

PSERS

Pennsylvania
Public School Employees' Retirement System

House Appropriations Committee

*Partners
for Your Future*

2010/2011 Budget Report



COMMONWEALTH OF PENNSYLVANIA
PUBLIC SCHOOL EMPLOYEES' RETIREMENT BOARD

MELVA S. VOGLER
Chairman

SALLY J. TURLEY
Vice Chairman

February 3, 2010

Members of the House Appropriations Committee

Dear Members:

On behalf of the Public School Employees' Retirement System (PSERS), I am pleased to present the accompanying report on the financial, actuarial, and investment operations of PSERS and the budgetary projections for the 2010-2011 fiscal year. In addition, PSERS Comprehensive Annual Financial Report for the fiscal year ended June 30, 2009, is also attached.

PSERS is responsible for administering a defined benefit pension plan for over 561,000 active and retired public school employees in the Commonwealth of Pennsylvania. PSERS also administers two postemployment health care programs, the Premium Assistance Program and the Health Options Program (HOP) for its annuitants. Some highlights of recent activities follow:

Financial Highlights

The worst economic contraction since the Great Depression led to a large decrease in U.S. Gross Domestic Product, an increase in the U.S. unemployment rate, the failure of several large financial institutions and the federal government bailout of several large public companies. The extremely difficult economic conditions in this business cycle, which is commonly being referred to as the "Great Recession," led to negative returns for equity, real estate and commodities around the world. As a result, PSERS experienced a very challenging fiscal year ended June 30, 2009 (FY 2009) as PSERS' investment portfolio generated a rate of return of -26.54%. Since that time period the investment markets have slowly improved.

- The long-term investment returns for the fund remain positive. The estimated investment rates of return for the one, three, five and ten-year periods ended December 31, 2009 were 11.21%, -3.84%, 3.20% and 3.50% respectively. Over the past 25 years the fund earned an annualized rate of return of 9.27% which remains above the fund's current assumed rate of return of 8.00%.
- PSERS' total plan net assets decreased from \$62.7 billion to \$43.2 billion from July 1, 2008 to June 30, 2009, which is PSERS' fiscal year. The decrease is primarily attributable to the fact that the combined net investment loss and payment of benefits and administrative expenses far exceeded member and employer contributions. PSERS estimate of total plan net assets as of December 31, 2009 was approximately \$46.6 billion.

- Despite the difficult economic environment in FY 2009, the Board has continued to fulfill its mission to maintain stability and the long-term optimum value of the Fund. This is evidenced in the long-term growth of the System's assets and the actuarial soundness of the Fund with respect to its funding status. Of utmost importance to the Board is the assurance that the required reserves are available for payment of retirement benefits.
- PSERS continues to benefit from managing almost 1/3 of its assets internally including operating its own equity trading room. For FY 2009 PSERS' internal asset management produced savings of \$21.2 million and additional excess performance of \$111.2 million.
- Total member contributions increased from \$1.04 billion in FY 2008 to \$1.09 billion in FY 2009 as a result of the increase in total active member payroll and an increase in the average member contribution rate from 7.25% in FY 2008 to 7.29% in FY 2009. Total employer contributions decreased from \$834.9 million in FY 2008 to \$608.4 million in FY 2009 due to a decrease in the employer contribution rate from 7.13% in FY 2008 to 4.76% in FY 2009.
- PSERS total administrative budget request is \$44.2 million for FY 2010-2011 compared to \$43.2 million available for FY 2009-2010. The Governor's Budget Office recommended budget for PSERS will be available February 9, 2010.

Funded Status

- PSERS uses an actuarial reserve type of funding that is financed by member contributions, employer contributions, and earnings from invested assets. An independent actuarial valuation of PSERS' actuarial assets and liabilities is performed annually. As part of this valuation, the progress toward funding pension obligations of PSERS is measured by comparing the actuarial value of assets to the actuarial accrued liability. This measurement is referred to as the funded ratio or funded status. The most recent actuarial valuation reports that PSERS is 79.2% funded as of June 30, 2009. This represents a decrease from PSERS' 86.0% funded status as of June 30, 2008.
- During the first half of the 1990s when PSERS funded status was in the mid-80% range, as it is near currently, the employer contribution rate ranged from 11.10% to 19.68%. This compares to the current employer contribution rate of 4.78%.

Investment and Pennsylvania Commitment

- PSERS has a continuing commitment to Pennsylvania companies by contracting with Pennsylvania-based investment advisor companies and by investing in Pennsylvania-based companies where investment characteristics, including yield, risk, and liquidity, are equivalent. Data on Pennsylvania investments is contained in the accompanying report.

- Total PSERS' benefit expense remained constant at \$4.9 billion in FY 2009 and FY 2008 as higher monthly benefits from an increase in the overall number of retirees and beneficiaries receiving benefits were offset by lower lump sum payments due to a decrease in the number of new retirees in FY 2009. The lower number of new retirees in FY 2009 is consistent with national trends as people delayed retirement due to the significant decline in world financial markets and the global economic recession. Of the \$4.9 billion in benefits, 90% was distributed to Pennsylvania residents. The total gross distribution of monthly retirement and survivor annuitant benefits to Pennsylvania residents during the 2009 calendar year exceeded \$3.77 billion dollars, representing PSERS' significant impact on the Commonwealth's economy.

Update on the Projected Increase in the Employer Contribution Rate in FY 2012- 2013

- The current funding issue confronting PSERS represents the greatest challenge the System has faced in its history. The funding issue commonly referred to as the "rate spike" or "rate plateau" refers to the significant increase in the employer contribution rate in FY 2012/2013 and following years that is paid by school employers and the Commonwealth to PSERS to fund pension benefits. This rate increase was first projected at 27.73% in PSERS' June 30, 2003 actuarial valuation.
- Based on the June 30, 2009 valuation, the current estimate for the FY 2012-2013 employer contribution rate is 29.22%. The actual peak in the rate, however, now appears two years later in FY 2014-2015 at 33.60%.
- This projection takes into consideration the actuarial impact of the pension benefit enhancement enacted in 2001 (Act 9 of 2001), a cost-of-living adjustment for retirees in 2002 (Act 38 of 2002), a major downturn in the investment markets between 2001 and 2003 and a series of legislative actions (Act 38 of 2002 and Act 40 of 2003) that changed the basic funding methodologies for PSERS and suppressed the employer contribution rate for a period of ten years. In addition, the recent historic economic downturn during FY 2008-2009 and the accompanying investment losses experienced by PSERS (-26.54% for FY 2008-2009) compounded the existing funding issue.
- As of December 2009, PSERS' estimated current fiscal year investment performance remained well above the fund's assumed annual investment rate of return of 8.00% which will help reduce the existing unfunded liabilities of the fund. While a few months remain until the end of the fiscal year on June 30th and the investment markets continue to improve, PSERS cannot earn its way out of the funding issue facing the System.
- There are options to address the projected large employer contribution rate increase in FY 2012-2013, but under all such options there remains a need for significant additional funding to PSERS.

- PSERS will continue to be very public with the funding issue in an attempt to raise awareness. Over the past year PSERS has significantly increased its educational efforts regarding the funding issues facing the System in the near future. PSERS Executive Director has traveled across the Commonwealth meeting with school districts, school boards, retiree and active member organizations and legislators and their staff. The purpose of these presentations is to make sure both school employers and the Commonwealth are aware of the impact this issue will have on their budgets and the options available to resolve the issue.
- PSERS has created a resource page on its website to help PSERS' members, the media, legislators and their staff, and the general public better understand the System and the complexity of the funding challenges facing PSERS, the Commonwealth and school employers. To view the resource page, go to the following link on PSERS' website.

http://www.psers.state.pa.us/press/pension_funding_issues/index.html

- The resolution of the current funding issues confronting PSERS is a vital imperative for the Agency. As in the past, PSERS remains committed to providing all available assistance to the General Assembly to solve the projected rate increase and future funding issues of PSERS.

In conclusion, please contact Jeffrey B. Clay, Executive Director, if you have any questions or would like additional information.

Respectfully,



Melva S. Vogler
Chairman of the Board

2010/2011 Budget Report

House Appropriations Committee

Budget Report Date February 3, 2010

2010/2011 Budget Hearing Materials

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- PSERS Board of Trustees
- PSERS Organizational Chart and Description
- Member Demographics
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- Employer Contribution Rates: Past, Present, and Future
- Consultants' Fees
- Legislative Information

Overview and Mission Statement

Overview

Established on July 18, 1917, the Pennsylvania Public School Employees' Retirement System (PSERS) provides retirement benefits to public school employees of the Commonwealth of Pennsylvania.

As of June 30, 2009, the System had approximately 280,000 active members. The annuitant membership was comprised of approximately 178,000 retirees and beneficiaries, who receive monthly pension benefit payments of over \$340 million including healthcare premium assistance. The average yearly pension benefit paid to annuitants was \$22,456. PSERS had 742 participating employers on June 30, 2009.

As reported in the latest Pension and Investments survey published December 28, 2009, PSERS is the 22nd largest plan among United States corporate and public pension plans, and the 12th largest state-sponsored defined benefit public pension fund in the nation. PSERS is the 41st largest plan among corporate and public pension plans worldwide. The net asset value of PSERS' investment portfolio was approximately \$46.6 billion as of December 31, 2009.

During the 2009 calendar year the overall gross distribution of pension benefits including monthly benefits, direct rollovers, survivor benefits and refunds totaled \$4.75 billion. Of this amount, 90% was distributed to Pennsylvania residents. The total gross distribution of monthly retirement and survivor annuitant benefits to Pennsylvania residents was approximately \$3.8 billion dollars, representing PSERS' significant impact on the Commonwealth's economy.

Mission Statement

The Board of Trustees and the employees of the Public School Employees' Retirement System serve the members and stakeholders of the System by:

- Providing timely and accurate payment of benefits,
- Maintaining a financially sound System,
- Prudently investing the assets of the System,
- Clearly communicating members' and employers' rights and responsibilities, and
- Effectively managing the resources of the System.

PSEERS Board of Trustees

PSERS Board of Trustees

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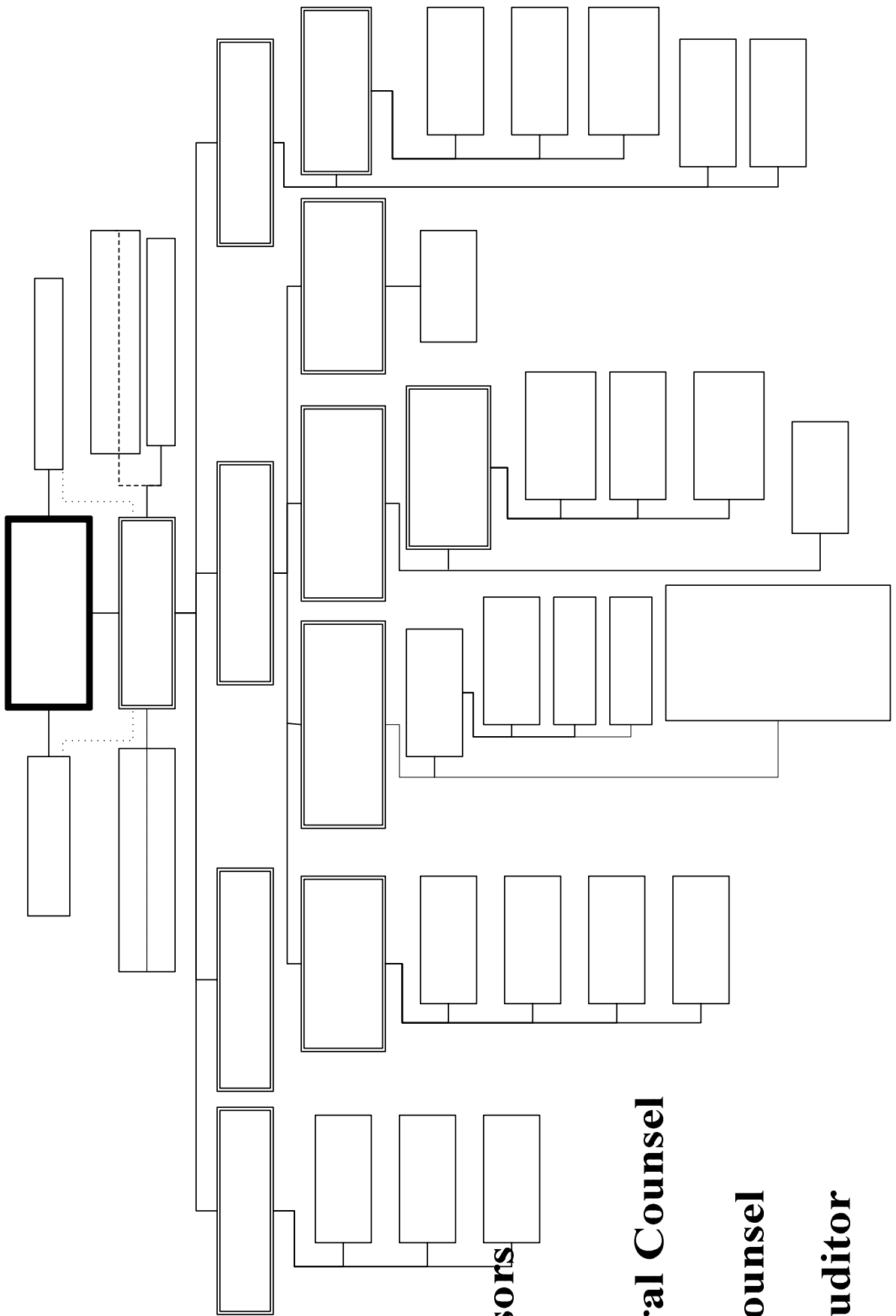
Patricia A. Tozer

Gerald L. Zahorchak, D.Ed.
Secretary of Education

PSERS Board Members as of November 6, 2009

PSERS Organizational Chart and Description

PSEERS Organizational Chart



Organizational Structure of the Public School Employees' Retirement System

Executive Office

This office is responsible for the overall management of the Public School Employees' Retirement System (PSERS) to achieve the primary objectives of the Fund as established by the Board of Trustees (Board). Reporting directly to the Executive Director are the Deputy Executive Director, Assistant Executive Director, Chief Investment Officer, Chief Financial Officer, Internal Auditor, Press Secretary, and Legislative Liaison. The Executive Director serves as chief executive officer responsible for the establishment, installation, and maintenance of modern management techniques to provide an efficient control of funds for and services to the active members and annuitants of the System.

The Executive Office monitors the operation of the investment portfolio and evaluates portfolio performance for consideration by the Board, certifies expenditures of the Fund, and measures performance of professional individuals or firms with whom the Board contracts for specialized services. The Executive Office also apprises the Board of any development that will in any way affect the System and its operation.

Investment Office

This office is responsible for the investment activities of the System. In compliance with the investment policy established by the Board, PSERS' investment assets are allocated to numerous outside professional investment advisors and internal investment professionals.

Chief Counsel's Office

This office provides legal services through a team of professional personnel under the Governor's Office of General Counsel. The Legal staff is responsible for representing PSERS in all administrative hearings and other litigation matters; drafting and negotiating PSERS' investment and administrative services contracts; and providing counsel on a wide variety of matters, including the interpretation of the Retirement Code and the Right-to-Know Law.

Internal Auditor's Office

This office performs systematic reviews of the various activities of PSERS, testing for compliance with applicable laws, policies and procedures. The Internal Auditor makes recommendations on the improvement of PSERS' internal control system.

Office of Financial Management

This office is directed by the Chief Financial Officer and has responsibility for planning, organizing and directing a complete accounting and financial reporting system in conformance with accounting principles generally accepted in the United States of America. Oversight is provided for new accounting systems development and maintenance of existing systems, and ensuring appropriate accounting controls. The office is the liaison for other state and federal agencies, reporting units, financial consultants, actuaries, and investment advisors for all accounting, treasury operations, taxation, actuarial and budgetary matters. The office is organized into three divisions: General Accounting Division, Annuitant Accounting and Budget Division, and Investment Accounting Division.

