 2012.

As reflected in the most recent actuarial valuation (June 30, 2011), the funded ratio decreased to 57.4% for State Employees and 59.7% for Teachers within the Employees' Retirement System plan. The funded ratio for the Judicial plan increased to 86.1%. The State Police plan's funded ratio increased to 98.6%. The Municipal Employees' Retirement System plans' funded ratio (composite for all units) decreased to 84.3%.

Details of the funded status of each plan within the System are included in the Schedules of Funding Progress on page 40.

All employers participating in the System's plans contributed 100% of their annual required contribution during fiscal 2012.

Management's Discussion and Analysis

Future Contribution Rates and Economic Outlook

The fiscal 2013 employer contribution rates are all based upon the actuarial valuation performed at June 30, 2010. The enactment of the Rhode Island Retirement Security Act on November 18, 2011 resulted in restated actuarial valuations for the plans as of June 30, 2010. The employer contribution rates for fiscal 2013 are 21.18% for State employees, 19.29% for Teachers, 19.69% for Judges and 11.07% for State Police.

Effective July 1, 2012, as a result of the enactment of the Rhode Island Retirement Security Act, member contributions to the ERS (exclusive of correctional officers) and MERS plans within the System are reduced. Members also contribute to a newly implemented defined contribution plan, which supplements the existing defined benefit plan. For example, in fiscal 2012, state employee members contributed 8.75% of salary to the defined contribution plan – in fiscal 2013 member contributions to the defined benefit plan are reduced to 3.75% with the remaining 5% going to the defined contribution plan.

Contacting the System's Management

This discussion and analysis presentation is designed to provide a general overview of the System's financial activity. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Employees' Retirement System, 50 Service Avenue, Warwick, RI, 02886.

EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND
Statements of Fiduciary Net Assets
June 30, 2012

	ERS	MERS	SPRBT	JRBT	Memorandum Total
Assets					
Cash and cash equivalents (Note 4)	$ 1,869,869	$ 725,276	$ 433,205	$ 64,325	$ 3,092,675
Receivables					
Contributions	35,655,699	5,444,745	240,105	93,089	41,433,638
Due from State for teachers	16,350,185	-	-	-	16,350,185
Other	2,844,972	59,153	-	-	2,904,125
Total receivables	54,850,856	5,503,898	240,105	93,089	60,687,948
Investments at fair value - equity in pooled trust (Note 4)	5,944,742,651	1,159,396,926	79,826,919	41,058,860	7,225,025,356
Property and equipment at cost, net of accumulated depreciation (Note 5)	407,655	61,487	1,659	1,063	471,864
Total Assets	6,001,871,031	1,165,687,587	80,501,888	41,217,337	7,289,277,843
Liabilities					
Accounts Payable	3,889,272	868,903	28,994	14,339	4,801,508
Total Liablilities	3,889,272	868,903	28,994	14,339	4,801,508
Net assets held in trust for pension benefits (Schedules of funding progress for each plan as presented on page 40)	$ 5,997,981,759	$ 1,164,818,684	$ 80,472,894	$ 41,202,998	$ 7,284,476,335

The accompanying notes are an integral part of this financial statement.

EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND
Statements of Changes in Fiduciary Net Assets - Fiscal Year Ended June 30, 2012

	ERS	MERS	SPRBT	JRBT	Memorandum Total
Additions					
Contributions (Note 6)					
Member contributions	$ 149,682,600	$ 23,546,848	$ 1,699,879	$ 808,534	$ 175,737,861
Employer contributions	282,588,841	35,998,489	5,333,298	1,718,379	325,639,007
State contribution for teachers	80,385,930	-	-	-	80,385,930
Interest on service credits purchased	612,783	325,305	36,452	-	974,540
Total contributions	513,270,154	59,870,642	7,069,629	2,526,913	582,737,338
Investment Income					
Net appreciation in fair value of investments	17,882,510	4,294,235	432,068	182,631	22,791,444
Interest	65,296,894	12,542,119	817,297	432,414	79,088,724
Dividends	983,021	189,548	12,492	6,571	1,191,632
Other investment income	20,803,509	4,013,047	265,102	139,259	25,220,917
	104,965,934	21,038,949	1,526,959	760,875	128,292,717
Less investment expense	(10,446,922)	(2,016,903)	(133,498)	(70,031)	(12,667,354)
Net investment income	94,519,012	19,022,046	1,393,461	690,844	115,625,363
Total Additions	607,789,166	78,892,688	8,463,090	3,217,757	698,362,701
Deductions					
Benefits					
Retirement benefits	589,543,863	64,630,907	377,208	1,294,966	655,846,944
Cost of living adjustments	184,956,563	12,108,932	28,500	88,203	197,182,198
SRA Plus option	20,985,090	2,648,508	-	-	23,633,598
Supplemental benefits	1,061,420	-	-	-	1,061,420
Death benefits	2,824,800	585,600	-	-	3,410,400
Total benefits	799,371,736	79,973,947	405,708	1,383,169	881,134,560
Refund of contributions	10,166,105	2,770,982	-	-	12,937,087
Administrative expense (Note 7)	7,334,381	1,283,433	63,519	36,534	8,717,867
Total Deductions	816,872,222	84,028,362	469,227	1,419,703	902,789,514
Net Increase (Decrease)	(209,083,056)	(5,135,674)	7,993,863	1,798,054	(204,426,813)
Net assets held in trust for pension benefits					
Beginning of year	6,207,064,815	1,169,954,358	72,479,031	39,404,944	7,488,903,148
End of year	$ 5,997,981,759	$ 1,164,818,684	$ 80,472,894	$ 41,202,998	$ 7,284,476,335

The accompanying notes are an integral part of this financial statement.

1. System Description and Governance

The Employees' Retirement System of the State of Rhode Island (the System) acts as a common investment and administrative agent for pension benefits to be provided for four defined benefit retirement plans as listed below:

Plan Name	***Type of Plan***
Employees' Retirement System (*ERS*)	Cost-sharing multiple-employer defined benefit plan
Municipal Employees' Retirement System (*MERS*)	Agent multiple-employer defined benefit plan
State Police Retirement Benefits Trust (*SPRBT*)	Single-employer defined benefit plan
Judicial Retirement Benefits Trust (*JRBT*)	Single-employer defined benefit plan

Although the assets of the plans are commingled for investment purposes, each plan's assets are accounted for separately and may be used only for the payment of benefits to the members of that plan, in accordance with the terms of that plan.

The System's financial statements are included as Pension Trust Funds within the Fiduciary Funds in the Comprehensive Annual Financial Report of the State of Rhode Island and Providence Plantations. The accompanying financial statements are not intended to present the financial position and results of operations of the State.

The System is administered by the State of Rhode Island Retirement Board which was authorized, created and established in the Office of the General Treasurer as an independent retirement board to hold and administer, in trust, the funds of the retirement system. The fifteen members of the retirement board are: the general treasurer or his or her designee who shall be a subordinate within the general treasurer's office; the director of administration or his or her designee who shall be a subordinate within the department of administration; a representative of the budget office or his or her designee from within the budget office, who shall be appointed by the director of administration; the president of the league of cities and towns or his or her designee; two (2) active state employee members of the retirement system or officials from state employee unions to be elected by active state employees; two (2) active teacher members of the retirement system or officials from a teachers union to be elected by active teachers; one active municipal employee member of the retirement system or an official from a municipal employees union to be elected by active municipal employees; two (2) retired members of the retirement system to be elected by retired members of the system; and four (4) public members, all of whom shall be competent by training or experience in the field of finance, accounting or pensions; two (2) of the public members shall be appointed by the governor, one of whom shall serve an initial term of three (3) years and one of whom shall serve an initial term of four (4) years and until his or her successor is appointed and qualified; and two (2) of the public members shall be appointed by the general treasurer, one of whom shall serve an initial term of three (3) years and one of whom shall serve an initial term of four (4) years and until his or her successor is appointed and qualified. Thereafter, the term of these four (4) public members shall be for four (4) years or until their successors are appointed and qualified by the Senate.

The System's purpose is to provide retirement benefits to state employees, public school teachers, certain general and public safety municipal employees, state police officers, and judges.

1. System Description and Governance (continued)

A summary of membership by plan as of the June 30, 2011 actuarial valuation follows:

	Retirees and beneficiaries	*Terminated plan members entitled to but not yet receiving benefits*	*Active Vested*	*Active Non-vested*	*Total by Plan*
ERS					
State Employees	11,271	2,650	8,756	2,477	25,154
Teachers	10,347	2,689	11,566	1,815	26,417
MERS					
General Employees	4,135	2,461	3,309	2,883	12,788
Public Safety	596	127	694	690	2,107
SPRBT	5	4	29	177	215
JRBT	12	-	10	44	66
Total by type	26,366	7,931	24,364	8,086	66,747

2. Plan Membership and Benefit Provisions

Membership and benefit provisions are outlined in the Rhode Island General Laws and are subject to modification by the General Assembly. Modifications to pension benefit and eligibility provisions have been made in recent years (2005, 2009, and 2010) as well as the comprehensive pension reform provisions contained in the Retirement Security Act enacted on November 18, 2011 and effective July 1, 2012. Accordingly, specific member retirement benefit and eligibility provisions vary depending upon a number of factors including years of service, age, and vesting provisions. The member benefit provisions outlined herein are a composite of enacted benefit provisions in effect for fiscal 2012. The provisions of the Retirement Security Act are effective July 1, 2012 (fiscal 2013) - those provisions are summarized immediately following the benefit provisions in effect for fiscal 2012.

EMPLOYEES' RETIREMENT SYSTEM (ERS)

The ERS was established and placed under the management of the Retirement Board for the purpose of providing retirement allowances for employees of the State of Rhode Island under the provisions of chapters 8 to 10, inclusive, of Title 36, and public school teachers under the provisions of chapters 15 to 17, inclusive, of Title 16 of the Rhode Island General Laws.

Plan members - The plan covers most State employees other than certain personnel at the State colleges and university (principally faculty and administrative personnel). The plan also covers teachers, including superintendents, principals, school nurses, and certain other school officials in the public schools in the cities and towns. Membership in the plan is mandatory for all covered state employees and teachers. Elected officials may become members on an optional basis and legislators may participate if elected to office prior to January 1, 1995.

2. Plan Membership and Benefit Provisions (continued)

Certain employees of the Rhode Island Airport Corporation (hired before July 1, 1993), the Rhode Island Economic Development Corporation (active contributing members and employees of the Department of Economic Development before October 31, 1995 who elected to continue membership) and, the Narragansett Bay Water Quality District Commission (members of a collective bargaining unit) are also covered and have the same benefits as State employees.

Plan vesting provisions – after ten years of service**.**

Retirement eligibility and plan benefits – are summarized in the following table:

Schedule		Retirement Eligibility	Benefit accrual rates	Maximum benefit
(A)	Completed 10 years of service on or before July, 1, 2005 and eligible to retire as of September 30, 2009	Age 60 with 10 years of service or after 28 years of service at any age	1.7% for each of first ten years 1.9% for each of next ten years 3.0% for each of next fourteen years 2% for the 35th year	80% of final average (3 consecutive highest years) earnings and 35 years of service
	Completed 10 years of service on or before July, 1, 2005 but ineligible to retire as of September 30, 2009	Minimum retirement age of 62 and ten years of service with a downward adjustment of the minimum retirement age based on the years of service credit as of September 30, 2009	Same accrual rates as (A) above to September 30, 2009 and then Schedule B rates (below) thereafter	80% of final average (5 consecutive highest years) earnings
(B)	Less than 10 years of service before July 1, 2005 and eligible to retire as of September 30, 2009	Age 65 with 10 years of service or after 29 years of service and age 59	1.6% for each of first ten years 1.8% for each of next ten years 2.0% for each of next five years 2.25% for each of next five years 2.5% for each of next seven years 2.25% for the 38th year	75% of final average earnings (3 consecutive highest years) and 38 years of service
	Less than 10 years of service before July 1, 2005 and ineligible to retire as of September 30, 2009	Age 65 with ten years of service, or age 62 with at least 29 years of service with a downward adjustment of the minimum retirement age based on the years of service credit as of September 30, 2009	Same as above	75% of final average earnings (5 consecutive highest years) and 38 years of service

State correctional officers may retire at age 50 with 20 years of service. However if not eligible to retire as of September 30, 2009, the minimum retirement age was modified to 55 with 25 years of service credit for correctional officers and registered nurses at the Department of Behavioral Healthcare, Developmental Disabilities, and Hospitals.

2. Plan Membership and Benefit Provisions (continued)

The plan provides for survivor's benefits for service-connected death and certain lump sum death benefits.

Joint and survivor options are available to members. The Service Retirement Allowance (SRA) Plus option provides for the payment of a larger benefit before the attainment of age sixty-two (62) and a reduced amount thereafter. The reduced amount is equal to the benefit before age sixty-two (62), including cost-of-living increases, minus the member's estimated social security benefit payable at age sixty-two (62).

Actuarially reduced retirement is available at age 55 and 20 years of service, the benefit is reduced actuarially for each month that the age of the member is less than sixty-five (65) years.

Cost of Living Adjustments – are summarized in the following table***:***

		Cost of Living Adjustment (COLA)
(A)	Completed 10 years of service on or before July, 1, 2005 and eligible to retire as of June 12, 2010	A COLA of 3% (compounded annually) payable on the third January after retirement.
(B)	Less than 10 years of service before July 1, 2005 and eligible to retire as of June 12, 2010	On the month following the third anniversary date of retirement, and on that month of each succeeding year, a COLA of 3% (compounded annually) or the percentage of increase in the Consumer Price Index, determined as of September 30 of the prior calendar year, whichever is less
	Category (A) or (B) **and** ineligible to retire as of June 12, 2010	A COLA of 3% (compounded annually) or the percentage of increase in the Consumer Price Index, determined as of September 30 of the prior calendar year, whichever is less applied to the first $35,000 of retirement allowance. The COLA shall commence upon the retiree's third anniversary of the date of retirement or when the retiree reaches age sixty-five (65), whichever is later. The $35,000 limit will increase annually by the percentage increase in the Consumer Price Index, determined as of September 30 of the prior calendar year or three percent (3%), whichever is less.

Disability retirement provisions - the plan also provides nonservice-connected disability benefits after five years of service and service-connected disability pensions with no minimum service requirement. Effective for applications filed after September 30, 2009, accidental disability will be available at 66 2/3% for members who are permanently and totally disabled as determined by the Retirement Board. If the disability is determined to be partial and the member is able to work in other jobs, the benefit will be limited to 50%. Disability benefits are subject to annual review by the Retirement Board.

Other plan provisions - Service credit purchases, excluding contribution refund paybacks and military service, requested after June 16, 2009 are calculated at full actuarial cost.

2. Plan Membership and Benefit Provisions (continued)

***Teachers Survivor Benefits* - t**he plan provides a survivor benefit to public school teachers in lieu of Social Security since not all school districts participate in the plan. The cost of the benefits provided by the plan are two percent (2%) of the member's annual salary up to but not exceeding an annual salary of $9,600; one-half (1/2) of the cost is contributed by the member by deductions from his or her salary, and the other half (1/2) is contributed and paid by the respective school district by which the member is employed. These contributions are in addition to the contributions required for regular pension benefits.

Spouse, parents, family and children's benefits are payable following the death of a member. A spouse shall be entitled to benefits upon attaining the age of sixty (60) years. Children's benefits are payable to the child, including a stepchild or adopted child of a deceased member if the child is unmarried and under the age of eighteen (18) years or twenty-three (23) years and a full time student, and was dependent upon the member at the time of the member's death. Family benefits are provided if at the time of the member's death the surviving spouse has in his or her care a child of the deceased member entitled to child benefits. Parents benefits are payable to the parent or parents of a deceased member if the member did not leave a widow, widower, or child who could ever qualify for monthly benefits on the member's wages and the parent has reached the age of 60 years, has not remarried, and received support from the member. In January, a yearly cost-of-living adjustment for spouse's benefits is paid and based on the annual social security adjustment.

The Teachers Survivor Benefits Fund provides benefits based on the highest salary at the time of retirement of the teacher. Benefits are payable in accordance with the following table:

Highest Annual Salary	Spousal Monthly Minimum Benefit
$17,000 or less	$ 750
$17,001 to $25,000	$ 875
$25,001 to $33,000	$ 1,000
$33,001 to $40,000	$ 1,125
$40,001 and over	$ 1,250

Benefits payable to children and families are equal to the spousal benefit multiplied by the percentage below:

Parent and 1 Child	Parent and 2 or more Children	One Child Alone	Two Children Alone	Three or more Children Alone
150%	175%	75%	150%	175%

Rhode Island Retirement Security Act of 2011(RIRSA) - Effective July 1, 2012 the defined benefit plan for state employees and teachers has been transitioned into a combination defined benefit/defined contribution plan. For state employees, the employee contribution rate for the defined benefit plan is reduced from 8.75% to 3.75% with 5.00% for the defined contribution plan. The employer rate for the defined benefit plan is actuarially determined and the employer rate for the defined contribution plan is 1%.

2. Plan Membership and Benefit Provisions (continued)

For teachers the employee contribution rate for the defined benefit plan will be 3.75% and 5.00% (or 7.00% for employees of school departments that do not participate in Social Security) for the defined contribution plan. The employer rate for the defined benefit plan is actuarially determined and the employer rate for the defined contribution plan is 1.00% (or 3.00% for school departments that do not participate in Social Security).

Members who had 10 years of contributory service prior to July 1, 2005 and were not eligible to retire as of September 30, 2009 or June 30, 2012, the retirement eligibility age becomes the Social Security Normal Retirement Age (SSNRA) with a proportional downward adjustment based upon service credit as of June 30, 2012. Effective July 1, 2012 the new retirement age will mirror the SSNRA not to exceed age 67.

The Cost of Living Adjustment (COLA) has been suspended until the collective ERS, SPRBT, and JRBT plans reach a funded status of 80%. The COLA provision can be reviewed in a five year interval. When the collective funding level of the plans exceeds 80%, eligible retirees may receive a COLA annually effective on their date of retirement plus one month. The COLA will be calculated as the five (5) year smoothed investment rate of return less 5.50%, with a 0.00% floor and a 4.0% cap. COLA will be delayed until the later of the SSNRA or three years after retirement. The COLA will be applied to the first $25,000 of benefits indexed annually.

Members will become vested in the defined benefit plan once they have obtained five years of contributing service. Active members with at least five years of contributing service on July 1, 2012 will become vested in the defined benefit plan. All benefit accruals accumulated as of June 30, 2012 will be frozen. Effective July 1, 2012 members will receive a benefit accrual of 1.0% per year based on the five year average compensation.

MUNICIPAL EMPLOYEES' RETIREMENT SYSTEM (MERS)

The MERS was established under the Rhode Island General Laws and placed under the management of the Retirement Board to provide retirement allowances to employees of municipalities, housing authorities, water and sewer districts, and municipal police and fire persons that have elected to participate.

Plan members – A summary of participating employers is listed below:

Municipalities, housing authorities, water and sewer districts	68
Municipal police and fire departments	43
Total participating units as of the actuarial valuation at June 30, 2011	111

Plan vesting provisions – after ten years of service.

2. Plan Membership and Benefit Provisions (continued)

Retirement eligibility and plan benefits –

The plan generally provides retirement benefits equal to 2% of a member's final average salary multiplied by the number of years of total service up to a maximum of 75%. Such benefits are available to members at least age 58 with 10 years of service or after 30 years of service at any age.

Joint and survivor options are available as well as the Service Retirement Allowance (SRA) Plus option that provides for the payment of a larger benefit before the attainment of age sixty-two (62) and a reduced amount thereafter. The reduced amount is equal to the benefit before age sixty-two (62), including cost-of-living increases, minus the member's estimated social security benefit payable at age sixty-two (62).

Police and fire personnel may retire at age 55 if they have 10 years of service or after 25 years of service at any age. An option may be elected to provide a 20 year service pension with a benefit equal to 2.5% for each year of service up to a maximum of 75% for police and fire personnel. Benefits are based on the average of the highest three consecutive years' earnings, exclusive of overtime.

The plan also provides survivor's benefits; and certain lump sum death benefits.

Cost of Living Adjustments – An optional cost-of-living provision may be elected for police and fire personnel and general employees.

Disability retirement provisions - The plan also provides nonservice-connected disability benefits after 5 years of service; service-connected disability pensions with no minimum service requirement.

Rhode Island Retirement Security Act of 2011(RIRSA)

General Employees - Effective July 1, 2012 the defined benefit plan for general municipal employees has been transitioned into a combination defined benefit/defined contribution plan. The employee contribution rate for the defined benefit plan will be 1.0% (2.0% for organizations that have a COLA provision) and 5.00% (or 7.00% for organizations that do not participate in Social Security) for the defined contribution plan. The employer rate for the defined benefit plan will be actuarially determined. The employer rate for the defined contribution plan will be 1.0% (or 3.00% for the organizations that do not participate in Social Security).