**Organizational Structure of the
Public School Employees' Retirement System
(continued)**

Deputy Executive Director

The Deputy Executive Director directly oversees the benefit programs for all active and retired members of the System, the development and implementation of the member and employer communications programs and the member counseling programs, and the maintenance of agency policies, procedures, and benefit related data. Additionally, this position supervises a Chief Technology Officer who oversees business and information technology strategic planning, policy development, and implementation. The organizational units directly reporting to this position include the Bureau of Benefits Administration, the Bureau of Communications and Counseling, and the Bureau of Information Management. The position oversees the Bureau of Information Technology through the Chief Technology Officer.

Information Technology Office

This office oversees the Bureau of Information Technology and the Business Architecture Center. It is responsible for strategic information technology planning and policy development, ensuring that information technology plans and policies are aligned with, in support of, and prioritized according to agency needs and requirements, as well as those Commonwealth needs and requirements that are consistent with agency needs, and for communicating such to the agency's information technology staff. Large information technology contracts and projects are managed by this office. This office is responsible for understanding, analyzing, documenting, and improving PSERS' organization, business rules, processes, information systems, and the relationships among these components so that PSERS is able to: conduct its business consistently and according to established rules; understand each component, its relationship to each of the other components and to PSERS' mission, vision, values and goals; fully, yet quickly analyze and understand the impact of potential change to one or more of these components on the others; more effectively identify inefficient, duplicate, or suspect processes, and/or technologies; and account for its organizational business rules and processes, information systems and technologies.

Bureau of Information Technology

This bureau is responsible for planning, coordinating, administering, and implementing information technology resources in accordance with the agency's strategic plans, goals, objectives, and priorities as communicated by PSERS' Chief Technology Officer, and for providing operational support for those technologies and initiatives. The bureau is organized into three divisions: the Network, Server, and Database Division, the Business Applications Division, and the Document Archive and Data Capture Division.

Bureau of Information Management

This bureau is responsible for maintaining, documenting, and cleansing PSERS' member and employer data, managing PSERS' electronic data records, imaged records, paper and film/fiche records, understanding the meaning and knowing the location of its data. The bureau currently includes the Data Stewardship Division which houses PSERS' records management program, and the Data Integrity and Member Accounting section.

**Organizational Structure of the
Public School Employees' Retirement System
(continued)**

Bureau of Benefits Administration

This bureau is responsible for administering a comprehensive pension benefits program for PSERS. The bureau provides professional and technical services to individuals who are employed full-time and part-time in one of Pennsylvania's 742 public schools or institutions. They also provide services to retirees, their beneficiaries and persons legally authorized to act on their behalf. The bureau is organized into three divisions: the Benefit Processing Division, Benefit Policy and Specialized Service Division, and Exception Processing Division.

Bureau of Communications and Counseling

This bureau is responsible for professionally communicating accurate and timely information. The goal is to promote the understanding of PSERS' benefits and processes to the members, the employers, the Legislature, the Governor's Office, other government organizations, professional organizations, and the public. It is organized into two divisions: the Field Services Division and the Communications Services Division.

Assistant Executive Director

This position reports to the Executive Director and may provide assistance to the Executive Director on agency-wide projects. The position administers the Health Options and Premium Assistance Programs in addition to the facilities, human resources, and procurement activities necessary to support, secure and optimize agency operations. Organizational units overseen by the Assistant Executive Director include the Bureau of Administration, the Human Resources Office, and the Health Insurance Office.

Bureau of Administration

This bureau is responsible for facilities, purchasing and contracting, documenting administrative policies and procedures, business continuity, automotive, mail, imaging, printing and other administrative services necessary to support agency functions. The bureau is organized into three divisions: the Purchasing and Contracting Division, the Administrative Services Division and the Security and Business Continuity Division.

Human Resources Office

This office is responsible for supporting management and staff to facilitate the accomplishment of the agency's mission. It administers all human resources programs and ensures compliance with labor law and Commonwealth regulations. Programs include position classification, labor relations, recruitment and placement, employee benefits, employee compensation and pay, training and staff development, time and attendance, performance management, organizational development and support, employee transactions, Equal Employment Opportunities and other miscellaneous programs.

Health Insurance Office

This office is responsible for all aspects of the PSERS' Health Options Program (HOP) and administering PSERS' health insurance Premium Assistance benefits. The HOP is a voluntary program that provides group health insurance coverage for 66,900 (at January 1, 2010) school retirees, their spouses, and eligible dependents.

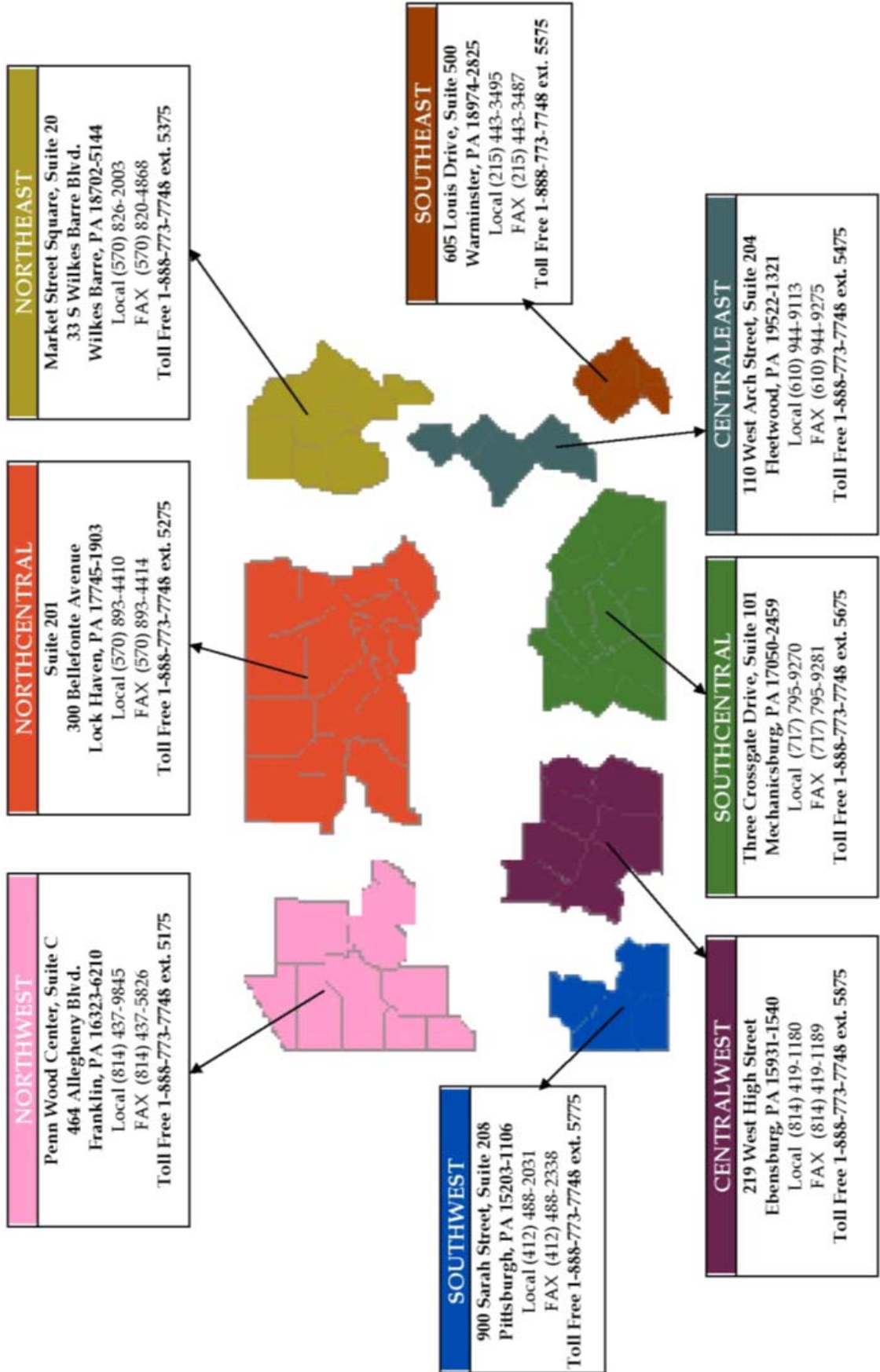
PSERS' Regional Offices

There are eight PSERS Regional Offices strategically located throughout the Commonwealth. These offices provide services to both active and retired PSERS members and 742 employers. Among these services are regularly scheduled retirement counseling meetings and other informational presentations on various topics relating to retirement benefits and programs. See map on next page.

Services provided to PSERS' Members (by the Bureau of Communications and Counseling and/or the Bureau of Benefits Administration)

	<u>2006/07</u>	<u>2007/08</u>	<u>2008/09</u>
Number of General Information Programs	237	224	197
Number of Members Attended	13,458	12,663	10,850
Number of Exit Counseling (small group) Sessions	1,059	1,005	908
Number of Members Attended	8,415	7,904	6,438
Individual Counseling Sessions	1,646	1,992	1,918
Telephone Calls Answered	246,264	227,252	229,773
Telephone Calls Out	56,224	50,421	54,628
E-Mail In	21,513	27,403	31,008
E-Mail Out	20,319	23,810	30,860
Purchase of Service Applications Processed	5,548	8,073	16,404
Retirements Processed			
• <i>Normal</i>	5,042	4,537	5,865
• <i>Early</i>	5,232	4,147	5,188
• <i>Disability</i>	397	415	458

PSERS REGIONAL OFFICES



Member Demographics

PSERS' Member Demographics

<u>Fiscal Year ending June 30</u>	<u>Active Members</u>	<u>Inactive Members</u>	<u>Annuitants, Beneficiaries, and Survivor Annuitants</u>	<u>Total Active/Retired Members</u>	<u>Ratio of Active/Retired</u>	<u>Overall Member Total Inactive, Active & Survivor Annuitants</u>
2009	279,701	103,805	177,963	457,664	1.57 to 1	561,469
2008	272,690	100,803	173,540	446,230	1.57	547,033
2007	264,023	109,186	168,026	432,049	1.57	541,235
2006	263,350	94,071	161,813	425,163	1.62	519,234
2005	255,465	58,720	156,519	411,984	1.63	470,704
2004	247,901	72,014	151,552	399,453	1.63	471,467
2003	246,700	65,453	145,693	392,393	1.69	457,846
2002	242,616	61,295	141,414	384,030	1.71	445,325
2001	243,311	53,979	132,716	376,027	1.83	430,006
2000	234,210	50,682	134,058	368,268	1.74	418,950

Age and Service Profile of Active Members as of June 30, 2008 and June 30, 2009

	<u>June 30, 2008</u>	<u>June 30, 2009</u>
Average Age	44.6 years	44.6 years
Average Years of PSERS Service	10.7 years	10.6 years
Average Annual Compensation	\$43,718	\$44,779

Profile of PSERS' Annuitants, Beneficiaries, and Survivor Annuitants as of June 30, 2008 and June 30, 2009

<u>Type of Member</u>	<u>Number of Members</u>		<u>Average Annual Benefit</u>	
	<u>6/30/2008</u>	<u>6/30/2009</u>	<u>6/30/2008</u>	<u>6/30/2009</u>
Normal/Early Retirees	157,656	162,206	\$22,748	\$23,343
Survivor Annuitants	8,449	8,044	\$9,805	\$9,836
Disability Retirees	<u>7,435</u>	<u>7,713</u>	\$19,144	\$16,948
Total	<u>173,540</u>	<u>177,963</u>	\$21,963	\$22,456

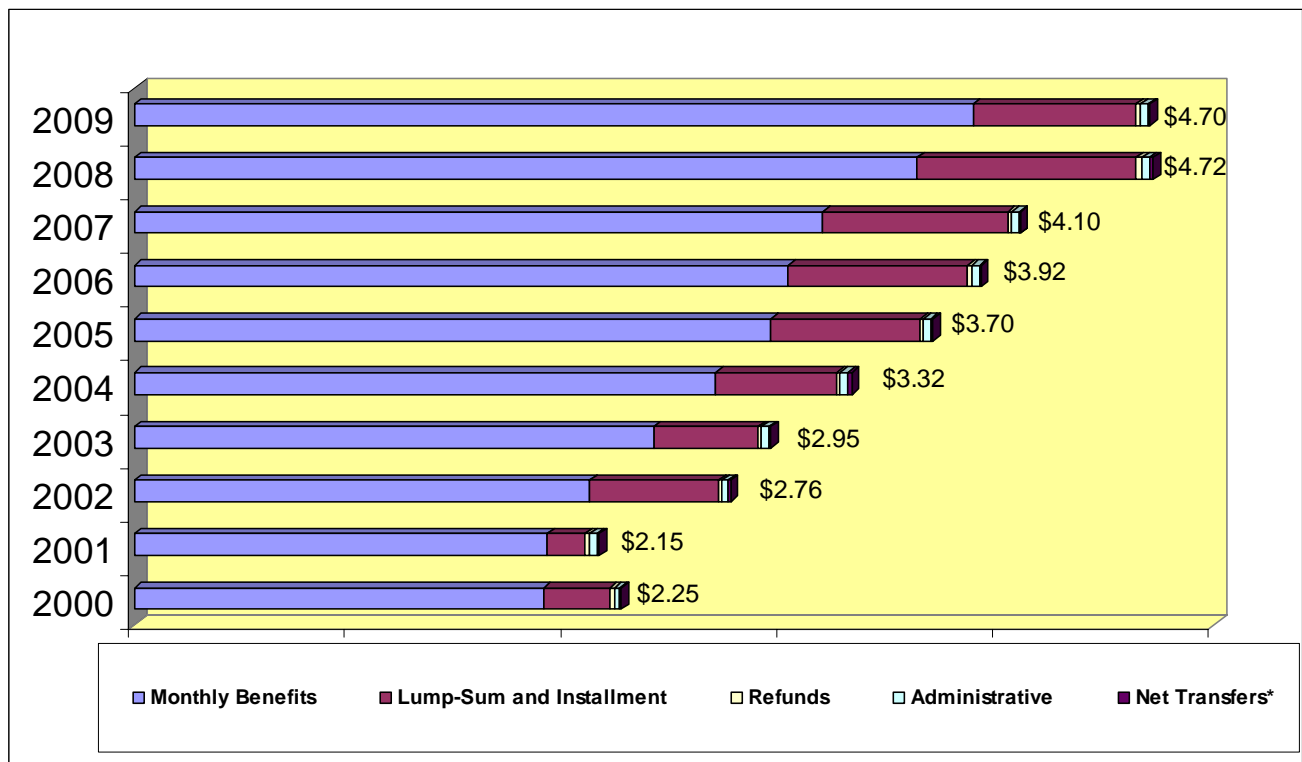
PSERS' Member Demographics
(continued)

Deductions from Pension Plan Net Assets
10 Year Trend
(Dollar Amounts in Thousands)

Year Ending June 30	Benefits		Refunds	Administrative	Net Transfers*	Total Deductions
	Monthly Benefits	Lump- Sum and Installment				
2009	\$3,885,286	\$ 754,011	\$20,369	\$35,639	\$ 7,947	\$4,703,252
2008	3,623,652	1,012,688	28,713	35,863	17,157	4,718,073
2007	3,189,004	855,431	18,180	35,239	6,010	4,103,864
2006	3,030,297	830,361	16,330	35,391	8,462	3,920,841
2005	2,947,749	692,089	16,233	32,670	10,859	3,699,600
2004	2,692,485	559,939	14,767	40,014	16,315	3,323,520
2003	2,404,697	485,495	13,943	34,293	12,116	2,950,544
2002	2,111,941	595,184	14,858	29,756	9,434	2,761,173
2001	1,914,062	176,228	22,369	31,335	10,867	2,154,861
2000	1,894,418	306,329	22,446	25,837	4,710	2,253,740

* Net transfers to the Commonwealth of Pennsylvania, State Employees' Retirement System.

Deductions from Pension Plan Net Assets
10 Year Trend
(Dollar Amounts in Billions)



Actuarial Process and Pension Plan Funding

The Actuarial Process and Pension Plan Funding

PSERS is a defined benefit plan, meaning benefits are based on members' service and salary history. The plan is funded through three sources: (1) employer contributions; (2) member contributions; and, (3) investment earnings. The following information highlights the actuarial process and funding for PSERS.