The new retirement age will mirror Social Security Normal Retirement Age (SSNRA) not to exceed age 67. The Cost of Living Adjustment (COLA) has been suspended for any unit whose funding level is less than 80%. The COLA provision can be reviewed in a five year interval. When the funding level of a plan exceeds 80% funded eligible retirees may receive a COLA annually effective on their date of retirement plus one month. The COLA will be calculated as the five (5) year smoothed investment rate of return less 5.50%, with a 0.00% floor and a 4.0% cap. COLA will be delayed until the later of the SSNRA or three years after retirement. The COLA will be applied to the first $25,000 of benefits indexed annually.

2. Plan Membership and Benefit Provisions (continued)

Members will become vested in the defined benefit plan once they have obtained five years of contributing service. Active members with at least five years of contributing service on July 1, 2012 will become vested in the defined benefit plan. Benefit accruals accumulated as of June 30, 2012 will be frozen. Effective July 1, 2012 members will receive a benefit accrual of 1.0% per year based on the five year average compensation.

Police and Fire - Effective July 1, 2012 created a combined defined benefit and defined contribution plans for employer organizations that do not participate in social security. For organizations that participate in social security a defined benefit plan will remain. The employee contribution rate for the defined benefit plan will be 7.0% (8.0% for organizations that have a COLA provision) and the defined contribution rate will be 3.0% if the organization does not participate in social security. The employer rates will be actuarially determined for the defined benefit plan and the employer defined contribution rate will be 3.0% if the organization does not participate in social security.

The new retirement age will be 55 years old with 25 years of total service or for members with five years of service but less than 25 years of service the new retirement age will mirror the Social Security Normal Retirement Age (SSNRA) not to exceed 67.

As of June 30, 2012 members will continue to have a frozen benefit accrual of 2.0% per year for a standard 25 year with any age and out plan; 2.5% for a standard 20 year with any age and out plan. After July 1, 2012 the optional 20 and 25 year with retirement at any age plans will be eliminated. The benefit accrual for all plans will be 2.0% per year based on the five year average compensation. Members will become vested in the defined benefit plan once they have obtained five years of contributing service. Active members with at least five years of contributing service on July 1, 2012 will become vested in the defined benefit plan.

The Cost of Living Adjustment (COLA) has been suspended for any unit whose funding level is less than 80%. The COLA provision can be reviewed in a five year interval. When the funding level of a plan exceeds 80% funded eligible retirees may receive a COLA annually effective on their date of retirement plus one month. The COLA will be calculated as the five (5) year smoothed investment rate of return less 5.50%, with a 0.00% floor and a 4.0% cap. COLA will be delayed until the later of age 55 or three years after retirement. The COLA will be applied to the first $25,000 of benefits indexed annually.

STATE POLICE RETIREMENT BENEFITS TRUST (SPRBT)

The State Police Retirement Benefits Trust was established under Rhode Island General Law Section 42-28-22.1 and was placed under the management of the Retirement Board for the purpose of providing retirement allowances to State Police.

Plan members – the plan covers all State Police and Superintendents hired after July 1, 1987.

2. Plan Membership and Benefit Provisions (continued)

Retirement eligibility and plan benefits –

The plan generally provides retirement benefits equal to 50% of final salary after 20 years of service, plus 3.0% of final salary times service in excess of 20 years through 25 years to a maximum of 65% of final salary. Such benefits are available to members after 20 years of service regardless of age. The Superintendent of the State Police will receive 50% of his/her final salary and may retire after attainment of age 60 and 10 years of service.

The General laws were amended such that any member of the state police, other than the superintendent, who is hired on or after July 1, 2007 and who has served for twenty-five (25) years shall be entitled to a retirement allowance of 50% of the final salary. In addition, any member may serve up to a maximum of 30 years, and shall be allowed an additional amount equal to 3.0% for each completed year served after 25 years to a maximum retirement allowance not to exceed 65% of the final salary.

Benefits are based on the final base salary earned at retirement including longevity increment, holiday pay, clothing allowance and up to 400 overtime hours.

Cost of Living Adjustments – a cost-of-living adjustment of $1,500 per annum beginning on January 1st of the year in which a member attains his/her third anniversary of retirement is provided to all members.

Disability retirement provisions - the plan provides nonservice-connected disability benefits after 10 years of service and service-connected disability pensions with no minimum service requirement.

Rhode Island Retirement Security Act of 2011(RIRSA) - for state police, the retirement age is extended to 25 years of service for officers with fewer than twenty (20) years of service on June 30, 2012.

The Cost of Living Adjustment (COLA) has been suspended until the collective ERS, SPRBT, and JRBT plans reach a funded status of 80%. The COLA provision can be reviewed in a five year interval. When the collective funding level of the plans exceeds 80%, eligible retirees may receive a COLA annually effective on their date of retirement plus one month. The COLA will be calculated as the five (5) year smoothed investment rate of return less 5.50%, with a 0.00% floor and a 4.0% cap. COLA will be delayed until the later of age 55 or three years after retirement. The COLA will be applied to the first $25,000 of benefits indexed annually.

JUDICIAL RETIREMENT BENEFITS TRUST (JRBT)

The Judicial Retirement Benefits Trust was established under Rhode Island General Laws 8-8.2-7; 8-3-16; 8-8-10.1; 28-30-18.1; and was placed under the management of the Retirement Board for the purpose of providing retirement allowances to Justices of the Traffic Tribunal, Supreme, Superior, Family, District and Workers Compensation courts.

Plan members – the plan covers all Judges appointed after December 31, 1989.

2. Plan Membership and Benefit Provisions (continued)

Retirement eligibility and plan benefits **–** are summarized in the following table:

	Retirement benefit
Judges appointed after December 31, 1989 but before July 2, 1997	75% of the final salary at the time of retirement after 20 years of service, or 10 years of service and attainment of age 65. Judges retiring after 20 years of service after age 65 or 15 years of service after age 70 receive full retirement benefits, which is the final salary at time of retirement.
Judges appointed after July 2, 1997 but before January 1, 2009	Same as above except, salary is the average highest three (3) consecutive years of compensation rather than final salary.
Judges appointed after January 1, 2009 but before July 1, 2009	Judges with 20 years of service after age 65 or judges with 15 years of service after age 70 will receive 90% of the average of the highest three consecutive years of compensation. Judges appointed on or after January 1, 2009 with 10 years of service and age 65 or 20 years of service at any age are entitled to a reduced benefit of 70% of the average highest three consecutive years of compensation. Judges designating a survivor benefit with 20 years of service and age 65 or 15 years of service and age 70 receive a reduced benefit equal to 80% of the average highest three consecutive years of compensation. Judges designating a survivor benefit with 10 years of service after age 65 or 20 years of service at any age receive a reduced benefit equal to 60% of the average highest three consecutive years of compensation.
Judges appointed after July 1, 2009	Judges with 20 years of service after age 65 or with 15 years of service after age 70 will receive 80% of the average of the highest five consecutive years of compensation. Judges with 10 years of service and age 65 or 20 years of service at any age are entitled to a reduced benefit of 65% of the average highest five consecutive years of compensation. Judges designating a survivor benefit with 20 years of service and age 65 or 15 years of service and age 70 receive a reduced benefit equal to 70% of average highest five consecutive years of compensation. Judges designating a survivor benefit with 10 years of service after age 65 or 20 years of service at any age receive a reduced benefit equal to 55% of average highest five consecutive years of compensation.

Certain survivor benefits are also provided to judges who are plan members, which is 50% of the benefit amount payable to the judicial member.

Cost of Living Adjustments **–** are summarized in the following table***:***

2. Plan Membership and Benefit Provisions (continued)

	Cost of Living Adjustment (COLA)
Plan members eligible to retire on or before June 12, 2010	Supreme, Superior, Family and District Court Judges, - a COLA of 3% (not compounded) payable on the third January after retirement. Traffic Tribunal and Workers' Compensation Court Judges, a COLA of 3% (compounded annually) payable on the third January after retirement.
Plan members not eligible to retire on or before June 12, 2010	Supreme, Superior, Family and District Court Judges, - a COLA equal to the lesser of their original benefit and the COLA limit in effect in the year the member retires, multiplied by the percentage increase in CPI up to a maximum of 3.0% per year of 3% (not compounded) payable upon the later of their third anniversary of retirement or when the member reaches age 65. The applicable annual COLA limit will initially be $35,000, and increase annually by the percentage increase in the Consumer Price Index (CPI) up to a maximum of 3.0% per year. No COLA is paid on the annual benefit in excess of this limit. The annual increase in the COLA limit is be determined on a compound basis. Traffic Tribunal and Workers' Compensation Court Judges – same as above except the COLA is paid on a compound basis.

Rhode Island Retirement Security Act of 2011(RIRSA) - Effective July 1, 2012, the employee contribution rate for judges increased to 12% of salary per year.

The Cost of Living Adjustment (COLA) has been suspended until the collective ERS, SPRBT, and JRBT plans reach a funded status of 80%. The COLA provision can be reviewed in a five year interval. When the collective funding level of the plans exceeds 80%, eligible retirees may receive a COLA annually effective on their date of retirement plus one month. The COLA will be calculated as the five (5) year smoothed investment rate of return less 5.50%, with a 0.00% floor and a 4.0% cap. COLA will be delayed until the later of the SSNRA or three years after retirement. The COLA will be applied to the first $25,000 of benefits indexed annually.

3. Summary of Significant Accounting Policies

These financial statements were prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). The Governmental Accounting Standards Board (GASB) is responsible for establishing generally accepted accounting principles for defined benefit pension plans established by governmental entities. In accordance with GASB Statement No. 20, in the absence of specific guidance from a GASB pronouncement, pronouncements of the Financial Accounting Standards Board (FASB) issued on or before November 30, 1989 have been followed.

Basis of Accounting - The financial statements of the System are prepared on the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded when incurred.

3. Summary of Significant Accounting Policies (continued)

Cash and Cash Equivalents - Cash represents cash held in trust in a financial institution. Cash equivalents are highly liquid investments with a maturity of three months or less at the time of purchase.

Investments - Investment transactions are recorded on a trade date basis. Gains or losses on foreign currency exchange contracts are included in income consistent with changes in the underlying exchange rates. Dividend income is recorded on the ex-dividend date.

Method Used to Value Investments - Investments are recorded in the financial statements at fair value. Fair value is the amount that a plan can reasonably expect to receive for an investment in a current sale between a willing buyer and a willing seller - that is, other than a forced liquidation sale.

Short-term investments are generally carried at cost which approximates fair value.

The fair value of fixed income securities and domestic and international equity securities is generally based on published market prices and quotations from national security exchanges and securities pricing services.

Commingled funds consist of institutional domestic equity index, international equity index, and real estate funds. The fair value of the commingled funds is based on the reported net asset value (NAV) of the respective fund based upon the fair value of the underlying securities or assets held in the commingled fund.

Futures contracts are valued at the settlement price established each day by the board of trade or exchange on which they are traded.

The System also trades in foreign exchange contracts to manage exposure to foreign currency risks. Such contracts are used to purchase and sell foreign currency at a guaranteed future price. The change in the estimated fair value of these contracts, which reflects current foreign exchange rates, is included in the determination of the fair value of the System's investments.

Other investments that are not traded on a national security exchange (primarily private equity and real estate investments) are generally valued based on audited December 31 net asset values adjusted for (1) cash flows for the period January 1 to June 30 (which principally include additional investments and partnership distributions), and (2) significant changes in fair value as determined or estimated by the general partners as of June 30. The general partners estimate the fair value of the underlying investments held by the partnership periodically. Publicly traded investments held by the partnerships are valued based on quoted market prices. If not publicly traded, the fair value is determined by the general partner. Financial Accounting Standards Board ASC Topic 820, *Fair Value Measurements and Disclosures,* requires private equity and real estate limited partnership general partners to value non-publicly traded assets at current fair value, taking into consideration the financial performance of the issuer, cash flow analysis, recent sales prices, market comparable transactions, a new round of financing, a change in economic conditions, and other pertinent information. ERSRI management considers the fair values reported by the general partners at June 30 in addition to the audited net asset values at December 31 adjusted for cash flows for the period January 1 to June 30 in determining the fair value of private equity and real estate investments on the financial statements of ERSRI.

3. Summary of Significant Accounting Policies (continued)

Private equity and real estate investments represented 8.5% and 3.7%, respectively of the total reported fair value of all ERSRI investments at June 30, 2012. Of the underlying holdings within private equity investments, approximately 15% were valued based on quoted market prices. The remaining underlying assets were valued generally following the objectives outlined above. Because these fair values were not determined based on quoted market prices, the fair values may differ from the values that would have been determined had a ready market for these investments existed.

Hedge funds are valued based on information provided by the fund manager and as verified by their respective third party administrator. Of the underlying holdings within the hedge funds approximately 63% were valued based on Tier 1 inputs (unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted investments) and 31% as Tier 2 inputs (other significant inputs, either directly or indirectly, at the measurement date such as a) quoted prices for similar assets or liabilities in active markets; b) quoted prices for identical or similar assets and liabilities in markets that are not active; c) observable inputs, other than quoted prices, for assets and liabilities; or d) inputs that are derived from or corroborated by observable market data by correlation or other means. The remaining underlying holdings within the hedge funds approximating 6% were valued based on Tier 3 inputs (unobservable inputs which are developed based on the best information available in the circumstances which might include the fund's own data).

Contributions - Plan member contributions are recognized in the period in which the wages, subject to required contributions, are earned for the performance of duties for covered employment. Employer contributions to each plan are recognized when due and the employer has made a formal commitment to provide the contributions.

Benefits - Benefits and refunds are recognized when due and payable in accordance with the terms of each plan.

Investment expenses – Investment management expenses are presented separately as a component of net investment income and include investment consultants, custodial fees and direct investment expenses allocated by managers. In some instances (hedge funds, private equity and real estate investments), investment related costs are not readily separable from investment income and consequently investment income is recorded net of related expenses.

Property and Equipment – These assets represent the Line of Business System and computer equipment recorded at cost. Depreciation is provided on a straight-line basis over the estimated useful lives, ten and five years respectively. Property and equipment is allocated to each plan based on its proportionate share of net assets. The System's capitalization threshold is $5,000.

Memorandum Total Columns - Total columns on the financial statements are captioned "memorandum only" to indicate that they are presented only to facilitate financial analysis. Data in these columns are not comparable to a consolidation. Inter-fund eliminations have not been made in the aggregation of this data.

3. Summary of Significant Accounting Policies (continued)

Use of Estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingencies. These estimates are subject to a certain amount of uncertainty in the near term, which could result in changes in the values reported for those assets in the statements of fiduciary net assets. Because of the inherent uncertainty in the valuation of privately held securities, the fair value may differ from the values that would have been used if a ready market for such securities existed, and the difference can be material. Estimates also affect the reported amounts of income/additions and expenses/deductions during the reporting period. Actual results could differ from these estimates.

Recently Issued Accounting Standards – The Governmental Accounting Standards Board issued Statement No. 67 – *Financial Reporting for Pension Plan*s and Statement No. 68 - *Accounting and Financial Reporting for Pensions,* which will impact the System's financial statements in future fiscal years. Management is determining the impact of these statements, specifically Statement No. 67 which is applicable to financial reporting for plans and is required to be implemented in fiscal 2014.

4. Cash Deposits and Investments

(a). Cash Deposits and Cash Equivalents

At June 30, 2012, the carrying amounts of the plans' cash deposits are listed below:

	ERS	MERS	SPRBT	JRBT	Total
Cash Deposits:					
Book balance	$ 1,869,869	$ 725,276	$ 433,205	$ 64,325	$ 3,092,675
Bank balance	$ 2,420,364	$ 875,981	$ 433,205	$ 64,325	$ 3,793,875

The bank and book balances represent the plans' deposits in short-term trust accounts which include demand deposit accounts and interest-bearing, collateralized bank deposit accounts. Of the bank balance, $2,176,994 is covered by federal depository insurance and the remainder representing interest-bearing collateralized bank deposits totaling $1,616,881 is collateralized (102%) with U.S. Treasury and agencies held by a third party custodian.

In accordance with Rhode Island General Law Chapter 35-10.1, depository institutions holding deposits of the State, its agencies or governmental subdivisions of the State shall, at a minimum, insure or pledge eligible collateral equal to one hundred percent of time deposits with maturities greater than sixty days. Any of these institutions that do not meet minimum capital standards prescribed by federal regulators shall insure or pledge eligible collateral equal to one hundred percent of deposits, regardless of maturity. None of the System's deposits were required to be collateralized at June 30, 2012 (excluding the collateralized interest-bearing deposits). However, the State Investment Commission has adopted a collateralization requirement for institutions holding the State's deposits. Financial institutions are required to pledge collateral equal to 102% of the deposit amounts that are not insured by federal depository insurance.

4. Cash Deposits and Investments (continued)

(b). Investments

The State Investment Commission oversees all investments made by the State of Rhode Island, including those made for the System. Investment managers engaged by the Commission, at their discretion and in accordance with the investment objectives and guidelines for the System, make certain investments. The General Treasurer makes certain short-term investments on a daily basis. Rhode Island General Law Section 35-10-11 (b)(3) requires that all investments shall be made in securities as would be acquired by prudent persons of discretion and intelligence who are seeking a reasonable income and the preservation of capital.

On July 1, 1992, the State Investment Commission pooled the assets of the ERS with the assets of the MERS for investment purposes only, and assigned units to the plans based on their respective share of market value. On September 29, 1994 and November 1, 1995, the assets of the SPRBT and the JRBT, respectively, were added to the pool for investment purposes only. The custodian bank holds assets of the System in a Pooled Trust and each plan holds units in the trust. The number of units held by each plan is a function of each plans' respective contributions to, or withdrawals from, the trust.

Investment expense is allocated to each plan based on the plan's units in the Pooled Trust at the end of each month.

The following table presents the fair value of investments by type that are held within the Pooled Trust at June 30, 2012:

Investment Type		Fair Value
Cash	$	15,561,337
Money Market Mutual Fund		148,465,699
US Government Securities		399,497,088
US Government Agency Securities		420,118,443
Collateralized Mortgage Obligations		26,499,391
Corporate Bonds		866,257,615
Domestic Equity Securities		140,764,076
International Equity Securities		7,703,389
Commingled Funds - Domestic Equity		2,186,537,659
Commingled Funds - International Equity		1,137,589,177
Hedge Funds		1,011,173,459
Private Equity		611,642,891
Real Estate		
Limited Partnerships		117,565,163
Commingled Funds		102,731,318
Real Estate Investment Trusts		48,672,651
	$	**7,240,779,356**
Net investment receivable (payable)		**(13,747,318)**
Payable to broker		**(2,006,682)**
Total Investments at Fair Value	**$**	**7,225,025,356**

4. Cash Deposits and Investments (continued)

(b). Investments

Consistent with a target asset allocation model adopted by the State Investment Commission, the System directs its investment managers to maintain well diversified portfolios by sector, credit rating and issuer using the prudent person standard, which is the standard of care employed solely in the interest of the participants and beneficiaries of the funds and for the exclusive purpose of providing benefits to participants and defraying reasonable expenses of administering the funds.

Specific manager performance objectives are outlined and generally stated in relation to a benchmark or relevant index. These guidelines also include prohibited investments, limitations on maximum exposure to a single industry or single issuer, a minimum number of holdings within the manager's portfolio and, for fixed income managers, minimum credit quality ratings and duration/maturity targets.

(c). Interest Rate Risk

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

Duration is a measure of a debt security's exposure to fair value changes arising from changes in interest rates. It uses the present value of cash flows, weighted for those cash flows as a percentage of the investment's full price. The System manages its exposure to interest rate risk by comparing each fixed income manager portfolio's effective duration against a predetermined benchmark index based on that manager's mandate. The fixed income indices currently used by the System are:

- Citigroup Broad Investment Grade Bond Index
- Barclays MBS Index
- Barclays Credit Index
- Credit Suisse First Boston Global High Yield Index
- Barclays US Tips Index

At June 30, 2012, no fixed income manager was outside of the policy guidelines.

The following table shows the System's fixed income investments by type, fair value and the effective duration at June 30, 2012:

Investment Type:		Fair Value	Effective Duration
US Government Securities	$	420,118,443	2.21
US Government Agency Securities		399,497,088	5.77
Collateralized Mortgage Obligations		26,499,391	3.47
Corporate Bonds		866,257,615	5.73
Total Fixed Income	$	1,712,372,537	4.86

4. Cash Deposits and Investments (continued)

(c). Interest Rate Risk

The System also invested in a short-term money market mutual fund (State Street Bank Institutional Liquid Reserves) that held investments with a weighted average maturity of 25 days.