Actuarial Process

The actuarial process presumes that there will be a systematic flow of contributions at a specified level to pay for plan benefits and that the flow of contributions, together with investment earnings, will be sufficient to meet all benefit and expense requirements of the plan. Actuarial cost methods for funding PSERS pension plan are defined in the Public School Employees' Retirement Code. The actuary for the pension plan reviews economic and demographic experience annually and over five-year periods. The actuary's periodic valuations test the validity of the underlying actuarial assumptions versus the actual experience of the plan. That experience is also used as a basis for formulating actuarial assumptions, which are essentially highly educated predictions about what will occur in the future with respect to salary growth, investment returns, and demographic factors such as rates of retirement and death. PSERS' primary economic assumptions for 2009/2010 project an average annual investment return of 8.00% and an average annual salary increase factor of 6.00%.

At the January 23, 2009 meeting, PSERS Board of Trustees voted to decrease the actuarial investment rate of return assumption from 8.50% to 8.25% effective for the June 30, 2008 actuarial valuation. The Board of Trustees also voted to decrease the rate of return assumption further from 8.25% to 8.00% for the June 30, 2009 actuarial valuation. The changes made by the Board lowers PSERS' rate of return assumption to the median investment rate of return assumption used by most public pension funds and provide a more realistic outlook of the future earning's potential of the Fund.

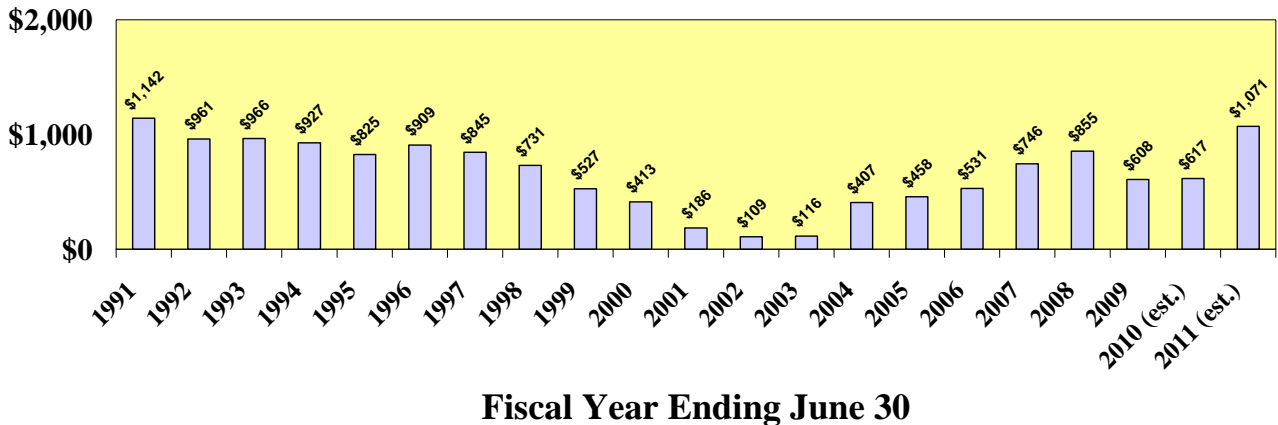
Employer Contributions

The Retirement Code vests the Board with the authority to establish the employer contribution rate. The Board, in consultation with the actuary, establishes the employer contribution rate annually, as part of the annual actuarial valuation. The employer contribution rate, which is expressed as a percentage of payroll, is composed of two items: 1) the pension contribution; and, 2) the contribution for health care premium assistance. The total employer contribution rate for the year ended June 30, 2009, was 4.76%, including 0.76% for health care premium assistance. The total employer contribution rate for the fiscal year ending June 30, 2010 is 4.78%, including 0.78% for health care premium assistance. The total employer contribution rate adopted by PSERS' Board of Trustees for the year ending June 30, 2011 is 8.22%, including 0.64% for health care premium assistance. The estimated FY 2012/2013 employer contribution rate is 29.22% which is based on the June 30, 2009 actuarial valuation.

The Actuarial Process and Pension Plan Funding (continued)

For the fiscal year ended June 30, 2009, PSERS' employer contributions totaled \$608 million, which includes \$92 million for healthcare premium assistance. For the fiscal year ending June 30, 2010 the employer contribution estimate is \$617 million, reflective of the 4.78% contribution rate. The contribution rate for the fiscal year ending June 30, 2011 is 8.22% which results in a contribution estimate of \$1.1 billion.

Employer Contribution History (in millions)



Member Contributions

Members of the Public School Employees' Retirement System who, prior to Act 9 of 2001, contributed to the Retirement Fund at the rate of 6.25% of their gross compensation, began contributing 7.50% in January of 2002, if they elected the higher retirement benefits. Members who contributed at the rate of 5.25% began contributing 6.50% if they elected the higher retirement benefits.

PSERS members contributed \$911 million for pension contributions for fiscal year 2008-2009, compared to \$880 million for the 2007-2008 fiscal year. Total member contributions are estimated to be \$944 million for the year ending June 30, 2010 and \$992 million for the year ending June 30, 2011. The annual increases are due to a projected increase in member payroll and due to small increases in the member contribution rate each year.

Investment Returns

The investment rate of return (net of fees) for the fiscal years ended June 30, 2009, and June 30, 2008, was -26.54% and -2.82%, respectively. The annualized rates of investment return for the three, five and ten-year periods ended June 30, 2009 were -4.26%, 2.68% and 3.28% respectively. The net asset value of PSERS' investments was \$43.2 billion as of June 30, 2009. The estimated investment rates of return for the one, three, five and ten-year periods ended December 31, 2009 were 11.21%, -3.84%, 3.20% and 3.50% respectively. Over the past 25 years the fund earned an annualized rate of return of 9.27% which remains above the fund's current assumed rate of return of 8.00%

The Actuarial Process and Pension Plan Funding (continued)

Funded Status

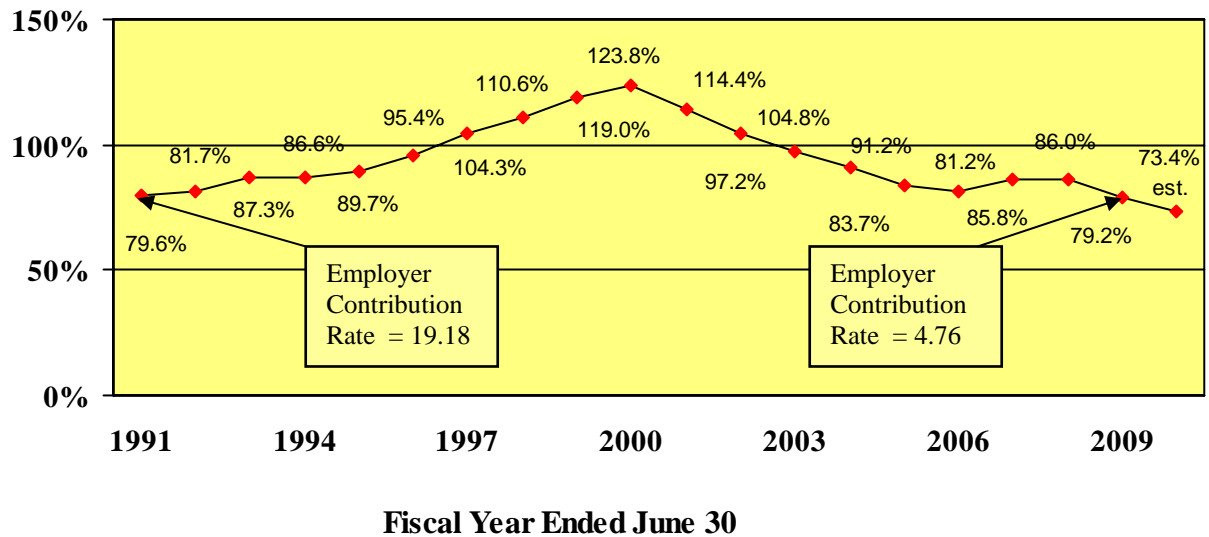
PSERS funded status is measured by comparing the actuarial value of assets with the accrued liability. The accrued liability is the present value of benefits accumulated to date for both active and retired members.

Key Facts

- Funded Status is 79.2% as of June 30, 2009
- Funded Status was 86.0% as of June 30, 2008
- The decrease in the funded status since 2000 is the result of several factors including: the unfavorable investment markets from FY 2001 to FY 2003 and FY 2008 to FY 2009; funding changes enacted in Act 38 of 2002 and Act 40 of 2003; and actuarial liability losses.

PSERS Funded Ratio

Funded Ratio = Actuarial Value of Assets/Actuarial Accrued Liability



Employer Contribution Rates: Past, Present, and Future

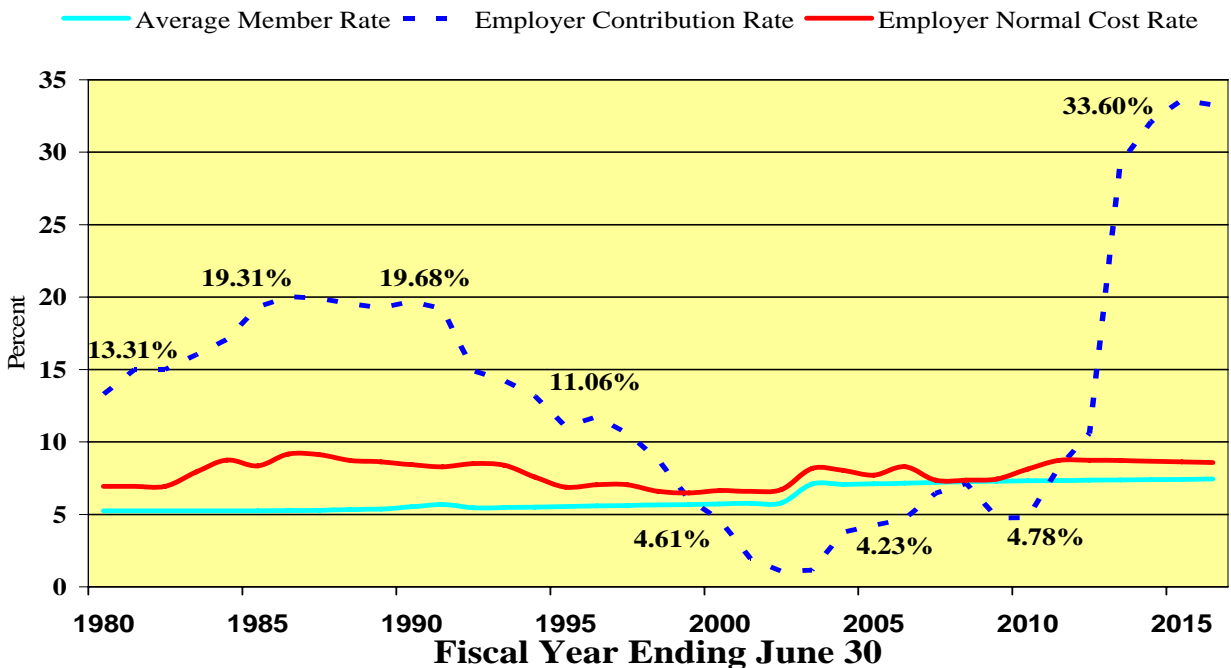
Employer Contribution Rate

PSERS undergoes an annual independent actuarial valuation to calculate the actuarial assets and liabilities of the pension fund. Based on the actuarial valuation process, the actuary develops the recommended Employer Contribution Rate (ECR) that determines the employer contributions to the pension plan. The valuation process also measures the progress of the pension system towards funding pensions for its active and retired members.

Employer Contribution Rate Statistics

• Highest historical ECR (1985/1986 year)	20.04%
• Lowest historical ECR (2001/2002 year)	1.09%
• Ten year average ECR (2001 to 2010)	4.63%
• Twenty year average ECR (1991 to 2010)	7.17%
• Thirty year average ECR (1981 to 2010)	10.94%
• Adopted ECR (2010/2011 year)	8.22%

PSERS' Contribution Rates as a Percent of Payroll



Employer Contribution Rate (continued)

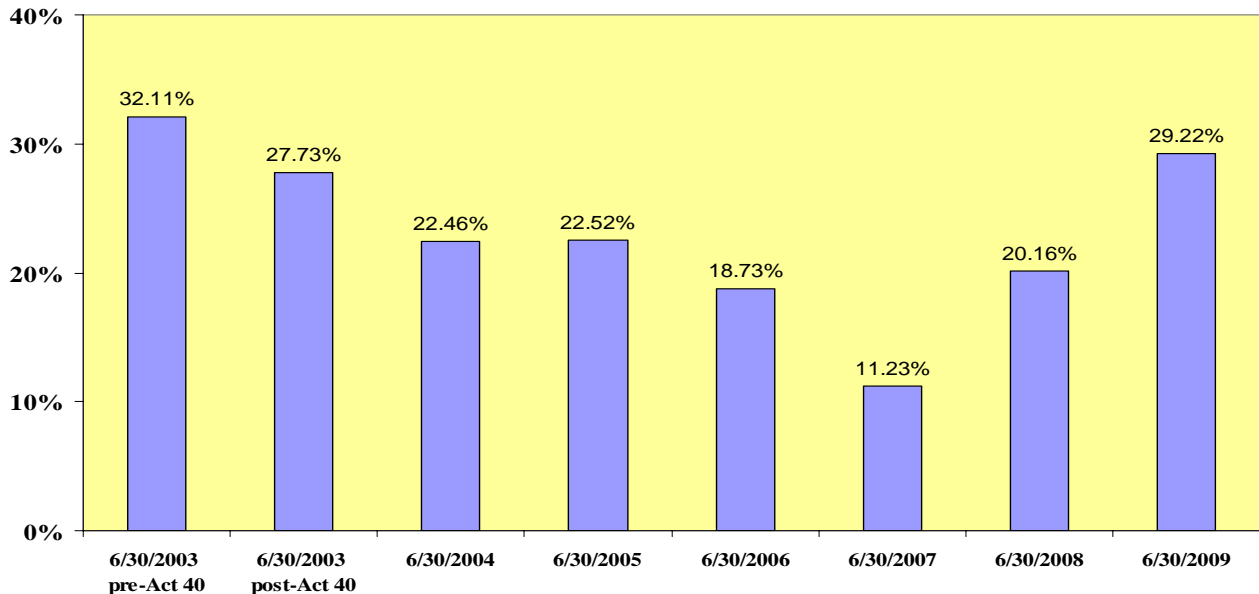
Significant Projected Employer Contribution Rate Increase

The current funding issue confronting PSERS represents the greatest challenge the System has faced in its history. The funding issue commonly referred to as the “rate spike” or “rate plateau” refers to the significant increase in the employer contribution rate in FY 2012-2013 and following years that is paid by school employers and the Commonwealth to PSERS to fund pension benefits.

The rate increase was first projected in the June 30, 2003 actuarial valuation. This projection took into consideration the actuarial impact of the pension benefit enhancement enacted in 2001 (Act 9 of 2001), a cost-of-living adjustment for retirees in 2002 (Act 38 of 2002), a major downturn in the investment markets between 2001 and 2003 and a series of legislative actions (Act 38 of 2002 and Act 40 of 2003) that changed the basic funding methodologies for PSERS and suppressed the employer contribution rate for a period of ten years. In addition, the recent historic economic downturn during FY 2008-2009 and the accompanying investment losses experienced by PSERS (-26.54% for FY 2008-2009) compounded the existing funding issue.

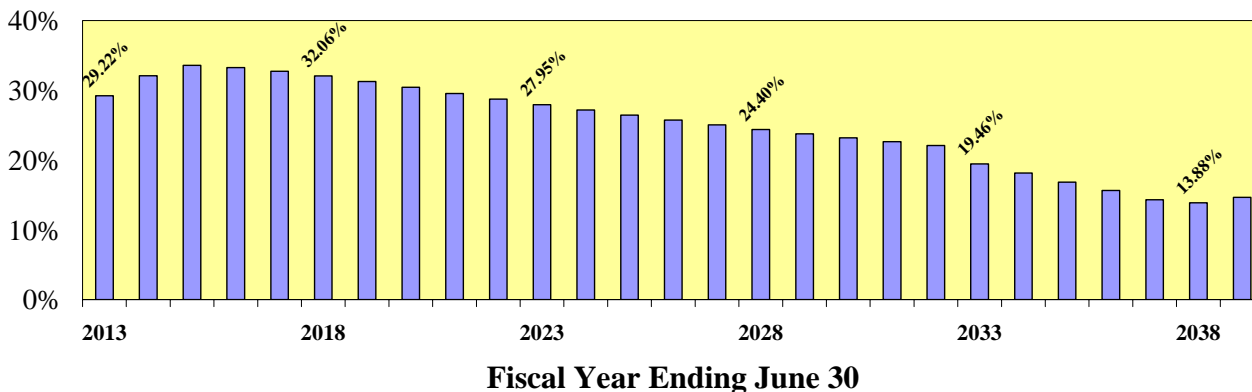
While a few months remain until the end of the current fiscal year on June 30th and the investment markets have improved, PSERS cannot earn its way out of the funding issue facing the System. The projected rate spike in FY 2012-2013 is currently 29.22% and the actual peak in the rate now appears two years later in FY 2014-2015 at 33.60%. As the chart below reflects, the projected rate spike decreased in the middle part of the decade due to excellent investment returns. However, the investment returns in the last two fiscal years ended June 30, 2009 have reversed the previous improvement in the projected rate spike in FY 2012-2013.

Evolution of PSERS 2012-2013 Rate Spike Projection



Employer Contribution Rate (continued)

Total Employer Contribution Rate Projection



Fundamentally, there are only three ways to address the funding issues at the System. They include:

- Increasing the funding of the System,
- Decreasing/cutting the costs/liabilities of the System, and/or
- Deferring the liabilities of the System.

Increase Funding

Increasing funding to the System is already projected to occur. Employer contribution rates have begun to rise and are projected to increase significantly in FY 2012-2013. High double digit employer contribution rates continue well into the future beyond FY 2012-2013.

Increased employee or member contributions can only occur prospectively for new employees due to constitutional impairment of contract issues and therefore will not have a significant impact on the current unfunded liabilities of the System.

Significantly increased investment returns could potentially impact the projected rate spike and decrease the funding issues. However, while the investment markets have improved and PSERS is currently on track to earn a positive return above its annual actuarial assumption of 8.00%, there is not enough time to earn investment returns that would significantly impact the rate in FY 2012-2013. In addition current investment market conditions remain volatile and any future investment downturns could further compound the funding issues at the System. It should be noted that over the past 25 years, even with the recent negative performance, PSERS investment returns have exceeded its investment rate of return assumption.

Employer Contribution Rate (continued)

Other options to increase funding include seeking another source of funding such as the use of federal stimulus funds or the proceeds of a pension obligation bond (POB). That said, it remains unclear if federal stimulus funds can legally be directly to fund pension contributions and there has been little discussion of a formal Federal bailout of public pension funds. POB's are debt instruments issued by a governmental entity to fund all or a portion of the unfunded actuarially accrued liabilities for pension and/or other postemployment benefits. These instruments have significant risk involved to the plan sponsor/bond issuer if the pension plan's investment returns are less than the debt costs.

Decrease/Cut Costs and Liabilities

Decreasing or cutting the costs or liabilities of the System to potentially solve funding issues would have a limited impact on the FY 2012-2013 rate spike or short-term funding issues because it can only be done prospectively for new employees.

Any such changes to pension benefits would have to be prospective only, (meaning impacting new hires after the effective date of the change), to avoid the PA Constitution's prohibition against the impairment of a contract (Article I, Section 17). The courts have ruled that PSERS' pension benefits are contracts with the existing members of the System, regardless of vesting, and thus subject to the constitutional impairment of contract prohibition (See e.g. *Pennsylvania Federation of Teachers v. School District of Philadelphia*, 484 A.2d 751 (Pa. 1984) and *American Federation of State, County and Municipal Employees, AFL-CIO, v. Commonwealth*, 479 A.2d 962 (Pa. 1984)). These changes may have more impact on the long term funding issues of the System. Possible methods could include: reducing the multiplier/repealing Act 2001-9, changing the terms of retirement, returning to a 10-year vesting period, and making the withdrawal of a member's contributions cost neutral to PSERS.

Another possible change includes converting PSERS to a Defined Contribution (DC) or Hybrid plan. A DC plan is a pension plan where the member's pension benefit will fluctuate up and down with investment performance and the member bears the investment risk. An example of a DC plan is a 401(k) plan. A Hybrid plan typically is a combination of both DC and defined benefit components. The Pennsylvania School Boards Association (PSBA) has proposed converting PSERS to a Hybrid plan for new employees. Legislation was introduced in the House in January 2010 and an identical bill is pending introduction in the Senate.

Because of the prospective nature of any benefit modification, changing the benefit structure would only reduce the long term liabilities of the System and thus reduce the rate plateau. It would have little impact on the short term liabilities facing the System in FY 2012-2013.

Defer Liabilities

Deferring liabilities into the future to marginally postpone the impact of funding issues at the System is another option to potentially help address the funding issue at the System. Such changes could lower the rate spike but would extend the duration of the rate plateau as the impact would extend funding of the unfunded liability over a longer period of time. Further adjustments to the actuarial funding methods at the System could be made although no single or combination of actuarial changes resolves the rate spike and funding issue.

Employer Contribution Rate (continued)

No Single Solution to the Funding Issue

While increasing the funding, decreasing/cutting the costs and liabilities, and/or deferring the liabilities all would impact the funding issues; there is no silver bullet to resolve PSERS' funding issues. A solution will likely be a combination of several approaches and will only smooth out the rate plateau and lower the peak. **Under all options there will be a need for significant additional funding to the System than what has been contributed over the past ten years.**

In addition, some suggestions may aggravate the funding issue. Converting PSERS to a DC or Hybrid plan may have a long term impact on funding issues but it will not affect the current liabilities already owed or resolve the immediate funding concerns of the System. In fact it may aggravate the Commonwealth's and School Employer's cash flow problems as they will be supporting two pension plans.

Educational Efforts

Finally, PSERS will continue to be very public with the funding issue in an attempt to raise awareness. Over the past year PSERS has significantly increased its educational efforts regarding the funding issues facing the System in the near future. PSERS Executive Director has traveled across the Commonwealth meeting with school districts, school boards, retiree and active member organizations and legislators and their staff. The purpose of these presentations is to make sure both school employers and the Commonwealth are aware of the impact this issue will have on their budgets and the options available to resolve the issue.

PSERS has also created a resource page on its website to help PSERS' members, the media, legislators and their staff, and the general public better understand the System and the complexity of the funding challenges facing PSERS, the Commonwealth and school employers. To view the resource page, go to the following link on PSERS' website.

http://www.psers.state.pa.us/press/pension_funding_issues/index.html

The resolution of the current funding issues confronting PSERS is a vital imperative for the Agency. PSERS remains committed to providing all available assistance to the Governor, General Assembly and School Employers to deal with the rate spike and subsequent rate plateau as soon as possible.

Consultants' Fees

Consultants' Fees (**\$50,000 and Over**)

The following benefit, investment, information technology and financial professional service firms were under contract to provide services to PSERS during the fiscal year ended June 30, 2009.

<u>Firm</u>	<u>Services Provided</u>	<u>Consulting Fee</u>	
CoreSource, Inc.	Postemployment healthcare benefits administration and claims adjudication	\$ 9,984,091	*
Vitech Systems Group, Inc.	V3 Benefit System Services	3,704,440	*
The Segal Company	Actuarial services and consulting for HOP and prescription drug plan	2,233,306	*
Rx Solutions, Inc.	Administration of postemployment healthcare benefits and prescription drug plan	1,611,620	*
Portfolio Advisors, LLC	Private market consulting	1,500,000	
Financial Control Systems, Inc.	Investment accounting application service provider	676,000	
Wilshire Associates	General investment consulting	577,000	
Buck Consultants LLC	Pension benefit actuarial services	557,001	*
Independent Pharmaceutical Consultants, Inc.	Administration of postemployment healthcare benefits and prescription drug plan	425,362	*
Courtland Partners, Ltd.	Real Estate investment consulting	228,000	
Glass, Lewis & Co., LLC	Proxy voting	213,000	
Clifton Gunderson LLP	Financial audit of pension system and postemployment healthcare programs	135,820	*
Gunther International Ltd.	Communication and mailing services	111,650	*
Institutional Shareholder Services	Corporate compliance/class actions consulting	68,000	

* Amounts as reported in PSERS' Comprehensive Annual Financial Report

Legislation Information

Legislation Information

There has been no legislation enacted affecting the operations or the membership of the Public School Employees' Retirement System, thus far into the 2009-2010 Legislative Session.

- *PSEERS 2010/2011*

Budget

- *Directed Commissions*

Recapture Program

Budget

PSERS 2010/2011 Budget

PSERS 2010/2011 Budget

	<u>Actual</u> <u>2008/2009</u>	<u>Available</u> <u>2009/2010</u>	<u>Request</u> <u>2010/2011</u>
Total Personnel Expenses	\$ 23,616,684	\$ 25,476,998	\$ 26,740,527
<u>Budgetary Reserve</u>	229,000	575,400	-
<u>Operating Expenses</u>			
Travel	144,160	229,000	227,000
Training	56,546	116,000	134,000
Telecommunication	592,596	741,000	672,000
Electricity	40,221	60,000	60,000
Consultant Services	609,242	766,000	927,000
Legal Services/Fees	-21,035	1,000	106,000
Specialized Services	326,690	485,000	471,000
Advertising	10,006	10,000	10,000
EDP Contract Service	6,713,594	6,203,000	6,717,000
Contr Maint Svcs - EDP	135,969	124,000	118,000
Contr Maint Svcs – non EDP	207,786	308,000	272,000
Contracted Repairs	6,869	16,000	15,000
EDP & Other Rental	711,579	1,005,000	927,000
Real Estate Rental	1,769,475	1,932,000	1,979,000
Office Supplies	220,947	388,000	339,000
Education Supplies	13,899	13,000	16,000
Medical Supplies	8,760	-	-
EDP Software	149,490	105,000	100,000
Other Computer Equipment	160,978	103,000	83,000
Furniture & Fixtures	34,466	51,000	51,000
Other Equipment & Supplies	313,626	392,000	345,000
Postage	1,247,376	1,615,000	1,478,000
Freight Charges	9,768	17,000	15,000
Printing	401,465	490,000	478,000
Subscriptions	27,601	29,000	62,000
Memberships	24,916	37,000	37,000
Conference Expense	35,519	73,000	80,000
Insurance	16,846	21,000	23,000
Interest Penalties	173	-	-
Other Operational Expenses	1,342,910	1,294,602	1,632,000
Total Operating Expenses	\$ 15,312,439	\$ 16,624,602	\$ 17,374,000
<u>Fixed Assets</u>			
Automobiles	-	-	75,000
EDP Computers & Peripherals	-	500,000	40,000
Telecommunications Equipment	-	50,000	-
Total Fixed Assets	-	\$ 550,000	\$ 115,000
Total Budget	<u>\$ 38,929,123</u>	<u>\$ 43,227,000</u>	<u>\$ 44,229,527</u>
Personnel Augmentations	<u>842,730</u>	<u>900,000</u>	<u>953,000</u>
Total with Augmentations	<u>\$ 39,771,853</u>	<u>\$ 44,127,000</u>	<u>\$ 45,182,527</u>

Agency: **Public School Employees' Retirement System**
 Appropriation: **Administrative (1053610000)**

Page # of Governor's Executive Budget:

Pp.

(\$ Amounts in Thousands)

I. Summary Financial Data

	2008/2009 <u>Actual</u>	2009/2010 <u>Available</u>	2010/2011 <u>Budget Request</u>
State Funds	\$38,929	\$43,227	\$44,230
Federal Funds	0	0	0
Augmentations	<u>842</u>	<u>900</u>	<u>953</u>
Total	\$39,771	\$44,127	\$45,183

IA. Requested Supplementals

	2008/2009	2009/2010	2010/2011
State Funds	\$0	\$0	\$0
Federal Funds	0	0	0
Augmentations	<u>0</u>	<u>0</u>	<u>0</u>
Total	\$0	\$0	\$0

II. Detail by Major Object

(\$ Amounts in Thousands)

	2008/2009 <u>Actual</u>	2009/2010 <u>Available</u>	2010/2011 <u>Budget Request</u>	Change Budgeted vs. Available	Percent Change
<i><u>Personnel</u></i>					
State	\$23,617	\$26,052	\$26,741	\$689	2.64%
Federal	0	0	0	0	NA
Augmentations	<u>842</u>	<u>900</u>	<u>953</u>	<u>53</u>	5.89%
Total	\$24,459	\$26,952	\$27,694	\$742	2.75%
<i><u>Operating</u></i>					
State	\$15,312	\$16,625	\$17,374	\$749	4.51%
Federal	0	0	0	0	NA
Augmentations	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	NA
Total	\$15,312	\$16,625	\$17,374	\$749	4.51%
<i><u>Fixed Assets</u></i>					
State	\$0	\$550	\$115	(\$435)	-79.09%
Federal	0	0	0	0	NA
Augmentations	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	NA
Total	\$0	\$550	\$115	(\$435)	-79.09%
<i><u>Total Funds</u></i>					
State	\$38,929	\$43,227	\$44,230	\$1,003	2.32%
Federal	0	0	0	0	NA
Augmentations	<u>842</u>	<u>900</u>	<u>953</u>	<u>53</u>	5.89%
Total	\$39,771	\$44,127	\$45,183	\$1,056	2.39%

Agency: **Public School Employees' Retirement System**

Appropriation: **Administrative (1053610000)**

(\$ Amounts in Thousands)

III. History of Lapses

	2008/2009 <u>Actual</u>	2009/2010 <u>Available</u>	2010/2011 <u>Budget Request</u>
State Funds	\$2,885	\$1,696	\$0

	<u>12/31/2008</u>	<u>12/31/2009</u>	2010/2011 <u>Budget Request</u>
IV. Complement Information			
State Funded			
<i>Authorized</i>	302	302	302
<i>Filled</i>	281	281	302
Federally Funded			
<i>Authorized</i>	0	0	0
<i>Filled</i>	0	0	0
Other Funded			
<i>Authorized</i>	0	0	0
<i>Filled</i>	<u>0</u>	<u>0</u>	<u>0</u>
Total			
<i>Authorized</i>	302	302	302
<i>Filled</i>	281	281	302

V. Derivation of Request/Legislative Citations/Disbursement Criteria

Derivation of Request:

None.

Legislative Citations:

24 Pa. C.S. §8101 et seq.

Disbursement Criteria:

This appropriation funds administrative costs for the Executive Office, Office of Financial Management, Human Resource Office, Bureau of Administration, Bureau of Information Management, Information Technology Office, Bureau of Benefits Administration, Bureau of Communications & Counseling, and the Investment Office. Disbursements are made on the basis of approved positions, established employee benefits, and invoices submitted for operating expenses and fixed assets.