The System invests in various mortgage-backed securities, such as collateralized mortgage obligations (CMO), interest-only and principal-only (PO) strips. They are reported in U.S. Government Agency Securities and Collateralized Mortgage Obligations in the table above. CMO's are bonds that are collateralized by whole loan mortgages, mortgage pass-through securities or stripped mortgage-backed securities. Income is derived from payments and prepayments of principal and interest generated from collateral mortgages. Cash flows are distributed to different investment classes or tranches in accordance with the CMO's established payment order. Some CMO tranches have more stable cash flows relative to changes in interest rates while others are significantly sensitive to interest rate fluctuations.

The System may invest in interest-only (IO) and principal-only strips (PO) in part to hedge against a rise in interest rates. Interest-only strips are based on cash flows from interest payments on underlying mortgages. Therefore, they are sensitive to pre-payments by mortgagees, which may result from a decline in interest rates. Principal-only strips receive principal cash flows from the underlying mortgages. In periods of rising interest rates, homeowners tend to make fewer mortgage prepayments.

(d). Credit Risk

The System manages exposure to credit risk generally by instructing fixed income managers to adhere to an overall target weighted average credit quality for the portfolio and by establishing limits on the percentage of the portfolio that is invested in non-investment grade securities. The System's exposure to credit risk as of June 30, 2012 is as follows:

Rating (1)	Collateralized Mortgage Obligations	US Government Agency Securities	Corporate Bonds
Aaa	$ 19,163,095	$ 420,118,443	$ 67,173,147
Aa	6,014,611		94,452,693
A			161,601,921
Baa	525,181		331,775,103
Ba	57,799		62,444,037
B	36,324		93,250,387
Caa			23,890,487
Ca			
Not Rated	702,381		31,669,842
Fair Value	$ 26,499,391	$ 420,118,443	$ 866,257,617

(1) Moody's Investors Service

4. Cash Deposits and Investments (continued)

(d). Credit Risk

During Fiscal 2012, Standard & Poors Investors Service downgraded the rating assigned to direct obligations of the United States government from AAA to AA+. Direct United States government obligations held within the System's Pooled Investment Trust, which totaled approximately $399 million at June 30, 2012 are not included in the above credit risk table based on Moody's ratings.

The System's investment in a short-term money market mutual fund (State Street Bank Institutional Liquid Reserves) was rated AAAm by Standard & Poors Investors Service.

(e). Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a System's investments in a single issuer. There is no single issuer exposure within the System's portfolio that comprises 5% of the overall portfolio.

(f). Custodial Credit Risk

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the System will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. At June 30, 2012 all securities were registered in the name of the System (or in the nominee name of its custodial agent) and were held in the possession of the System's custodial bank, State Street Bank and Trust.

(g). Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely impact the fair value of an investment. Portfolios are diversified to limit foreign currency and security risk. The System may enter into foreign currency exchange contracts to minimize the short-term impact of foreign currency fluctuations on foreign investments. The System's exposure to foreign currency risk at June 30, 2012, was as follows:

4. Cash Deposits and Investments (continued)

(g). Foreign Currency Risk

Currency	Commingled Fund	Foreign Cash	Foreign Currency Forward Contracts	Equities	Private Equity	Total
Australian Dollar	$ 66,140,115	$ (84,660)	$ 164,614	$ -	$ -	$ 66,220,069
Brazilian Real	35,301,351	-		888,801	-	36,190,151
Canadian Dollar	90,715,071	(413,894)	53,950	395,825	12,711,154	103,462,106
Chilean Peso	5,238,548	-		-	-	5,238,548
Colombian Peso	3,475,728	-		-	-	3,475,728
Czech Koruna	749,246	-		-	-	749,246
Danish Krone	9,008,394	-		-	-	9,008,394
Egyptian Pound	801,480	-		-	-	801,480
Euro Currency	204,787,515	(820,890)	227,297	1,181,270	84,854,339	290,229,531
Hong Kong Dollar	69,870,604	(17,151)	489	1,791,124		71,645,066
Hungarian Forint	775,372	-		-	-	775,372
Indian Rupee	17,482,292	-		-	-	17,482,292
Indonesian Rupiah	7,365,131	-		-	-	7,365,131
Israeli Shekel	4,564,205	-		-	-	4,564,205
Japanese Yen	165,039,943	(376,138)	(86,653)	-	-	164,577,152
Malaysian Ringgit	9,660,132	-		-	-	9,660,132
Mexican Peso	13,421,816	-		-	-	13,421,816
Moroccan Dirham	253,397	-		-	-	253,397
New Taiwan Dollar	29,457,703	-		-	-	29,457,703
New Zealand Dollar	909,649	-		-	-	909,649
Norwegian Krone	7,099,327	-		-	-	7,099,327
Peruvian Nouveau Sol	173,170	-		-	-	173,170
Philippine Peso	2,568,639	-		-	-	2,568,639
Polish Zloty	3,883,250	-		-	-	3,883,250
Pound Sterling	177,543,521	(288,823)	101,621	3,446,369	-	180,802,688
Singapore Dollar	13,979,735	-		-	-	13,979,735
South African Rand	21,313,544	-		-	-	21,313,544
South Korean Won	40,411,087	-		-	-	40,411,087
Swedish Krona	23,575,465	(5,126)	36,255		94,593	23,701,187
Swiss Franc	64,514,985	-		-	-	64,514,985
Thailand Baht	5,954,058	-		-	-	5,954,058
Turkish Lira	4,528,409	-		-	-	4,528,409
	$ 1,100,562,881	$ (2,006,682)	$ 497,573	$ 7,703,389	$ 97,660,086	$ 1,204,417,247
US Dollar	37,026,296					
Commingled Fund Total	$ 1,137,589,177					

In addition to the foreign currency exposure highlighted in the foregoing table, certain hedge fund investments also have foreign currency exposure.

4. Cash Deposits and Investments (continued)

(h). Derivatives and Other Similar Investments

Certain of the System's investment managers are allowed to invest in derivative type transactions consistent with the terms and limitations governing their investment objective and related contract specifications. Derivatives and other similar investments are financial contracts whose value depends on one or more underlying assets, reference rates, or financial indices.

The System's derivative investments include forward foreign currency transactions, futures contracts, options, rights and warrants. The System enters into these transactions to enhance performance, rebalance the portfolio consistent with overall asset allocation targets, gain or reduce exposure to a specific market, or mitigate specific risks.

Forward foreign currency contracts – The System enters into foreign currency exchange contracts to minimize the short-term impact of foreign currency fluctuations on foreign investments. A currency forward is a contractual agreement to pay or receive specific amounts of foreign currency at a future date in exchange for another currency at an agreed upon exchange rate. These contracts involve risk in excess of the amount reflected in the System's Statements of Fiduciary Net Assets. The face or contract amount in U.S. dollars reflects the total exposure the System has in currency contracts. The U.S. dollar value of forward foreign currency contracts is determined using forward currency exchange rates supplied by a quotation service. Losses may arise due to changes in the value of the foreign currency or if the counterparty does not perform under the contract.

Futures contracts – The System uses futures to manage its exposure to the domestic and international equity, money market, and bond markets and the fluctuations in interest rates and currency values. Futures are also used to obtain target market exposures in a cost effective manner and to narrow the gap between the System's actual physical exposures and the target policy exposures. Using futures contracts in this fashion is designed to reduce (or hedge) the risk of the actual plan portfolio deviating from the policy portfolio more efficiently than by using physical securities. The program is only used to manage intended exposures and asset allocation rebalancing.

Buying futures tends to increase the System's exposure to the underlying instrument. Selling futures tends to decrease the System's exposure to the underlying instrument, or hedge other System investments. Losses may arise due to movements in the underlying or reference markets.

Through commingled funds, the System also indirectly holds derivative type instruments, primarily equity index futures.

The System invests in mortgage-backed securities, which are included in the categories described as collateralized mortgage obligations and U.S. Government Agency Securities in Note 3(b). These securities are based on the cash flows from interest and principal payments by the underlying mortgages. As a result, they are sensitive to prepayments by mortgagees, which are likely in declining interest rate environments, thereby reducing the value of these securities.

4. Cash Deposits and Investments (continued)

(h). Derivatives and Other Similar Investments

Additional information regarding interest rate risks for these investments is included in Note 4(c) *Interest Rate Risk.*

The System may sell a security in anticipation of a decline in the fair value of that security or to lessen the portfolio allocation of an asset class. Short sales may increase the risk of loss to the System when the price of a security underlying the short sale increases and the System is obligated to deliver the security in order to cover the position.

The following summarize the System's exposure to specific derivative investments at June 30, 2012.

Investment Derivative Instruments	Change in fair value included in investment income	Fair Value at June 30, 2012		Notional Amount
Fixed income futures - long	$ 9,836,726	$ -		$ -
Fixed incomes futures - short	(207,297)	-		(22,846,125)
Foreign currency forward contracts	(923,660)	497,573	(a)	76,396,837
Index futures - long	13,893,774	-		83,924,771
Index futures - short	1,828,141	-		(28,280,940)
Warrants	(26,000)	6,500		325
Total	$ 24,401,682	$ 504,073		

(a) - Foreign Currency Forward Contracts:

Pending receivable	$ 584,226
Pending payable	(86,653)
Foreign currency forward contract asset (liability)	$ 497,573

The System is exposed to credit risk on foreign currency contracts that are in asset positions. The aggregate fair value of derivative instruments in asset positions at June 30, 2012 was $590,726 (including $497,573 related to foreign currency contracts). This represents the maximum loss that would be recognized if all counterparties failed to perform as contracted. Risk is mitigated by using a continuous linked settlement process.

The System executes (through its investment managers) derivative instruments with various counterparties. The credit ratings of these counterparties were Baa1 (Moody's) or better, one counterparty not rated by Moody's but is rated A+ by Fitch.

5. Property and Equipment

Property and equipment consist of the line of business system and computer equipment at historical cost. Balances at June 30, 2012 were as follows:

	ERS	MERS	SPRBT	JRBT	Total
Line of Business System	$ 15,544,862	$ 2,287,990	$ 38,780	$ 24,973	$ 17,896,605
Equipment	160,074	25,213	842	550	186,679
Property and Equipment	15,704,936	2,313,203	39,622	25,523	18,083,284
Accumulated Depreciation	(15,297,281)	(2,251,716)	(37,963)	(24,460)	(17,611,420)
Net Property and Equipment	$ 407,655	$ 61,487	$ 1,659	$ 1,063	$ 471,864

6. Contributions

Contribution requirements for plan members and employers are established pursuant to Rhode Island General Laws. Employers are required to contribute at an actuarially determined rate. Plan member contributions are fixed by statute.

(a). Funding Policy

The funding policies, as set forth in Rhode Island General Law, Section 36-10-2 and 45-21-42 provide for actuarially determined periodic contributions to the plans. The actuarial valuation uses the Entry Age Normal actuarial cost method. Under this method, the employer contribution rate is the sum of (i) the employer normal cost rate, and (ii) a rate that will amortize the unfunded actuarial liability. The valuation is prepared on the projected benefit basis, under which the present value, at the assumed rate of return (currently 7.5 percent), of each participant's expected benefit payable at retirement or death is determined, based on age, service, gender and compensation.

The employer contributions required to support the benefits of the Plan are determined following a level funding approach, and consist of a normal contribution and an accrued liability contribution. The normal contribution is determined using the "entry age normal" method. Under this method, a calculation is made to determine the rate of contribution which, if applied to the compensation of each individual member during the entire period of anticipated covered service, would be required to meet the cost of all benefits payable on his behalf. This method is commonly referred to as the Individual Entry Age Actuarial Cost Method.

The unfunded accrued liability contributions are determined by subtracting the actuarial value of assets from the actuarial accrued liability and amortizing the result over a period not to exceed 30 years from June 30, 1999 for actuarial valuations as of June 30, 2009 and prior. Beginning with the valuations performed as of June 30, 2010, the unfunded accrued liability is amortized over a twenty-five year period from June 30, 2010.

6. Contributions (continued)

(a). Funding Policy

The General Laws also require, in addition to the contributions provided for by the funding policy, for each fiscal year in which the actuarially determined state contribution rate for state employees and teachers is lower than that for the prior fiscal year, the governor shall include an appropriation to that system equivalent to twenty percent (20%) of the rate reduction to be applied to the actuarial accrued liability. The amounts to be appropriated shall be included in the annual appropriation bill and shall be paid by the general treasurer into the retirement system. The retirement system's actuary shall not adjust the computation of the annual required contribution for the year in which supplemental contributions are received; such contributions once made may be treated as reducing the actuarial liability remaining for amortization in the next following actuarial valuation to be performed.

The General Laws also require that for any fiscal year in which the State's actual general revenues exceed estimated amounts, the difference shall be paid to the ERS plan upon completion and release of the State's audited financial statements.

Beginning in Fiscal 2013, the Retirement Security Act provides for additional contributions to the System based on 5.5% of the value of contracts where the services performed by the contractor were previously performed by state employees.

(b). Contribution rates

Employer contribution rates for fiscal 2012 for all plans were developed based on actuarial valuations performed as of June 30, 2009. Employee contribution rates are statutorily determined. The table below displays the contribution rates for the year ended June 30, 2012:

Plan	Employee	Employer
ERS		
State Employees	8.75%	22.98%
Teachers	9.50%	
Municipal funded		13.23% (*12.55% for towns not participating in the 1990 early retirement incentive*)
State funded		9.09% (*8.64% for towns not participating in the 1990 early retirement incentive*)
MERS		
General Employees	6.00% (additional 1% with a cost-of-living adjustment)	68 Municipalities, housing authorities, water and sewer districts contributed various actuarially determined rates.
Public Safety	7.00% (additional 1% with a cost-of-living adjustment and /or 1% with a 20 year service plan), Cranston Police and Cranston Fire are contributing 10% due to special plan provisions	43 Municipal police and fire departments contributed various actuarially determined rates.
SPRBT	8.75%	25.39%
JRBT	8.75%	18.69%

6. Contributions (continued)
(b). Contribution rates

The actuarial assumptions and methods employed in the valuation of the plans performed as of June 30, 2009 (used to determine contribution rates for fiscal 2012) differ from those employed in the June 30, 2011 valuation (the most recent valuation performed of the plans). The notes to the required supplementary information describe changes to actuarial methods and assumptions**.** A summary of the actuarial assumptions used in the June 30, 2009 valuations of the plans is provided in table below:

Summary of Actuarial Assumptions Used in the June 30, 2009 Valuation

	ERS		**MERS**	**SPRBT**	**JRBT**
	State Employees	***Teachers***			
Actuarial Cost Method	Entry Age Normal – Ultimate Normal Cost Method				
Amortization Method	Level Percent of Payroll – Closed				
Equivalent Single Remaining Amortization Period	20 years	20 years	20 Years	20 years	20 years
Asset Valuation Method	5 Year Smoothed Market				
Actuarial Assumptions					
Investment Rate of Return	8.25%	8.25%	8.25%	8.25%	8.25%
Projected Salary Increases	4.50% to 9.00%	4.50% to 13.25%	*General Employees* 4.50% to 8.50% *Police & Fire Employees* 4.75% to 14.75%	4.50% to 12.50%	4.50%
Inflation	3.00%	3.00%	3.00%	3.00%	3.00%
Cost of Living Adjustments	Schedule A – ▪ members eligible at 9/30/09 - 3.0% compounded ▪ members not eligible at 9/30/09 - 2.5% [1] compounded Schedule B members – 2.5% [1] compounded	Schedule A – ▪ members eligible at 9/30/09 - 3.0% compounded ▪ members not eligible at 9/30/09 - 2.5% [1] compounded Schedule B members – 2.5% [1] compounded	3.0% Non-compounded with a few exceptions	$1,500 per annum	3.0%

Schedule A - ERS members are those with 10 years or more of contributory service on or before July 1, 2005.

Schedule B - ERS members are those with less than 10 years of contributory service on or before July 1, 2005.

Note 1 – Cost of Living Adjustments (COLA) are based on the actual Consumer Price Index or 3%, whichever is lower. For actuarial purposes, the actuary assumes a 2.5% COLA increase.

6. Contributions (continued)
(c). Funded Status and Funding Progress

The table below displays the funded status of each plan at June 30, 2011, the most recent actuarial valuation date:

	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age - (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a / b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b - a) / c)
ERS						
State Employees	$ 2,443,690,798	$ 4,255,362,463	$ 1,811,671,665	57.4%	$ 633,146,197	286.1%
Teachers	3,776,407,834	6,325,941,951	2,549,534,117	59.7%	1,002,656,294	254.3%
MERS	1,204,814,823	1,428,879,301	224,064,478	84.3%	305,394,098	73.4%
SPRBT	73,151,768	74,185,705	1,033,937	98.6%	19,711,694	5.2%
JRBT	40,105,919	46,594,407	6,488,488	86.1%	8,474,716	76.6%

The schedules of funding progress (page 40) , presented as required supplementary information (RSI), present multiyear trend information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the Actuarial Accrued Liabilities (AAL) for benefits. The notes to the required supplementary information describe changes to actuarial methods and assumptions as well as statutory benefit changes applicable to each of the valuation periods.

The June 30, 2011 actuarial valuations (as well as the prior June 30, 2010 actuarial valuations) reflect comprehensive changes to plan member benefit provisions which are effective beginning July 1, 2012 as enacted in the Retirement Security Act by the General Assembly on November 18, 2011.

For the June 30, 2011 actuarial valuation, the retirement rates were modified to be consistent with the retirement eligibility changes instituted by the Rhode Island Retirement Security Act of 2011. Members that were assumed to retire prior to the Act, but before the earliest allowable age under the Act, are assumed to retire once eligible.

For future cost of living benefit adjustments, the benefit adjustments are assumed to be suspended for approximately 16 years, except for the intermittent adjustment every fifth year.

A summary of the assumptions used in the June 30, 2011 actuarial valuations follows on the next page:

6. Contributions (continued)
(c). Funded Status and Funding Progress

Summary of Actuarial Assumptions Used in the June 30, 2011 Valuation

	ERS		MERS	SPRBT	JRBT
	State Employees	***Teachers***			
Actuarial Cost Method	Entry Age Normal - the Individual Entry Age Actuarial Cost methodology is used.				
Amortization Method	Level Percent of Payroll – Closed				
Equivalent Single Remaining Amortization Period	24 years	24 years	24 years	24 years	24 years
Asset Valuation Method	5 Year Smoothed Market				
Actuarial Assumptions					
Investment Rate of Return	7.50%	7.50%	7.50%	7.50%	7.50%
Projected Salary Increases	4.00% to 7.00%	4.00% to 12.75%	General Employees 4.00% to 8.00% Police & Fire Employees 4.25% to 14.25%	4.00% to 12.00%	4.00%
Inflation	2.75%	2.75%	2.75%	2.75%	2.75%
Cost of Living Adjustments [1]	COLA is equal to the average five-year fund asset performance (percent) greater than 5.5% up to a maximum of 4% - the COLA is to be applied to the first $25,000 of benefits, indexed over time (see note 2 below). COLA is delayed until the later of Social Security eligibility age or 3 years after retirement except for State Police and MERS Police and Fire for which the COLA is delayed until the later of age 55 or 3 years after retirement.				

Note 1 – Cost of Living Adjustments (COLA) in member benefit provisions prior to the enactment of pension reform legislation on November 18, 2011 will remain in effect through June 30, 2012.

For the MERS plan, a 2% COLA is assumed after July 1, 2012. For all other plans, a COLA of 2% is assumed only every five years until the plans achieve a 80% collective funded status in accordance with the law. It is assumed that the plans will not achieve the targeted 80% funded status for 16 years.

7. Administrative Expenses

Pursuant to General Law section 36-8-10.1, administrative costs of the System are financed through investment earnings up to a maximum of .175% of the average total investments before lending activities as reported in the annual report of the Auditor General for the next preceding five (5) fiscal years. Such amounts are transferred to a restricted receipt account within the State's general fund. Any unencumbered funds on June 30 of any fiscal year are credited to the plans in the same proportion as their contributions to the restricted receipt account.

8. Commitments

The State Investment Commission has committed to fund certain private equity and real estate investment managers at a predetermined subscription amount. Outstanding unfunded investment commitments at June 30, 2012 totaled $173 million. These commitments will be funded through cash available within the pooled investment trust generated through investment income and/or liquidation of other investments.

The System's investments in hedge funds are generally subject to "lock-up" provisions that limit (subject to certain exceptions) the ability to withdraw amounts previously invested for a period of one to two years after the initial investment. The System began investing in hedge funds during fiscal 2012 and consequently investments totaling $1,011,173,459 at June 30, 2012 are subject to these withdrawal limitation provisions.