Agency: **Public School Employees' Retirement System**
 Appropriation: **Administrative (1053610000)**
 (\$ Amounts in Thousands)

VI. Explanation of Changes

	<u>State \$</u>	<u>Federal \$</u>	<u>Other \$</u>	<u>Total \$</u>
Non-recurring				
Operational				
EDP Software				
Web Ex License, Team Track Licenses, & Safeboot for Laptops	\$11	\$0	\$0	\$11
Other Computer Equipment				
Replace older Printers, new PCs & Printers for 3-4 new Board Members. Laptops for Investment Accounting managers.	\$10	\$0	\$0	\$10
Other Equipment				
Includes printer for photo badging system	-\$17	\$0	\$0	-\$17
Fixed				
Five replacement automobiles. (PSERS owns 17 automobiles & Leases 1 van used by the Mail Center)	\$75	\$0	\$0	\$75
EDP Computers & Peripherals				
Replacement of Domain Controllers	-\$460	\$0	\$0	-\$460
<u>Cost to Carry</u>				
<u>Personnel</u>				
Budgetary Reserve in 2009/2010 in Personnel	-\$575	\$0	\$0	-\$575
No New Positions, General Pay & Longevity Increases	\$782	\$0	\$0	\$782
Decrease in Wages. Per Diem for Board Members, request includes 27 full & part time wage positions	-\$153	\$0	\$0	-\$153
Increase in Overtime	\$22	\$0	\$0	\$22
Social Security Contributions, Medicare, Retirement Contributions, State Worker's Compensation & Insurance & Employee Life Insurance	\$197	\$0	\$0	\$197
Hospitalization & Health Benefits State Share	\$403	\$0	\$0	\$403
Leave Payout Assessment	\$13	\$0	\$0	\$13
Cross Charges	\$0	\$0	\$53	\$53
Operational				
Decrease in Travel Increase in Training	\$16	\$0	\$0	\$16
Telephone- Recurring, & Non Recurring & Telephone Equip	-\$69	\$0	\$0	-\$69
Financial Audit	\$136	\$0	\$0	\$136
Legal Fees	\$98	\$0	\$0	\$98
Board Elections	\$8	\$0	\$0	\$8
Clerical Pool	\$41	\$0	\$0	\$41
IES Billing	-\$6	\$0	\$0	-\$6
SEAP	\$7	\$0	\$0	\$7
Decrease Comptroller Payroll & Travel	-\$68	\$0	\$0	-\$68
Increases/Decreases in State Recycling, Vital Records, Iron Mountain, Video Audio, Employer Statements, GFOA & Consulting	\$4	\$0	\$0	\$4
Increase in Data PH Open Systems (ongoing services provided by the Data Powerhouse)	\$200	\$0	\$0	\$200
CAI - Network support Staff Augmentation	-\$59	\$0	\$0	-\$59
Computer Aid Inc - Aqua Logic Staff augmentation needed for Aqua Logic conversion (From PSERS 3-year IT Strategic plan)	\$180	\$0	\$0	\$180

Agency: **Public School Employees' Retirement System**
 Appropriation: **Administrative (1053610000)**
 (\$ Amounts in Thousands)

VI. Explanation of Changes (continued)

	<u>State \$</u>	<u>Federal \$</u>	<u>Other \$</u>	<u>Total \$</u>
Boardroom Sound System Maintenance	\$1	\$0	\$0	\$1
Lexis/Nexis	-\$3	\$0	\$0	-\$3
Tech Writer	\$40	\$0	\$0	\$40
Servers/SAN at DPH	\$100	\$0	\$0	\$100
Vitech Systems Group - Change Requests	\$20	\$0	\$0	\$20
V3 Support Training to be able to support V3 (ie. Admin functions, etc.)	\$5	\$0	\$0	\$5
Increase - Lawson Upgrade Services & Image Tech	\$10	\$0	\$0	\$10
Decrease in Contracted Maintenance Services - EDP	-\$41	\$0	\$0	-\$41
Increase in Contracted Maint Services - Non EDP	\$4	\$0	\$0	\$4
Decrease in Contracted Repairs - Non EDP	-\$38	\$0	\$0	-\$38
Decrease in Contracted Repairs - Motorized Equip	-\$1	\$0	\$0	-\$1
Decrease in EDP Rental	-\$86	\$0	\$0	-\$86
Increase in Real Estate Rental	\$47	\$0	\$0	\$47
Increase in Vehicle Rental	\$2	\$0	\$0	\$2
Decrease in Office Equipment Rental	-\$27	\$0	\$0	-\$27
Decrease in Other Rentals	-\$5	\$0	\$0	-\$5
Decrease in Office Supplies	-\$45	\$0	\$0	-\$45
Decrease in Medical Supplies	-\$4	\$0	\$0	-\$4
Increase in Educational Supplies	\$3	\$0	\$0	\$3
Decrease in Motorized Equipment Supplies	-\$5	\$0	\$0	-\$5
Postage Decrease	-\$137	\$0	\$0	-\$137
Decrease in Printing - Annual Updates to members, CAFR, newsletters & other member communications, Fiche to Image conversion & increase of imaging documents, & their conversion to microfilm (HRF)	-\$12	\$0	\$0	-\$12
Increase in Subscriptions	\$33	\$0	\$0	\$33
Increase in Conference Expenses - Includes Board Meetings, Field Offices Room Rentals & Exit Counseling Meetings & Employee Recognition Program	\$7	\$0	\$0	\$7
Auto Insur, Emp Liability Insur, Tort Claims, Emp Performance Bonds, Excess Property Insurance	\$2	\$0	\$0	\$2
Decrease in Graphic Services	-\$2	\$0	\$0	-\$2
Increase in Shared services billings from DGS, Civil Service, Treasury, etc	\$339	\$0	\$0	\$339

Directed Commissions Recapture Program Budget

Directed Commissions Recapture Program

(Dollar Amounts in Thousands)

(unaudited)

Directed Commissions Recapture Budget is a program whereby a portion of commissions incurred by PSERS through investment trading activity is returned to PSERS. These funds, which are held in a restricted revenue account at Treasury, can be used for the administration of the Fund or can be reinvested back into the asset allocation through a transfer to the PSERS Retirement Account. Expenditures paid from the Directed Commissions Recapture Program Budget have the same approval process as any other expenditure made by the Fund.

Note: Beginning with the 2008-2009 Fiscal Year – Investment Information Services have been included as part of the Investment Related Expense Appropriation 5003300000.

**Directed Commissions Recapture Program -
Directed Commissions Appropriation #6012700000**

	<u>Actual</u> <u>2008-2009</u>	<u>Available</u> <u>2009-2010</u>	<u>Budget Request</u> <u>2010-2011</u>
Budgetary Reserve		\$1,000,000	\$1,000,000
Total	-	\$1,000,000	\$1,000,000

- Investment Policy, Objectives, and Performance
- Asset Allocation
- Investment Program Summary
- Investment Advisory Fees
- Internal Equity Trading Desk
- Public Market Emerging Investment Manager Program

Investment Policy, Objectives, and Performance

Investment Policy

The Public School Employees' Retirement Board of Trustees (the Board) is responsible for, among other things, the formulation of an Investment Policy (the Policy) for the Public School Employees' Retirement System (the System). As articulated in the Public School Employees' Retirement Code, the Board and Staff delegated with investment authority must act in a manner consistent with the Prudent Investor Standard, which requires "the exercise of that degree of judgment, skill and care under the circumstances then prevailing which persons of prudence, discretion and intelligence who are familiar with such matters exercise in the management of their own affairs not in regard to speculation, but in regard to the permanent disposition of the fund, considering the probable income to be derived therefrom as well as the probable safety of their capital." 24 Pa. C.S. §8521(a). The Prudent Investor Standard recognizes modern portfolio theory and guides investment and management decisions respecting individual assets so that the trade-offs between risk and return for each asset are considered in the context of an overall investment strategy.

The System's Investment Policy, which is available at <http://www.psers.state.pa.us/invest/invest.htm>, reflects the many implications of the Prudent Investor Standard. The Board reviews the Policy at least annually, and may make more frequent changes as necessary. The Policy establishes clear criteria for the management of the assets by or on behalf of the Board. For example:

- The Board, PSERS' staff, investment consultants, and investment managers are assigned appropriate responsibilities and made to clearly understand the objectives and policies of the Board and the System;
- Allocation plans are prepared to guide the investment of the System's assets;
- Guidelines are established for each investment category so that asset quality, diversification, and return can be monitored;
- Investment managers are given guidance and limitations on the investment of the System's assets; and,
- The Board has created a meaningful basis for evaluating the investment performance of individual investment managers, as well as for evaluating overall success in meeting its objectives.

General Investment Objectives

The System seeks to provide benefits to its members through a carefully planned and well-executed investment program. The overall investment objective of the Board is to provide adequate funding for member benefits. Realization of this overall return objective would be sufficient to achieve funding adequacy (defined as when the actuarial market value of assets is at least equal to the System's projected benefit obligations) on an inflation-adjusted basis. The Policy also identifies the following general investment objectives and constraints:

Return Objectives

- The System has an overall return objective of meeting or exceeding the actuarial rate (currently 8.0%) over the long term;
- The assets of the System shall be invested to maximize the returns for the level of risk taken; and,
- The System shall strive to achieve a return that exceeds the Policy Index.

Risk Objectives

- The assets of the System shall be diversified to minimize the risk of losses within any one asset class, investment type, industry or sector distribution, maturity date, or geographic location; and,
- The System's assets shall be invested so that the probability of investment losses (as measured by the Policy Index) in excess of 15% in any one year is no greater than 2.5% (or two standard deviations below the expected return).

Constraints

- The System shall maintain adequate liquidity to meet required benefit payments to the System's beneficiaries;
- The System's assets shall be invested in a manner that is consistent with the System's long-term investment horizon; and,
- As a tax-exempt investor, the System's assets may be invested without distinction between returns generated from income and returns generated from capital gains.

Investment Performance
Net of Fees
(for the period ended June 30, 2009)

Annualized Total Returns (%)

<i>Asset Class</i>	<i>One Year</i>	<i>Three Year</i>	<i>Five Year</i>	<i>Ten Year</i>
PSERS U.S. Equities	-29.37	-9.90	-2.81	-0.49
Domestic Equity Policy Index (1)	-26.30	-8.09	-1.58	-1.31
PSERS Non-U.S. Equities	-25.66	-4.15	6.14	4.40
International Equity Policy Index (2)	-27.01	-4.98	5.20	3.06
PSERS U.S. Fixed Income	-1.00	4.13	4.21	5.84
Domestic Fixed Income Policy Index (3)	4.75	6.54	5.17	6.06
PSERS Global Fixed Income	0.98	5.17	4.98	5.80
Global Fixed Income Policy Index (4)	2.54	6.46	5.40	6.03
PSERS Commodities	-45.09	N/A	N/A	N/A
DJ UBS Commodity Index	-47.08	N/A	N/A	N/A
PSERS Real Estate (5)	-42.68	-10.95	4.26	7.55
Blended Real Estate Index (6)	-16.35	1.46	8.52	9.33
PSERS Alternative Investments (5)	-27.23	5.67	12.52	8.89
Venture Economics Median Return, Vintage Year Weighted	-13.36	0.59	3.21	1.13
PSERS Absolute Return (7)	N/A	N/A	N/A	N/A
Absolute Return of 8.0% annualized	N/A	N/A	N/A	N/A
PSERS Cash (8)	N/A	N/A	N/A	N/A
Merrill Lynch U.S. Treasury Bill 0 – 3 Months Index	N/A	N/A	N/A	N/A
Total Fund (9)	-26.54	-4.26	2.68	3.28
Policy Index	-20.67	-2.75	2.51	2.46

- (1) MSCI U.S. Broad Market Index effective April 1, 2009; previously was the Dow Jones Wilshire 5000 Index.
- (2) MSCI All Country World ex. U.S. Investable Market Index effective July 1, 2008; previously was the MSCI ACW ex. U.S. Index. The benchmark was 30% hedged to the U.S. dollar from July 1, 2006 to March 31, 2009; otherwise, the benchmark is unhedged.
- (3) Returns presented are a blend of the Barclays Capital U.S. Universal Index (34.9%), Barclays Capital U.S. TIPS Index (Series-L) (23.2%), and Barclays U.S. High Yield Index (41.9%) effective April 1, 2009. The weights to these indexes have varied in previous quarters. Prior to April 1, 2007, the Barclays Capital Aggregate Bond Index was used in place of the Barclays Capital U.S. Universal Index.
- (4) Barclays Multiverse Index effective April 1, 2007; previously was the Barclays Global Aggregate Bond Index.
- (5) Returns reported on a one-quarter lag, except for publicly traded real estate security investments.
- (6) Returns presented are a blend of the FTSE EPRA/NAREIT Global Real Estate Index (13.6%) and the NCREIF Index (86.4%). The NCREIF Index is reported on a one-quarter lag. Prior to October 1, 2007, the Dow Jones Wilshire Real Estate Securities Index was used in place of the FTSE EPRA/NAREIT Global Real Estate Index.
- (7) Absolute Return started April 1, 2009.
- (8) Cash started December 1, 2008.
- (9) Over the past 25 years the Fund earned an annualized rate of return of 9.23 percent which remains above the Fund's current assumed actuarial rate of return of 8.00 percent.

Estimated Investment Performance
Net of Fees
(for the period ended December 31, 2009)

Annualized Total Returns (%)

<i>Asset Class</i>	<i>One Year</i>	<i>Three Year</i>	<i>Five Year</i>	<i>Ten Year</i>
PSERS U.S. Equities	33.94	-6.39	0.01	0.91
Domestic Equity Policy Index (1)	28.22	-5.27	0.92	-0.27
PSERS Non-U.S. Equities	45.88	-1.57	7.70	4.03
International Equity Policy Index (2)	45.36	-2.46	6.58	3.25
PSERS U.S. Fixed Income	22.54	6.63	5.44	6.95
Domestic Fixed Income Policy Index (3)	27.91	9.00	6.52	7.18
PSERS Global Fixed Income	19.43	7.82	5.09	6.87
Global Fixed Income Policy Index (4)	8.03	6.97	4.51	6.39
PSERS Commodities	33.40	-0.43	N/A	N/A
DJ UBS Commodity Index	18.89	-3.84	N/A	N/A
PSERS Real Estate (5)	-39.17	-17.72	-0.60	5.80
Blended Real Estate Index (6)	N/A	N/A	N/A	N/A
PSERS Alternative Investments	-9.71	6.94	13.45	9.62
Venture Economics Median Return, Vintage Year Weighted (6)	N/A	N/A	N/A	N/A
PSERS Absolute Return (7)	N/A	N/A	N/A	N/A
Absolute Return of 8.0% annualized	N/A	N/A	N/A	N/A
PSERS Cash (8)	1.14	N/A	N/A	N/A
Merrill Lynch U.S. Treasury Bill 0 - 3 Months Index	0.15	N/A	N/A	N/A
Total Fund (9)	11.21	-3.84	3.20	3.50
Policy Index (6)	N/A	N/A	N/A	N/A

- (1) MSCI U.S. Broad Market Index effective April 1, 2009; previously was the Dow Jones Wilshire 5000 Index.
- (2) MSCI All Country World ex. U.S. Investable Market Index effective July 1, 2008; previously was the MSCI ACW ex. U.S. Index. The benchmark was 30% hedged to the U.S. dollar from July 1, 2006 to March 31, 2009; otherwise, the benchmark is unhedged.
- (3) Returns presented are a blend of the Barclays Capital U.S. Universal Index (34.9%), Barclays Capital U.S. TIPS Index (Series-L) (23.2%), and Barclays U.S. High Yield Index (41.9%) effective April 1, 2009. The weights to these indexes have varied in previous quarters. Prior to April 1, 2007, the Barclays Capital Aggregate Bond Index was used in place of the Barclays Capital U.S. Universal Index.
- (4) Barclays Multiverse Index effective April 1, 2007; previously was the Barclays Global Aggregate Bond Index.
- (5) Returns reported on a one-quarter lag, except for publicly traded real estate security investments.
- (6) The index returns were not available at the time this document was produced.
- (7) Absolute Return started April 1, 2009.
- (8) Cash started November 1, 2008.
- (9) Over the past 25 years the Fund earned an annualized rate of return of 9.27 percent which remains above the Fund's current assumed actuarial rate of return of 8.00 percent.