9. Postemployment Healthcare Plan

Plan Description - The System contributes to the State Employees' defined benefit post-employment health care plan, a cost sharing multiple employer plan administered though the Rhode Island State Employees' and Electing Teachers OPEB System (OPEB System). The State of Rhode Island OPEB Board (Board) was authorized, created and established under Chapter 36-12.1 of the RI General Laws. The Board was established to independently hold and administer, in trust, the funds of the OPEB system. The plan provides medical benefits to certain retired employees of participating employers including the System.

Pursuant to legislation enacted by the General Assembly, a trust was established to accumulate assets and pay benefits and other costs associated with the OPEB system.

The OPEB system issues a stand-alone, publicly available financial report that includes the financial statements and required supplementary information. A copy of the report can be obtained from the Office of Accounts and Control, One Capitol Hill, Providence, RI 02903.

Funding Policy - RIGL Sections 36-12.1, 36-12-2.2, and 36-12-4 govern the provisions of the OPEB system. The contribution requirements of plan members, the State, and other participating employers are established and may be amended by the General Assembly. Active employees make no contribution to the OPEB plan. Employees who retired after October 1, 2008 must contribute 20% of the annual estimated benefit cost (working rate) or annual premium for Medicare supplemental coverage. Employees retiring before October 1, 2008 have varying co-pay percentages ranging from 0% to 50% based on age and years of service at retirement. Further information about the contributions of plan members can be found in the financial report of the OPEB system.

All participating employers are required by law to fund the actuarially determined annual required contribution (ARC), which for fiscal year 2012 was 6.86% of covered payroll. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The System's contribution to the plan for the years ended June 30, 2011 and June 30, 2012 were $175,528 and $183,867 respectively, which represents 100% of the annual required contribution.

10. Contingencies

Challenges to the 2009 and 2010 Pension Reform - A number of unions representing state employees and teachers filed a lawsuit in State court in May 2010 initially challenging and attempting to block the 2009 pension reforms enacted by the General Assembly and later amended the suit to include 2010 reforms. The 2005 reforms were not challenged. The State intends to vigorously contest the lawsuit. The defendant State officials filed a Motion for Summary Judgment on the claims set forth in the Amended Complaint, which was heard on July 18, 2011. Prior to the hearing, the parties stipulated that the only issue that would be presented to the Court during the hearing on the Motion would concern whether the statute created a contract between the state and its participants. The parties agreed that in the event that the Court concluded that the statute did create a contract, the remaining issues of whether the contract had been impaired and whether any such impairment was legally justified would be briefed and argued at a later date. On September 13, 2011, the Superior Court issued its decision in which it ruled that pension plan participants have a contractual right based on an implied-in-fact contract theory. Consistent with the parties' stipulation, the Court did not decide whether that contract had been impaired or whether any such impairment was legally justified. The defendants State officials believe the Superior Court's ruling was legally wrong. On October 3, 2011, Defendants filed a Petition for Issuance of a Writ of Certiorari and Supporting Memorandum of Law with the Rhode Island Supreme Court. Defendants also filed a motion through which they requested that the Supreme Court expedite its review of the Petition for Issuance of a Writ of Certiorari. On November 22, 2011, the Supreme Court denied the petition for Writ of Certiorari. The litigation is proceeding through discovery at this time.

Challenges to the 2011 Pension Reform - In June 2012, certain retiree groups and unions representing state and municipal employees who maintain they are current beneficiaries of ERSRI commenced five separate lawsuits in State court challenging the Rhode Island Retirement Security Act of 2011 ("RIRSA") enacted by the General Assembly. In each of the five cases, the plaintiffs alleged that RIRSA violates the Contract Clause, the Takings Clause and the Due Process Clause of the Rhode Island Constitution. In addition, in the *Rhode Island Public Employees' Retirement Coalition v. Chafee,* C.A. No. 12-3166 case, the plaintiffs also allege counts for promissory estoppel and breach of contract. The State intends to vigorously contest the lawsuit.

On August 17, 2012, the defendants filed a motion to dismiss the *Rhode Island Public Employees' Retirement Coalition v. Chafee,* C.A. No. 12-3166 case on the ground that Rhode Island's pension legislation does not create a contract with ERSRI participants and that general contract principles, such as implied contracts, cannot be used to determine whether a state statute creates a contract. In the remaining four cases, the defendants filed motions for more definite statements in which they argued that it is not clear from the plaintiffs' pleadings what purported contract or contract(s) plaintiffs allege have been impaired. The defendants also moved in the alternative and asked the Court to dismiss the remaining four cases if the Court concluded that the plaintiffs' purported contracts derive from Rhode Island's pension legislation. A hearing on defendants' motions is anticipated in late 2012.

An adverse judgment to the State rendered in the pension litigation could significantly increase both the unfunded liability under the plans with in the System and the State's actuarially determined annual required contribution.

11. Subsequent Event

On July 1, 2012, the State implemented a new defined contribution plan for ERS (exclusive of correctional officers) and MERS plan members to supplement the existing benefits available under the defined benefit plans. Plan member contributions to the defined benefit plans within the System are reduced compared to member contribution rates in effect for fiscal 2012.

Employees’ Retirement System of the State of Rhode Island

Required Supplementary Information

Schedules of Funding Progress

Schedules of Employer Contributions

EMPLOYEES' RETIREMENT SYSTEM OF THE STATE OF RHODE ISLAND

REQUIRED SUPPLEMENTARY INFORMATION

Schedules of Funding Progress

Actuarial Valuation Date		Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age - (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a / b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b - a) / c)
ERS (*State Employees*)							
6/30/2011		$ 2,443,690,798	$ 4,255,362,463	$ 1,811,671,665	57.4%	$ 633,146,197	286.1%
6/30/2010	***	2,532,090,798	4,234,045,007	1,701,954,209	59.8%	630,246,973	270.0%
6/30/2009		2,646,081,020	4,482,244,291	1,836,163,271	59.0%	605,872,460	303.1%
6/30/2008	**	2,700,368,568	4,331,504,516	1,631,135,948	62.3%	587,500,000	277.6%
6/30/2007		2,493,428,522	4,332,888,818	1,839,460,296	57.5%	660,044,273	278.7%
6/30/2006		2,256,979,077	4,131,157,601	1,874,178,524	54.6%	644,980,127	290.6%
ERS (*Teachers*)							
6/30/2011		$ 3,776,407,834	$ 6,325,941,951	$ 2,549,534,117	59.7%	$ 1,002,656,294	254.3%
6/30/2010	***	3,873,118,262	6,265,273,231	2,392,154,969	61.8%	989,236,951	241.8%
6/30/2009		4,008,931,337	6,900,963,108	2,892,031,771	58.1%	987,463,633	292.9%
6/30/2008	**	4,044,954,378	6,632,016,708	2,587,062,330	61.0%	985,898,174	262.4%
6/30/2007		3,737,981,686	6,750,125,236	3,012,143,550	55.4%	959,372,837	314.0%
6/30/2006		3,394,086,565	6,444,693,666	3,050,607,101	52.7%	914,985,746	333.4%
SPRBT							
6/30/2011		$ 73,151,768	$ 74,185,705	$ 1,033,937	98.6%	$ 19,711,694	5.2%
6/30/2010	***	65,760,284	73,048,680	7,288,396	90.0%	19,715,070	37.0%
6/30/2009		60,232,045	75,480,005	15,247,960	79.8%	17,096,202	89.2%
6/30/2008		54,927,390	69,029,513	14,102,123	79.6%	16,698,764	84.5%
6/30/2007	*	45,996,910	60,427,947	14,431,037	76.1%	15,836,354	91.1%
6/30/2006		36,314,689	42,216,142	5,901,453	86.0%	13,474,588	43.8%
JRBT							
6/30/2011		$ 40,105,919	$ 46,594,407	$ 6,488,488	86.1%	$ 8,474,716	76.6%
6/30/2010	***	38,074,287	46,641,701	8,567,414	81.6%	7,461,120	114.8%
6/30/2009		36,839,221	41,738,040	4,898,819	88.3%	6,843,454	71.6%
6/30/2008	**	34,670,394	38,115,602	3,445,208	91.0%	6,601,889	52.2%
6/30/2007	*	29,630,637	35,355,326	5,724,689	83.8%	6,451,666	88.7%
6/30/2006		23,873,009	27,504,102	3,631,093	86.8%	6,313,069	57.5%
MERS							
6/30/2011		$ 1,204,814,823	$ 1,428,879,301	$ 224,064,478	84.3%	$ 305,394,098	73.4%
6/30/2010	***	1,196,385,142	1,372,495,862	176,110,720	87.2%	305,813,678	57.6%
6/30/2009		1,196,366,995	1,355,652,690	159,285,696	88.3%	306,587,441	52.0%
6/30/2008		1,174,567,205	1,266,286,829	91,719,624	92.8%	304,952,020	30.1%
6/30/2007		1,064,615,664	1,179,233,489	114,617,825	90.3%	298,234,571	38.4%
6/30/2006		945,876,282	1,085,648,196	139,771,914	87.1%	281,291,831	49.7%

*** Reflects adoption of Rhode Island Retirement Security Act of 2011 enacted on November 18, 2011.

** Reflects adoption of Article 16 of Chapter 23 of the 2010 Public Laws enacted on June 12, 2010.

* Restated June 30, 2007 actuarial valuation after 2008 amendment to General Laws

See notes to required supplementary information.

EMPLOYEES' RETIREMENT SYSTEM OF THE STATE OF RHODE ISLAND

REQUIRED SUPPLEMENTARY INFORMATION

Schedules of Contributions From the Employers And Other Contributing Entity

ERS

Fiscal Year Ended June 30		State Employees		Teachers (State)		Teachers (Employers)	
		Annual Required Contribution	Percentage Contributed	Annual Required Contribution	Percentage Contributed	Annual Required Contribution	Percentage Contributed
2012		$ 153,448,309	100%	$ 80,385,930	100%	$ 126,395,672	100%
2011		126,560,644	100%	70,286,262	100%	113,422,000	100%
2010	**	123,547,738	100%	68,542,956	100%	109,566,352	100%
2009	*	126,297,706	100%	73,600,069	100%	115,234,100	100%
2008		131,560,248	100%	82,455,777	100%	122,906,860	100%
2007		118,300,522	100%	70,531,472	100%	109,415,227	100%

MERS

Fiscal Year Ended June 30	Annual Required Contribution	Percentage Contributed
2012	$ 35,998,489	100%
2011	29,469,064	100%
2010	31,269,020	100%
2009	33,514,681	100%
2008	33,415,530	100%
2007	26,697,326	100%

SPRBT

Fiscal Year Ended June 30	Annual Required Contribution	Percentage Contributed
2012	$ 5,333,298	100%
2011	3,786,553	100%
2010	3,590,615	100%
2009	3,340,746	100%
2008	3,720,281	100%
2007	4,038,828	100%

JRBT

Fiscal Year Ended June 30		Annual Required Contribution	Percentage Contributed
2012		$ 1,718,379	100%
2011		1,298,278	100%
2010	**	1,180,817	100%
2009	*	1,700,174	100%
2008		2,127,643	100%
2007		2,362,671	100%

* Reflects adoption of H5983Aaa, Article 7, Substitute A as amended, enacted on June 30, 2009

** Reflects adoption of Article 16 of Chapter 23 of the 2010 Public Laws enacted on June 12, 2010

See notes to required supplementary information.

1. Actuarial Assumptions and Methods

The information presented in the required supplementary information schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation, June 30, 2011, follows.

Summary of Actuarial Assumptions Used in the June 30, 2011 Valuation

	ERS		MERS	SPRBT	JRBT
	State Employees	*Teachers*			
Actuarial Cost Method	Entry Age Normal - the Individual Entry Age Actuarial Cost methodology is used.				
Amortization Method	Level Percent of Payroll – Closed				
Equivalent Single Remaining Amortization Period	24 years	24 years	24 years	24 years	24 years
Asset Valuation Method	5 Year Smoothed Market				
Actuarial Assumptions					
Investment Rate of Return	7.50%	7.50%	7.50%	7.50%	7.50%
Projected Salary Increases	4.00% to 7.00%	4.00% to 12.75%	General Employees 4.00% to 8.00% Police & Fire Employees 4.25% to 14.25%	4.00% to 12.00%	4.00%
Inflation	2.75%	2.75%	2.75%	2.75%	2.75%
Cost of Living Adjustments [1]	COLA is equal to the average five-year fund asset performance (percent) greater than 5.5% up to a maximum of 4% - the COLA is to be applied to the first $25,000 of benefits, indexed over time (see note 2 below). COLA is delayed until the later of Social Security eligibility age or 3 years after retirement except for State Police and MERS Police and Fire for which the COLA is delayed until the later of age 55 or 3 years after retirement.				

Note 1 – Cost of Living Adjustments (COLA) in member benefit provisions prior to the enactment of pension reform legislation on November 18, 2011 will remain in effect through June 30, 2012.

For the MERS plan, a 2% COLA is assumed after July 1, 2012. For all other plans, a COLA of 2% is assumed only every five years until the plans achieve a 80% collective funded status in accordance with the law. It is assumed that the plans will not achieve the targeted 80% funded status for 16 years.

2. Schedules of Funding Progress

The MERS funded ratio is a composite of all units in the plan. The System performs a separate valuation for each unit.

Changes affecting the June 30, 2011 actuarial valuation:

The retirement rates were modified to be consistent with the retirement eligibility changes instituted by the Rhode Island Retirement Security Act of 2011. Members that were assumed to retire prior to the Act, but before the earliest allowable age under the Act, are assumed to retire once eligible.

For future cost of living benefit adjustments, the benefit adjustments are assumed to be suspended for approximately 16 years, except for the intermittent adjustment every fifth year.

Changes affecting the June 30, 2010 actuarial valuation** (as restated to reflect the provisions of pension reform legislation enacted on November 18, 2011)**:

The June 30, 2010 valuations (as restated to reflect the provisions of pension reform legislation enacted on November 18, 2011) reflect comprehensive changes to plan member benefit provisions which are effective beginning July 1, 2012. The June 30, 2010 valuations also reflect material changes to certain actuarial assumptions.

The revised member benefit provisions become effective on July 1, 2012. These include changes in service period accrual rates, retirement eligibility age, and future cost of living adjustments. Additionally, the unfunded accrued liability is now amortized over a twenty-five year period from June 30, 2010 compared to the 30 year period from June 30, 1999 employed in prior actuarial valuations.

The Individual Entry Age Cost Method is used in the June 30, 2010 actuarial valuations. Prior valuations utilized the Ultimate Normal Cost methodology where normal cost was determined based on the benefits applicable to new hires under the replacement benefit structure resulting from prior pension reform measures.

The annual investment rate of return was lowered from 8.25% to 7.5%.

The post-termination mortality rates for non-disabled state employees and members of the MERS, State Police and Judicial plans were previously based on the 1994 Group Annuity Mortality Tables. New mortality tables have been constructed and adopted with adjustments for these employees using the RP-2000 Combined Healthy for Males and Females with White Collar adjustments, projected with Scale AA from 2000 for non-disabled individuals.

The post-termination mortality rates used for non-disabled teachers in the June 30, 2009 and June 30, 2010 valuations were both based on tables developed by ERSRI's actuary based on teacher experience. The rates used in the June 30, 2010 valuation for male teachers were lowered to 97% of the rates in these tables based on male teacher experience, projected with Scale AA from 2000 from 100% of the actuary's table based on male teacher experience used in the June 30, 2009 valuation. The rates used in the June 30, 2010 valuation for female teachers were lowered to 92% of the rates used in the actuary's tables based on female teacher experience, projected with

2. Schedules of Funding Progress (continued)

Scale AA from 2000 from 95% of the actuary's table based on female teacher experience used in the June 30, 2009 valuation.

The post-termination mortality rates for disabled members of all ERSRI plans are based on the PBGC table Va for males and table VIa for females. The rates used in the June 30, 2010 valuation for disabled males eligible for social security disability benefits were lowered to 60% of PBGC table Va from 65% of this table in the June 30, 2009 valuation. The rates used in the June 30, 2010 valuation for disabled females eligible for social security disability benefits were lowered to 60% of PBGC table VIa from 100% of this table in the June 30, 2009 valuation.

The pre-retirement mortality rates for all members of the ERSRI plans were previously based on the 1994 Group Annuity Mortality Tables. The rates used in the June 30, 2010 valuation for these employees were based on the RP-2000 Combined Tables with white collar adjustment for males and females. The tables were adjusted for each individual plan.

The inflation assumption rate was decreased from 3% to 2.75% and the projected salary increase assumptions were also decreased compared to the prior valuation. The assumption for cost of living adjustments subject to the Consumer Price Index (for those not eligible to retire on September 30, 2009) was decreased from 2.5% to 2.35%.

Changes affecting the June 30, 2009 actuarial valuation:

The June 30, 2009 valuation for the Employees' Retirement System and the Judicial Retirement Benefit Trust reflects the enactment of Article 16 of Chapter 23 of the 2010 Public Laws which amended the laws governing benefits for state employees, teachers and judges not eligible to retire by June 12, 2010 – see note 1(b) to the financial statements entitled *Plan Descriptions – Membership and Benefit Provisions*.

The changes enacted as a result of Article 16 of Chapter 23 of the 2010 Public Laws governing benefit provisions for the Employees' Retirement System and the Judicial Retirement Benefit Trust are reflected and were applied in determining the contributions rates for the fiscal years ended June 30, 2010 and June 30, 2011 - see note 1(b) to the financial statements entitled Plan Descriptions – Membership and Benefit Provisions.

Changes affecting the June 30, 2008 actuarial valuation:

The June 30, 2008 valuation for the Employees' Retirement System and the Judicial Retirement Benefit Trust reflects the enactment of H5983Aaa, Article 7, Substitute A to the laws governing benefits for state employees and teachers not eligible to retire by September 30, 2009 and judges appointed after July 1, 2009 – see note 1(b) to the financial statements entitled *Plan Descriptions – Membership and Benefit Provisions*.

The changes enacted as a result of Article 7 Substitute A to the laws governing benefits provisions for the Employees' Retirement System and the Judicial Retirement Benefit Trust are reflected and were applied in determining the contributions rates for the fiscal years ended June 30, 2009, June 30, 2010 and June 30, 2011 - see note 1(b) to the financial statements entitled *Plan Descriptions – Membership and Benefit Provisions*.

2. Schedules of Funding Progress (continued)

Changes affecting the June 30, 2007 actuarial valuation:

The June 30, 2007 actuarial accrued liability was restated for the Judicial Retirement Benefit Trust to reflect the amendment to the law governing benefits for judges appointed after January 1, 2009 – see note 1(b) to the financial statements entitled *Plan Descriptions – Membership and Benefit Provisions*.

Changes affecting the June 30, 2006 actuarial valuation:

Material changes were made to increase the salary, payroll growth and termination assumptions. In addition, there were changes in the Post-retirement mortality rates for non-disabled retirees. Currently rates are based on the 1994 Group Annuity Mortality Tables for males and females, with adjustments to the tables for male teachers and male state employees. The tables are then compared to the A/E ratio (actual deaths to expected deaths). It was determined the tables for state employees required no changes. However, the A/E ratios for teachers were lower than the acceptable actuarial ranges. Therefore, new mortality tables have been constructed and adopted for teachers based on teacher mortality rates in another state with similar life expectancies. The pre-termination mortality currently uses the post-retirement mortality assumption. The rates for pre-termination mortality are computed at a rate equal to 65% of the post-retirement rates.

The base salary rate for ERS and MERS General Employees remained unchanged. Judges base salary rates decreased from 5.25% to 4.50% and State Police decreased from 5.00% to 4.50%. The salary rate increase for state employees changed from 4.50% - 8.25% to 4.50% - 9.00%. Teachers changed from a range of 4.50% - 17.00% to 4.50% - 13.25%. MERS General Employees changed from a range of 4.50% - 9.00% to 4.50% - 8.50%. MERS Police & Fire Employees changed from a range of 5.00% - 15.50% to 4.75% - 14.75%.

The payroll growth rate was increased from 3.75% to 4.25% for ERS and MERS; it also increased from 3.75% to 4.5% for State Police and decreased from 5.25% to 4.5% for Judges. The marriage assumption for members being married was changed from 100% to 85%.

3. Schedules of Employer Contributions

Employer contributions for the ERS plan included in the Schedules of Contributions from the Employers and Other Contributing Entity do not include Teacher Survivor Benefits as described in Note 1(b) and any employer contributions related to supplemental pension benefits that are attributable and paid by a specific employer. These amounts are not included in the annual required contribution.

The unfunded liabilities of the plans are amortized over a 30 year period from June 30, 1999. The closed period ends 30 years from June 30, 1999 for actuarial valuations as of June 30, 2009 and prior. Beginning with the valuations performed as of June 30, 2010, the unfunded accrued liability is amortized over a twenty-five year period from June 30, 2010.