Asset Allocation

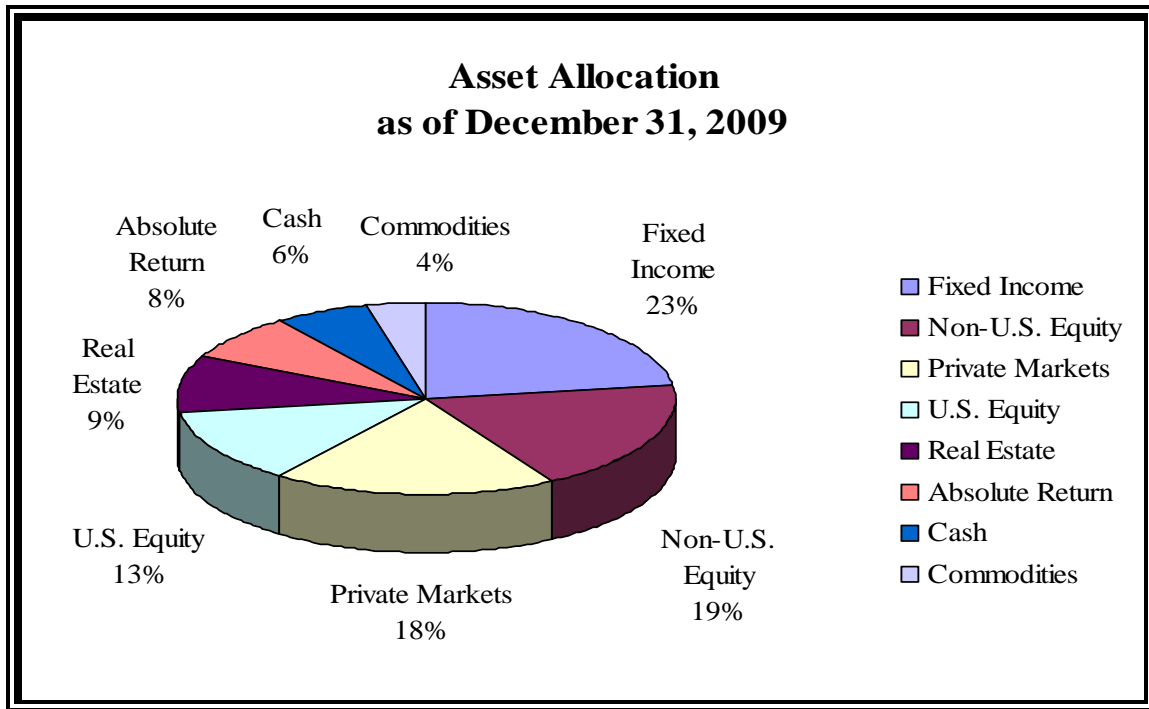
Asset Allocation (as of December 31, 2009)

The Board reviews the long-term asset allocation targets of the System at least annually. In establishing the asset allocation plan, the Board will consult with its actuary, consultants, investment staff, and other sources of information it deems appropriate in formulating this allocation. The purpose of the asset allocation is to meet the long-term financial needs and investment objectives of the System.

The following represents PSERS' asset allocation as of December 31, 2009 (unaudited):

<u>Asset Class</u>	<u>Market Value (in millions)</u>	<u>Percentage of Total</u>	<u>Target Allocation</u>	<u>Target Allocation Range</u>
Fixed Income	\$ 10,663.0	22.8%	24.5%	21 - 28%
Non-U.S. Equity	8,790.0	18.9	17.8	13 - 23
Private Markets	8,553.6	18.3	18.5	-
U.S. Equity	5,930.8	12.7	13.2	8 - 18
Real Estate (Public and Private)	4,484.8	9.6	9.5	-
Absolute Return	3,607.0	7.7	7.5	4 - 12
Cash*	2,891.7	6.2	5.0	0 - 10
Commodities	<u>1,771.3</u>	<u>3.8</u>	<u>4.0</u>	0 - 8
Totals	\$ <u>46,692.2</u>	<u>100.0%</u>	<u>100.0%</u>	

*- Cash represents the total short-term investment fund (STIF) managed by PSERS in the PSERS Proprietary Fund. Cash is unitized and the managers in the various asset classes are allocated units of STIF. For purposes of this schedule, units of STIF are not included in the various asset classes. For example, a U.S. Equity manager may manage \$200 million, but if that manager has \$10 million in STIF, \$190 million would be included in U.S. Equity and \$10 million would be included in Cash.



Asset Allocation
(as of December 31, 2009)
(continued)

Number of Investment Managers and Portfolios

Public Market Asset Classes (ex. Real Estate):

PSERS public market equity, fixed income, and commodity asset classes used 71 external investment managers who were responsible for 80 portfolios, and 6 internal portfolio managers who were responsible for 9 portfolios. There were 9 external public market investment managers with portfolios in multiple asset classes. A further breakdown of the external and internal portfolio managers follows:

Public Market Asset Classes (excluding Public Market Real Estate):

	<i>Portfolio Managers</i>	<i>Portfolios/Accounts</i>
<i>Non-U.S. Equity Investments:</i>		
External*	21	23
Internal	1	1
<i>U.S. Equity Investments:</i>		
External*	15	15
Internal	2	3
<i>Fixed Income Investments:</i>		
External*	18	23
Internal**	2	4
<i>Commodities:</i>		
External	5	5
<i>Absolute Return:</i>		
External*	11	12
Internal	1	1
<i>Cash:</i>		
Internal	1	1
<i>Securities Lending:</i>		
External	1	2
<i>Total</i>	77	89
<i>Total External*</i>	71	80
<i>Total Internal</i>	6	9

* The Public Market Emerging Investment Manager Program consisted of 17 portfolio managers each managing a single portfolio. There were 8 U.S. Equity, 3 Non-U.S. Equity, 3 Fixed Income portfolios, and 3 Absolute Return portfolios in the Program.

** PSERS managed \$189.9 million for the System's healthcare account.

Private Markets and Real Estate:

PSERS private markets and real estate (public and private markets) asset classes used 41 active external general partners to invest in 78 limited partnership interests of various private market real estate, private debt, private equity, and venture capital funds. PSERS also used 6 external and 2 internal real estate investment managers who were responsible for 6 public market real estate portfolios. Finally, PSERS had 6 external and 2 internal real estate asset managers who oversee the direct management of 6 separate real estate accounts.

Investment Program Summary

Investment Program Summary

Summary of PSERS' U.S. Equity Investments

(as of December 31, 2009)

U.S. Equities represent one of eight major asset classes that PSERS uses to diversify the investments of the Fund. PSERS' investment plan diversifies equity investments and balances equity management styles. PSERS contracts with external investment managers and hires internal portfolio managers to manage U.S. portfolios.

Policy

U.S. Equities are utilized by the Fund primarily because their expected large return premiums versus inflation will, if realized, help preserve and enhance the real value of the Fund over long periods of time. The U.S. Equity asset class is to be managed on a total return basis.

U.S. Equity investments shall consist almost entirely of publicly-traded securities listed on the New York, American, and Nasdaq Stock Exchanges or derivatives such as swaps or listed futures to replicate the performance of U.S. equity indexes such as the S&P 500 Index. Swaps and futures are employed by PSERS to equitize cash and portable alpha portfolios.

PSERS' Asset Allocation targets an eventual allocation of 13.25% of assets to U.S. Equities. It assigns (i) the investment of 80% of U.S. Equities in large capitalization stocks and 20% in medium/small/micro capitalization stocks.

Market Value as of December 31, 2009: \$5,930.8 million, or 12.7% of the Fund's total market value.

Number of External Investment Managers: PSERS had contracts with 15 external investment managers responsible for various U.S. Equity portfolios (including 8 Public Market Emerging Manager Program managers).

Number of Internal Portfolio Managers: PSERS had two employees managing various U.S. Equity portfolios.

Types of Investment Portfolios at December 31, 2009:

- 75.1% large capitalization stock strategies, 20.7% medium/small capitalization stock strategies, and 4.2% in micro capitalization stock strategies
- 87.2% passively-managed portfolios, and 12.8% actively-managed stock selection portfolios
- 87.2% was managed by internal portfolio managers and 12.8% is managed by external investment managers

Summary of PSERS' U.S. Equity Portfolios (unaudited)
(as of December 31, 2009)

	<u>Market Value</u> (in millions)	<u>% of</u> <u>U.S.</u> <u>Equities</u>	<u>% of</u> <u>Total</u> <u>Fund</u>
<u>Passively Managed Portfolios</u>			
PSERS S&P 400 Index Fund	\$ 441.0	7.4%	0.9%
PSERS S&P 500 Index Fund	4,317.5	72.8%	9.3%
PSERS S&P 600 Index Fund	<u>413.1</u>	<u>7.0%</u>	<u>0.9%</u>
Total Passively Managed U.S. Equity	<u>\$ 5,171.6</u>	87.2%	11.1%
<u>Actively Managed Large Cap Portfolios</u>			
Biondo Group	\$ 12.2	0.2%	0.0%
EDMP, Inc.	43.9	0.7%	0.1%
Hanseatic Management Services, Inc.	45.0	0.8%	0.1%
Hellman Jordan	27.7	0.5%	0.1%
Other (Includes PSERS Equity Rebalance)	<u>5.8</u>	<u>0.1%</u>	<u>0.0%</u>
Total Actively Managed Large Cap U.S. Equity	<u>\$ 134.6</u>	2.3%	0.3%
<u>Actively Managed Mid and Small Cap Portfolios</u>			
AH Lisanti Capital Growth, LLC	\$ 26.1	0.4%	0.1%
Conestoga Capital Advisors	47.6	0.8%	0.1%
Emerald Advisors, Inc.	46.5	0.8%	0.1%
First Pacific Advisors, Inc.	225.6	3.8%	0.5%
Opus Capital Management	<u>32.0</u>	<u>0.5%</u>	<u>0.1%</u>
Total Actively Managed Mid and Small Cap U.S. Equity	<u>\$ 377.7</u>	6.3%	0.8%
<u>Actively Managed MicroCap Portfolios</u>			
Ativo Capital Management	\$ 18.7	0.3%	0.0%
Donald Smith & Co., Inc.	39.7	0.7%	0.1%
NorthPointe Capital, LLC	46.8	0.8%	0.1%
Oberweis Asset Management, Inc.	49.0	0.8%	0.1%
Thomson Horstmann & Bryant, Inc.	41.4	0.7%	0.1%
Turner Investment Partners	<u>51.2</u>	<u>0.9%</u>	<u>0.1%</u>
Total Actively Managed MicroCap U.S. Equity	<u>\$ 246.8</u>	4.2%	0.5%
Total U.S. Equity	<u>\$ 5,930.8</u>	<u>100.0%</u>	<u>12.7%</u>

Numbers may not add due to rounding.

Summary of PSERS' Non-U.S. Equity Investments (as of December 31, 2009)

Non-U.S. Equities represent one of eight major asset classes that PSERS uses to diversify the investments of the Fund. PSERS' investment plan diversifies equity investments and balances equity management styles. PSERS contracts with external investment managers and hires internal portfolio managers to manage Non-U.S. portfolios.

Policy

Non-U.S. Equities are utilized by the Fund primarily because their expected large return premiums versus inflation will, if realized, help preserve and enhance the real value of the Fund over long periods of time. The Non-U.S. Equity asset class is to be managed on a total return basis.

Non-U.S. Equity investments shall consist almost entirely of publicly-traded securities listed on the exchanges in the countries approved by PSERS that provide PSERS with an equity interest in private sector concerns (i.e. common stock, preferred stock, convertible preferred stock, convertible bonds, etc.).

PSERS' Asset Allocation targets an eventual allocation of 17.75% of assets to Non-U.S. Equities. It assigns the investment of 79% of Non-U.S. Equities in generally large capitalization stocks of developed and emerging markets, 11% of Non-U.S. Equities in generally small capitalization stocks of developed and emerging markets, and 10% of Non-U.S. Equities in medium/small capitalization stocks in emerging markets.

Market Value as of December 31, 2009: \$8,790.0 million, or 18.8% of the Fund's total market value.

Number of External Investment Managers: PSERS had contracts with 21 external investment managers responsible for various Non-U.S. Equity portfolios (including 3 Public Market Emerging Investment Manager Program manager).

Number of Internal Portfolio Managers: PSERS had 1 employee managing a Non-U.S. Equity portfolio.

Types of Investment Portfolios at December 31, 2009:

- 79.6% large capitalization stock strategies, 11.6% small capitalization strategies, and 8.8% emerging market stock strategies
- 51.9% passively-managed portfolios (managed internally) and 48.1% actively-managed portfolios (managed externally)

Summary of PSERS' Non-U.S. Equity Portfolios (unaudited)

(as of December 31, 2009)

	Market Value (in millions)	% of Non-U.S. Equities	% of Total Fund
<u>Passively Managed Portfolio</u>			
PSERS ACWI x-US Index Fund	<u>\$ 4,564.1</u>	51.9%	9.8%
<u>Actively Managed Developed Large Cap Portfolios</u>			
Baillie Gifford Overseas Ltd.	508.5	5.8%	1.1%
BlackRock Financial Management, Inc.	533.7	6.1%	1.1%
John Hsu Capital Group, Inc.	68.0	0.8%	0.1%
Marathon Asset Management Limited	457.8	5.2%	1.0%
Martin Currie, Inc.	391.2	4.5%	0.8%
Mercator Asset Management	408.1	4.6%	0.9%
Shah Capital Management	62.2	0.7%	0.1%
Other	<u>2.4</u>	<u>0.0%</u>	<u>0.0%</u>
Total Actively Managed Developed Large Cap Non-U.S. Equity	<u>\$ 2,431.9</u>	27.7%	5.2%
<u>Actively Managed Emerging Market Portfolios</u>			
Batterymarch Financial Mgmt., Inc.	\$ 127.3	1.4%	0.3%
Boston Co. Asset Management	176.5	2.0%	0.4%
Templeton Investment Counsel, Inc.	178.8	2.0%	0.4%
Wellington Management Co., LLP	129.6	1.5%	0.3%
Westwood Global Investments	55.4	0.6%	0.1%
William Blair & Co.	<u>109.4</u>	<u>1.2%</u>	<u>0.2%</u>
Total Actively Managed Emerging Market Non-U.S. Equity	<u>\$ 776.9</u>	8.8%	1.7%
<u>Actively Managed Developed Small Cap Portfolios</u>			
Acadian Asset Management	\$ 127.5	1.5%	0.3%
AXA Rosenberg Investment Management	92.5	1.1%	0.2%
Batterymarch Financial Mgmt., Inc.	83.9	1.0%	0.2%
GlobeFlex Capital, L.P.	82.0	0.9%	0.2%
Munder Capital Management	85.6	1.0%	0.2%
Oberweis Asset Management, Inc.	67.4	0.8%	0.1%
Pyramis Global Advisors	100.0	1.1%	0.2%
Victory Capital Management	107.3	1.2%	0.2%
Wasatch Advisors, Inc.	119.1	1.4%	0.3%
Wasatch Advisors – Small Cap Emerging Markets	<u>151.8</u>	<u>1.7%</u>	<u>0.3%</u>
Total Actively Managed Developed Small Cap Non-U.S. Equity	<u>\$ 1,017.1</u>	11.6%	2.2%
Total Non-U.S. Equity	<u>\$ 8,790.0</u>	<u>100.0%</u>	<u>18.9%</u>

Numbers may not add due to rounding.

Summary of PSERS' Fixed Income Investments (as of December 31, 2009)

Fixed Income represents one of eight major asset classes that PSERS uses to diversify the investments of the Fund. PSERS' investment plan diversifies Fixed Income investments and balances Fixed Income management styles. PSERS contracts with external investment managers and hires internal portfolio managers to manage portfolios.

Policy

Fixed Income investments are utilized by the Fund primarily because of their ability to serve as a hedge against disinflation and/or deflation, their general ability to produce current income in the form of periodic interest payments, and because such investments help diversify the overall Fund. The Fixed Income class is to be managed on a total return basis.

PSERS' Asset Allocation targets an eventual allocation of 24.5% of assets to Fixed Income, 30.6% of which is designated to core/core plus strategies, 20.4% of which is designated to TIPS strategies, 36.7% is designated to high yield/opportunistic strategies, and 12.2% which is designated to global core/core plus strategies. Of the total Fixed Income allocation, 87.8% is assigned to U.S. fixed income portfolios and 12.2% is assigned to global fixed income portfolios. Fixed Income Investments are targeted to be 100% actively managed.

Market Value as of December 31, 2009: \$10,663.0 million, or 22.8% of the Fund's total market value.

Number of External Investment Managers: PSERS had contracts with 18 external investment managers responsible for various Fixed Income portfolios (including 3 Public Market Emerging Investment Manager Program managers).

Number of Internal Portfolio Managers: PSERS had 2 employees managing various Fixed Income portfolios.

Types of Investment Portfolios at December 31, 2009:

- 90.5% U.S. fixed income portfolios and 9.5% global fixed income portfolios
- 31.3% core/core plus strategy portfolios, 21.2% TIPS portfolios, 12.7% collectively in the high yield and absolute return portfolios, 25.7% credit opportunity strategy portfolios, and 9.5% global core/core plus strategy portfolios
- 23.4% was managed by internal portfolio managers and 76.6% is managed by external investment managers

Summary of PSERS' Fixed Income Portfolios (unaudited)
(as of December 31, 2009)

	Market Value (in millions)	% of Total Fixed Income	% of Total Fund
<u>Actively Managed U.S. Core/Core Plus Fixed Income Portfolios</u>			
Aberdeen Asset Management, Inc.	\$ 302.7	2.9%	0.6%
BlackRock Financial Management, Inc.	461.1	4.3%	1.0%
BlackRock U.S. Extended Core Global Alpha Fund	602.0	5.6%	1.3%
Pacific Investment Mgmt. Co. (PIMCO)	443.7	4.2%	1.0%
Piedmont Investment Advisors	18.4	0.2%	0.0%
PSERS Active Aggregate	1,151.7	10.9%	2.5%
Pugh Capital Management, Inc.	43.4	0.4%	0.1%
Western Asset Management Co.	289.8	2.7%	0.6%
Other	<u>3.8</u>	<u>0.0%</u>	<u>0.0%</u>
Total Actively Managed U.S. Core/Core Plus Fixed Income	<u>\$ 3,316.6</u>	31.2%	7.1%
<u>Actively Managed Treasury Inflation-Protected Securities (TIPS) Portfolios</u>			
Bridgewater Associates, Inc.	\$ 914.4	8.6%	2.0%
PSERS TIPS Portfolio	<u>1,330.6</u>	<u>12.5%</u>	<u>2.8%</u>
Total Actively Managed Treasury Inflation-Protected Securities (TIPS)	<u>\$ 2,245.0</u>	21.1%	4.8%
<u>Actively Managed High Yield Fixed Income Portfolio</u>			
MacKay-Shields Financial Corporation	<u>\$ 450.4</u>	4.2%	1.0%
<u>Actively Managed Absolute Return Portfolio</u>			
Brigade Capital Management	<u>\$ 899.2</u>	8.4%	1.9%
<u>Actively Managed Credit Opportunity Portfolios</u>			
BlackRock Mortgage (Offshore) Investors	\$ 467.1	4.4%	1.0%
Brookfield Asset Management, Inc.	397.6	3.7%	0.9%
LBC Credit Partners II, LP	61.7	0.6%	0.1%

Numbers may not add due to rounding.

Summary of PSERS' Fixed Income Portfolios (unaudited)
 (as of December 31, 2009)
 (continued)

	Market Value <u>(in millions)</u>	% of Total Fixed <u>Income</u>	% of Total <u>Fund</u>
<u>Actively Managed Credit Opportunity Portfolios (cont'd)</u>			
Oaktree Loan Fund	\$ 238.9	2.2%	0.5%
Sankaty Credit Opportunities Fund IV, LP	413.9	3.9%	0.9%
Sankaty Advisors LLC - Bank Loans	553.3	5.2%	1.2%
TCW Mortgage	315.0	3.0%	0.7%
Stillwater Capital Partners, Inc.	30.0	0.3%	0.1%
TCW Credit Opportunities Fund, LP	<u>261.8</u>	<u>2.5%</u>	<u>0.6%</u>
Total Actively Managed Credit Opportunity Fixed Income	<u>\$ 2,739.3</u>	25.7%	5.9%
Total Actively Managed U.S. Fixed Income	<u>\$ 9,650.6</u>	90.5%	20.7%
<u>Actively Managed Global Core Plus Fixed Income Portfolios</u>			
Aberdeen Asset Management, Inc.	\$ 219.4	2.1%	0.5%
Fischer, Francis, Trees & Watts, Inc.	231.7	2.2%	0.5%
Franklin Templeton	337.5	3.2%	0.7%
Rogge Global Partners	<u>223.8</u>	<u>2.1%</u>	<u>0.5%</u>
Total Actively Managed Global Core Plus Fixed Income	<u>\$ 1,012.4</u>	9.5%	2.2%
Total Fixed Income	<u>\$ 10,663.0</u>	<u>100.0%</u>	<u>22.8%</u>

Numbers may not add due to rounding.

Summary of PSERS' Commodity Investments (as of December 31, 2009)

Commodities represent one of eight major asset classes that PSERS uses to diversify the investments of the Fund. PSERS' investment plan diversifies Commodity Investments and balances Commodity management styles. PSERS contracts with external investment managers to manage commodity portfolios.

Policy

Commodity investments are utilized by the Fund for diversification within the portfolio and to act as a hedge against unanticipated inflation. The prices of commodities are determined primarily by near-term events in global supply and demand conditions and are positively related with both the level of inflation and the changes in the rate of inflation. However, stock and bond valuations are based on longer-term expectations and react negatively to inflation. Therefore, commodity returns have had a historically negative correlation to stock and bond returns. As such, commodities, when combined with stocks and bonds, lower the risk of a portfolio.

The Fund benchmarks its Commodity Investments to the Dow Jones-UBS Commodity Index (DJ UBS). The DJ UBS is a broadly diversified basket of 20 commodities from 4 sectors (energy, industrial metals, precious metals, and agriculture).

PSERS' Asset Allocation currently targets an allocation of 4.0% of assets to Commodity Investments, 40% of which is designated to full discretion active strategies and 60% of which is designated to core/enhanced strategies. Full discretion strategies permit the use of both commodity derivatives (futures and swaps) and commodity-related stocks to gain commodity exposure. Core/enhanced strategies use only commodity derivatives to gain commodity exposure. Commodity Investments are targeted to be 100.0% actively managed.

Market Value of December 31, 2009: \$1,771.3 million, or 3.8% of the Fund's total market value.

Number of External Investment Managers: PSERS had contracts with 5 external investment managers to manage Commodity portfolios.

Number of Internal Investment Managers: None.

Type of Investment Portfolios at December 31, 2009:

- 43.8% full discretion strategy portfolio and 56.2% core/enhanced strategy portfolio
- 100.0% was managed by external investment managers

Summary of PSERS' Commodity Portfolios (unaudited)
(as of December 31, 2009)

	Market Value (in millions)	% of Total Commodities	% of Total Fund
<u>Full Discretion Commodity Portfolios</u>			
Deutsche Asset Management	\$ 221.4	12.5%	0.5%
Wellington Management Company, LLP	<u>554.2</u>	<u>31.3%</u>	<u>1.2%</u>
Total Full Discretion Commodities	<u>\$ 775.6</u>	43.8%	1.7%
<u>Core/Enhanced Commodity Portfolios</u>			
Credit Suisse Asset Management	\$ 292.4	16.5%	0.6%
Neuberger Berman Group, LLC	354.8	20.0%	0.8%
Schroders Investment Management	<u>348.5</u>	<u>19.7%</u>	<u>0.7%</u>
Total Core/Enhanced Commodities	<u>\$ 995.7</u>	56.2%	2.1%
Total Commodities	<u>\$ 1,771.3</u>	<u>100.0%</u>	<u>3.8%</u>

Numbers may not add due to rounding.

Summary of PSERS' Absolute Return Investments

(as of December 31, 2009)

Absolute Return represents one of eight major asset classes that PSERS uses to diversify the investments of the Fund. PSERS contracts with external investment managers to manage absolute return portfolios.

Policy

Absolute Return investments are utilized by the Fund primarily to generate returns that are uncorrelated with other asset classes or investments and because such investments help diversify the overall Fund. The benchmark for PSERS' absolute return investments is an absolute return of 8.0% annualized with risk of 8% or lower at the program level over a full market cycle.

Absolute Return investments shall be in a variety of unique, non-directional investment strategies, including equity and fixed income long/short, global macro, currency, option, capital structure arbitrage, and other strategies. The Fund shall diversify this program by manager and style.

PSERS' Asset Allocation currently targets an allocation of 7.5% of assets in Absolute Return investments.

Market Value as of December 31, 2009: \$3,607.0 million, or 7.7% of the Fund's total market value.

Number of External Investment Managers: PSERS had contracts with 11 external investment managers responsible for the various Absolute Return portfolios (including 3 Public Market Emerging Manager Program managers).

Number of Internal Investment Managers: None.

Summary of PSERS' Absolute Return Portfolios (unaudited)
(as of December 31, 2009)

	Market Value (in millions)	% of Total Absolute Return	% of Total Fund
<u>Actively Managed Absolute Return Portfolios</u>			
AQR Capital Management	\$ 672.8	18.7%	1.4%
BlackRock Financial Management, Inc.	664.4	18.4%	1.4%
BlackRock Capital Structure Investments Fund	201.4	5.6%	0.4%
Boston Company Asset Management	180.6	5.0%	0.4%
Bridgewater Associates, Inc.	711.7	19.7%	1.5%
Denali Advisors, LLC	37.7	1.0%	0.1%
First Quadrant, L.P.	541.4	15.0%	1.2%
FX Concepts, Inc.	3.8	0.1%	0.0%
Harvest MLP II	53.3	1.5%	0.1%
Lazard Asset Management	109.8	3.0%	0.2%
Pacific Investment Mgmt. Co. (PIMCO)	381.1	10.6%	0.8%
Zacks Investment Management	<u>49.0</u>	<u>1.4%</u>	<u>0.1%</u>
Total Absolute Return	<u>\$ 3,607.0</u>	<u>100.0%</u>	<u>7.7%</u>

Numbers may not add due to rounding.

Summary of PSERS' Real Estate Investments (as of December 31, 2009)

Real Estate represents one of eight major asset classes that PSERS uses to diversify the investments of the Fund. The primary objective of the real estate program is to invest in real property directly or indirectly through global publicly-traded real estate securities (PTRES), direct investments, commingled fund investments, limited partnerships, and direct private placements. This is done in a prudent manner to create a diversified real estate portfolio of high quality investments which will enhance PSERS' overall long-term investment performance, diversify the asset base, and reduce the volatility of returns of the total investment portfolio.

Policy

The real estate program is designed to create the highest possible risk-adjusted returns in a controlled, coordinated, and comprehensive manner. Recognizing that real estate market conditions and PSERS' objectives for real estate may change over time, the program is reviewed periodically and updated as needed. The existing target allocation is 9.5% of total assets.

Investments are made through global PTRES, direct investments, commingled fund investments, limited partnerships, and direct private placements. It is PSERS' intent to liquidate any investment at the point in time when its value has been maximized. PSERS seeks to diversify its real estate portfolio by investing in a mix of Opportunistic (50%), Value Added (30%) and Core (20%) real estate investments.

Opportunistic real estate investing is the financing, acquisition or investment in real estate assets, real estate companies, portfolios of real estate assets, private and public REIT's that do not have access to traditional public equity or debt financing. Opportunistic real estate consists of investment strategies that seek to exploit market inefficiencies with an emphasis on total return. Opportunistic investments require specialized expertise and the flexibility to respond quickly to market imbalances or changing market conditions. Investments may include non-traditional property types and/or assets that involve development, re-development, or leasing risks.

Value Added real estate investing typically focuses on both income growth and appreciation potential, where opportunities created by dislocations and inefficiencies between and within segments of the real estate capital markets are capitalized upon to enhance returns. Investments can include high-yield equity and debt investments and undervalued or impaired properties in need of repositioning, re-development or leasing.

Core real estate investing is the financing, acquisition or investment in real estate assets, real estate companies, portfolios of real estate assets, private REITs that are broadly diversified by property type and location, focused primarily on completed, well-leased properties with modest levels of leasing risk, using relatively low leverage, and investing mainly in institutional property types and qualities allowing for relative ease of resale.

Summary of PSERS' Real Estate Investments
(as of December 31, 2009)
(continued)

Market Value as of December 31, 2009: \$4,484.8 million or 9.6% of the Fund's total market value. This market value represents the combination of December 31, 2009 and September 30, 2009 market values adjusted for cash flows that occurred during the fourth quarter of 2009.

Number of External Investment Managers: PSERS had contracts with 6 external public market real estate investment managers, 6 external directly managed real estate asset managers, and 78 external general partners to manage the real estate separate account, public securities, and pool fund portfolios.

Number of Internal Portfolio Managers: PSERS had 2 employees managing real estate portfolios.

Type of Investment Portfolios at December 31, 2009:

- 4.7% Separate Account Portfolios
- 15.6% Public Securities Portfolios
- 79.8% Pooled Fund Portfolios

Summary of PSERS' Real Estate Portfolios (unaudited)
(as of December 31, 2009)

<u>Separate Accounts</u>	Market Value (in millions)	% of Total Real Estate	% of Total Fund
Charter Oak Advisors, Inc.	\$ 88.8	2.0%	0.2%
GF Management, Inc.	60.7	1.4%	0.1%
Grandbridge Real Estate Capital, LLC	3.0	0.1%	0.0%
Grosvenor Investment Management U.S., Inc.	8.1	0.2%	0.0%
L&B Realty Advisors, LLP	26.9	0.6%	0.1%
Prudential Agricultural Group	<u>23.6</u>	<u>0.5%</u>	<u>0.1%</u>
Total Real Estate Separate Accounts	<u>\$ 211.0</u>	4.7%	0.5%

Public Securities

Actively Managed Publicly Traded Real Estate Securities
Portfolios

Cohen and Steers Capital Management, Inc.	\$ 55.4	1.2%	0.1%
European Investors Inc.	148.5	3.3%	0.3%
LaSalle Investment Management	42.5	0.9%	0.1%
Morgan Stanley Investment Mgmt., Inc.	204.1	4.6%	0.4%
Security Capital Research & Management, Inc. - Preferred Growth	182.1	4.1%	0.4%
Security Capital Research & Management, Inc.	<u>65.1</u>	<u>1.5%</u>	<u>0.1%</u>
Total Actively Managed Publicly Traded Real Estate Securities	<u>\$ 697.7</u>	15.6%	1.5%

Numbers may not add due to rounding.

Summary of PSERS' Real Estate Portfolios (unaudited)
(as of December 31, 2009)
(continued)

<u>Pooled Funds</u>	Market Value (in millions)	% of Total Real Estate	% of Total Fund
Apollo European Real Estate Fund III, L.P.	\$ 48.2	1.1%	0.1%
Apollo Real Estate Finance Corp.	103.1	2.3%	0.2%
AREFIN Co-Invest Corp.	9.9	0.2%	0.0%
AvalonBay Value Added Fund, L.P.	49.5	1.1%	0.1%
AvalonBay Value Added Fund II, L.P.	13.5	0.3%	0.0%
Avenue Real Estate Fund Parallel, L.P.	42.6	1.0%	0.1%
Beacon Capital Strategic Partners V, L.P.	40.4	0.9%	0.1%
Berwind Property Group, Fund IV & V, L.P.	18.6	0.4%	0.0%
Berwind Property Group, Fund VI, L.P.	33.0	0.7%	0.1%
Blackstone Real Estate Partners V. TE.1, L.P.	105.5	2.4%	0.2%
Blackstone Real Estate Partners VI. TE.1, L.P.	81.5	1.8%	0.2%
Blackstone Real Estate Partners Europe III, L.P.	8.4	0.2%	0.0%
BPG Co-Investment Partnership, L.P.	20.5	0.5%	0.0%
Broadway Partners Parallel Fund P III, L.P.	11.9	0.3%	0.0%
Cabot Industrial Value Fund III, L.P.	6.1	0.1%	0.0%
Carlyle Europe Real Estate Partners III-A, L.P.	65.0	1.4%	0.1%
Carlyle Realty III, L.P.	66.9	1.5%	0.1%
Carlyle Realty IV, L.P.	85.7	1.9%	0.2%
Carlyle Realty V, L.P.	185.7	4.1%	0.4%
Centerline High Yield CMBS Fund III, LLC	16.7	0.4%	0.0%
Centerline RE Special Situations Mortgage Fund, LLC	26.7	0.6%	0.1%
Cornerstone Patriot Fund, L.P.	63.3	1.4%	0.1%
CS Strategic Partners IV Real Estate, L.P.	38.4	0.9%	0.1%
CSFB Strategic Partners II RE, L.P.	16.8	0.4%	0.0%
CSFB Strategic Partners III RE, L.P.	33.9	0.8%	0.1%
DLJ Real Estate Capital Partners II, L.P.	26.2	0.6%	0.1%
DLJ Real Estate Capital Partners III, L.P.	96.4	2.2%	0.2%
DLJ Real Estate Capital Partners IV, L.P.	61.2	1.4%	0.1%
DRA Growth and Income Fund VI, L.P.	70.8	1.6%	0.2%
Fillmore West Fund, L.P.	19.9	0.4%	0.0%
Five Arrows Realty Securities V, L.P.	14.1	0.3%	0.0%
Fortress Investment Fund IV, L.P.	68.3	1.5%	0.1%
Fortress Investment Fund V (Fund A) , L.P.	69.3	1.5%	0.1%
Fortress PSERS Investment, L.P.	41.4	0.9%	0.1%
Hines U.S. Office Value Added Fund, L.P.	48.2	1.1%	0.1%
JPMCB Strategic Property Fund	16.9	0.4%	0.0%

Summary of PSERS' Real Estate Portfolios (unaudited)
(as of December 31, 2009)
(continued)

<u>Pooled Funds (cont'd)</u>	Market Value (in millions)	% of Total Real Estate	% of Total Fund
Legg Mason Real Estate Capital, Inc.	\$ 10.4	0.2%	0.0%
Legg Mason Real Estate Capital II, Inc.	93.5	2.1%	0.2%
Lehman Brothers PSERS Real Estate, L.P.	54.4	1.2%	0.1%
Lehman Brothers Real Estate Pension Partners II, L.P.	91.3	2.0%	0.2%
Lehman Brothers Real Estate Pension Partners III, L.P.	64.2	1.4%	0.1%
LEM Real Estate Mezzanine Fund II, L.P.	37.3	0.8%	0.1%
LF Strategic Realty Investors I, L.P.	2.5	0.1%	0.0%
LF Strategic Realty Investors II, L.P.	82.4	1.8%	0.2%
Lubert-Adler Real Estate Fund II, L.P.	3.1	0.1%	0.0%
Lubert-Adler Real Estate Fund III, L.P.	12.3	0.3%	0.0%
Lubert-Adler Real Estate Fund IV, L.P.	38.6	0.9%	0.1%
Lubert-Adler Real Estate Fund V, L.P.	61.7	1.4%	0.1%
Lubert-Adler Real Estate Fund VI, L.P.	57.3	1.3%	0.1%
Madison Marquette Retail Enhancement Fund, L.P.	29.1	0.6%	0.1%
MGPA Asia Fund III, L.P.	24.0	0.5%	0.1%
MGPA Europe Fund III, L.P.	30.3	0.7%	0.1%
Morgan Stanley Real Estate Fund II L.P.	15.1	0.3%	0.0%
Morgan Stanley Real Estate Fund IV Sp. Dom. L.P.	16.6	0.4%	0.0%
Morgan Stanley Real Estate Fund IV Sp. Int'l L.P.	16.3	0.4%	0.0%
Morgan Stanley Real Estate Fund V Sp. Int'l L.P.	81.9	1.8%	0.2%
Morgan Stanley Real Estate Fund V Sp. U.S. L.P.	11.4	0.3%	0.0%
Morgan Stanley Real Estate Fund VI Sp. Int'l L.P.	63.2	1.4%	0.1%
Morgan Stanley Real Estate Fund VII Global L.P.	6.0	0.1%	0.0%
O'Connor North American Property Partners, L.P.	40.6	0.9%	0.1%
O'Connor North American Property Partners II, L.P.	27.6	0.6%	0.1%
Paladin Realty Latin America III, L.P.	39.9	0.9%	0.1%
Peabody Global Real Estate Partners, L.P.	10.1	0.2%	0.0%
Prime Property Fund, LLC	34.2	0.8%	0.1%
PRISA	61.9	1.4%	0.1%
ProLogis North American Industrial Fund, L.P.	137.0	3.1%	0.3%
RCG Longview Debt Fund IV, L.P.	48.8	1.1%	0.1%
RCG Longview Equity Fund PA PSERS, L.P.	72.4	1.6%	0.2%
RREEF America REIT II, Inc.	7.0	0.2%	0.0%

Summary of PSERS' Real Estate Portfolios (unaudited)
(as of December 31, 2009)
(continued)

<u>Pooled Funds (cont'd)</u>	Market Value <u>(in millions)</u>	% of Total <u>Real Estate</u>	% of Total <u>Fund</u>
Stockbridge Real Estate Fund I, L.P.	\$ 192.8	4.3%	0.4%
Stockbridge Real Estate Fund II-A, L.P.	74.5	1.7%	0.2%
Stockbridge Real Estate Fund III, L.P.	38.7	0.9%	0.1%
Strategic Partners Value Enhancement Fund, L.P.	56.5	1.3%	0.1%
UBS Trumbull Property Fund, L.P.	58.8	1.3%	0.1%
Westbrook Real Estate Fund, L.P.	1.0	0.0%	0.0%
Whitehall Street Real Estate V & VI, L.P.	0.3	0.0%	0.0%
Whitehall Street Real Estate VII & VIII, L.P.	2.2	0.0%	0.0%
William E. Simon & Sons Realty Partners, L.P.	<u>44.7</u>	<u>1.0%</u>	<u>0.1%</u>
Total Real Estate Pooled Fund	<u>\$ 3,576.1</u>	79.8%	7.7%
Total Real Estate	<u>\$ 4,484.8</u>	<u>100.0%</u>	<u>9.6%</u>

Numbers may not add due to rounding.

Summary of PSERS' Private Market Investments (as of December 31, 2009)

Private Market Investments represent one of eight major asset classes that PSERS uses to diversify the investments of the Fund. The Private Market Investments program is a portion of PSERS asset allocation used to diversify the Fund. The primary vehicle used to invest funds in this asset class is the limited partnership. Individual management groups selected by PSERS form these partnerships for the purpose of investing in and managing private equity and unlisted-subordinated debt positions on behalf of PSERS and other limited partners. PSERS' Asset Allocation currently targets an allocation of 18.5% to Private Market Investments. Private Market Investment sub-asset class explanations are as follows:

Private Equity involves investments in private companies which normally do not have technology risk associated with traditional venture capital investments. It has evolved to include the financing of more mature, profitable companies that do not have access to, or qualify for, public equity and debt funding. Private Equity strategies include:

- *Buyouts* - Investment strategy is to acquire the assets of a publicly or privately held company. A subset of this category is the leveraged buyout, where financing enables companies to be acquired through the use of borrowed funds. Typically, the assets of target companies serve as collateral for loans originated in the transaction.
- *Secondary Partnerships* - An investment strategy to acquire interests in established limited partnerships. Secondary investing can often be lucrative due to the fact that the partnerships are purchased at significant discounts to net asset value and the timing of the purchase frequently occurs as the acquired partnerships begin to realize profits.

Venture Capital is considered the financing of young, relatively small, rapidly growing companies. In traditional venture capital investments, companies have a 5-10 year investment horizon and develop technology for a particular market, such as pharmaceuticals, software, medical products, etc. Venture capital strategies are typically classified as follows:

- *Seed* - An investment strategy that involves companies that are still in the conceptual stage of growth. Seed stage investing involves product viability risk.
- *Early Stage* - An investment strategy involving financing portfolio companies for product development and initial marketing, manufacturing and sales activities. Typically, early stage companies have been formed, but revenues have not been realized. Early stage investment involves risks associated with defining competitive markets, developing production and marketing channels.
- *Later Stage* - An investment strategy involving financing portfolio companies for rapid expansion. Risk at this stage revolves around capturing market share while increasing production and delivery capabilities and building sales volume.
- *Balanced* - An investment strategy including a variety of portfolio company development stages (Seed, Early, Later, etc.).

Summary of PSERS' Private Market Investments
 (as of December 31, 2009)
 (continued)

Private Debt involves investments in the secured and/or unsecured debt obligations of private and/or public companies. This debt is typically acquired through directly negotiated or competitively bid transactions. Owners of these debt instruments typically take either an active or passive role in the management of the firm. Private Debt strategies are typically classified as follows:

- *Mezzanine* - Investments in unsecured or junior debt securities with equity enhancements such as warrants or nominally priced equity.
- *Distressed Debt* - Investments in the debt obligations of under-performing companies that are in need of operating or financial restructuring, and are either in or out of bankruptcy.
- *Structured Products* - Investments in the debt tranche of a security that is generally leveraged and backed by a diversified pool of assets. Assets include bank debt, investment grade debt, non-investment grade debt, or mortgages.

Policy

For the Private Market Investments program, PSERS long-term investment objective is to achieve a risk-adjusted total return, net of fees, that exceeds market returns for similar investments, or benchmark returns furnished by Venture Economics on a vintage year weighted basis.

Market Value as of December 31, 2009: \$8,553.6 million, or 18.3% of the Fund's total market value. Sub-asset class market values (unaudited) and fund percentages were as follows:

	<i>Total Commitments (in millions)</i>		<i>Market Value (in millions)</i>		<i>Percent Allocation to Total Fund</i>
Private Equity	\$ 15,829.5		\$ 5,618.4		12.0%
Venture Capital	2,208.9		\$ 732.8		1.6%
Private Debt	4,016.8		\$ 2,202.4		4.7%
Total	\$ 22,055.2		\$ 8,553.6		18.3%

Summary of PSERS' Private Market Investments
(as of December 31, 2009)
(continued)

An objective of PSERS' Private Market Investments program is to maintain investment diversification by industry, geographic location, and investment strategy. Diversification levels as of December 31, 2009 are as follows:

Industry diversification (by number of companies in each industry):

Secondary Funds	29.6%	Computer	9.8%	Transportation	3.0%
Services	12.7%	Medical	8.2%	Energy	1.7%
Industrial	11.1%	Communication	6.4%	Real estate	1.6%
Financial	10.4%	Consumer	4.8%	Other	0.7%

Geographical diversity (by percentage of companies located in each state):

International	25.7%	Texas	3.9%	Maryland	1.8%
New York	18.5%	New Jersey	2.9%	Ohio	1.4%
California	15.7%	Illinois	2.5%	Michigan	1.2%
Massachusetts	4.8%	Connecticut	2.0%	Colorado	1.1%
Pennsylvania	4.4%	Florida	1.8%	Other	12.3%

PSERS' **Private Equity** program has committed a total of \$15,829.5 million to 104 partnerships through December 31, 2009. 5 of these partnerships are located in Pennsylvania. 24 of the 29 international investment partnerships are included within the private equity sector. The international investments serve to increase the diversification of this asset class while providing the opportunity of increasing total returns.

PSERS' **Venture Capital** program consists of 50 partnerships with committed capital totaling \$2,208.9 million through December 31, 2009. A significant number of the venture capital partnerships, 31 out of 50, are located in Pennsylvania. 1 of the 29 international partnerships is included within the venture capital sector.

PSERS' **Private Debt** program has committed \$4,016.8 million to 25 partnerships through December 31, 2009. The Private Debt program was initiated in 2000 by re-allocating \$1.0 billion from the Fixed Income allocation to take advantage of the attractive market conditions within the mezzanine and distressed debt sectors. 2 partnerships are located in Pennsylvania, and 4 of the 29 international partnerships are included within the private debt sector.

Summary of PSERS' Active Private Market Investments Committed, Drawn, and Distributed (unaudited) (as of December 31, 2009)

Partnership Name	Vintage	Capital	Capital	Capital
Private Equity:	<u>Year</u>	<u>Committed</u>	<u>Drawn</u>	<u>Distributions*</u>
ABS Capital Partners II	1996	\$ 40,000,000	\$ 39,291,734	\$ 45,555,770
Actis Emerging Markets 3, L.P.	2007	200,000,000	54,893,239	850,182
Allegheny New Mountain Partners, L.P.	2004	100,000,000	81,860,150	13,621,900
Apax Europe VII, L.P.	2007	286,620,000	135,252,540	(119,052)
BG Media Investors, L.P.	1997	25,000,000	24,629,069	21,018,842
Baring Asia Private Equity Fund III, L.P.	2005	122,500,000	124,815,392	163,626,344
Baring Asia Private Equity Fund IV, L.P.	2007	300,000,000	198,482,240	111,224
Bastion Capital Fund	1994	12,500,000	12,246,895	24,148,319
Blue Point Capital Partners (B), L.P.	2001	103,750,000	81,998,175	100,814,308
Blue Point Capital Partners II (B), L.P.	2007	100,000,000	51,720,162	(834,453)
Bridgepoint Capital II (Secondary)	1998	84,714,906	81,290,641	162,520,963
Bridgepoint Europe I	1998	79,622,624	75,126,567	132,241,583
Bridgepoint Europe II	2001	429,930,000	317,885,713	509,838,341
Bridgepoint Europe III A, L.P.	2005	286,620,000	239,489,196	-
Bridgepoint Europe IV, L.P.	2008	429,930,000	33,363,079	-
Bruckmann, Rosser, Sherrill & Co. L.P.	1995	25,000,000	24,395,229	43,478,206
CIGNA	1988	4,566,946	4,566,946	6,645,349
CS Strategic Partners IV, L.P.	2008	100,000,000	45,619,600	2,204,382
CSFB Strategic Partners II, L.P.	2003	300,000,000	253,703,169	345,621,471
CSFB Strategic Partners III-B, L.P.	2005	200,000,000	212,144,594	59,106,932
CVC Capital Partners Asia Pacific III, L.P.	2008	300,000,000	78,455,636	689,134
CVC European Equity Partners V (A), L.P.	2008	429,930,000	85,594,099	1,010,710
Capital International P. E. Fund V L.P.	2007	200,000,000	124,332,831	1,402,961
Catterton Growth Partners, L.P.	2008	75,000,000	35,944,198	1,624,318
Catterton Partners V, L.P.	2004	100,000,000	99,486,751	45,830,109
Catterton Partners VI, L.P.	2006	130,000,000	90,272,503	3,880,755
Cinven Fund (Fourth), L.P.	2006	214,965,000	128,133,873	-
Clarity PSERS II, L.P.	2008	23,250,000	9,698,963	562,500
Clarity Partners L.P.	2000	203,590,000	202,836,723	113,127,294
Credit Suisse Equity Partners, L.P.	1998	137,172,500	112,858,565	22,089,623
Credit Suisse Int'l Equity Partners, L.P.	1997	83,000,000	75,537,254	93,920,749
Crestview Partners II (PF) LP	2008	200,000,000	27,499,754	-
Crestview Partners, L.P.	2005	150,000,000	144,752,846	12,037,074
DLJ Merchant Banking Partners III, L.P.	2000	300,000,000	301,849,680	388,717,417
DLJ Strategic Partners	2001	200,000,000	187,139,614	257,784,144
Deutsche European Partners IV	1999	200,000,000	182,925,445	224,969,264
Dubin Clark Fund II, L.P.	2000	24,083,333	23,435,569	15,061,337
Edgewater Growth Capital Partners, L.P.	2001	59,196,500	58,604,535	34,047,637
Edgewater Private Equity Fund III, L.P.	1998	39,000,000	39,000,000	13,627,787
Evergreen Pacific Partners II, L.P.	2008	80,954,545	6,575,599	-
Evergreen Pacific Partners, L.P.	2004	50,000,000	30,457,261	3,483
First Reserve Fund XI, L.P.	2006	200,000,000	166,914,414	3,142,877
First Reserve Fund XII, L.P.	2008	250,000,000	92,528,752	(482,276)
Furman Selz Investors II L.P.	1998	56,250,000	51,479,146	84,984,647
Furman Selz Investors III L.P.	2000	100,000,000	85,443,338	177,911,190
GS Mezzanine Partners	1996	30,000,000	26,883,828	39,260,072

*Includes capital contributions for management fees, late interest, etc. that are not applied to the capital commitment.

**Summary of PSERS' Active Private Market Investments Committed,
Drawn, and Distributed (unaudited)**

(as of December 31, 2009)

(continued)

Partnership Name	Vintage	Capital	Capital	
Private Equity (cont'd):	Year	Committed	Drawn	Distributions*
Graham Partners	1999	\$ 56,671,214	\$ 48,472,084	\$ 40,612,055
Green Equity Investors II	1994	25,000,000	24,151,005	50,646,227
Greenpark International Investors III L.P.	2007	143,310,000	112,908,687	12,460,016
Greenwich Street Capital Partners II	1998	200,000,000	192,779,634	181,328,085
HSBC Private Equity Fund 6, L.P.	2008	200,000,000	48,742,846	2,447,258
Halifax Capital Partners	1999	50,000,000	39,520,692	53,011,023
Heritage Fund I	1994	25,000,000	24,999,999	23,298,166
Irving Place Capital Partners II L.P.	2000	300,000,000	282,044,425	237,185,264
Irving Place Capital Partners III L.P.	2006	150,000,000	72,179,061	856,988
Jefferies Capital Partners IV, L.P.	2005	100,000,000	64,607,098	(7,053,779)
KKR 2006 Fund L.P.	2006	300,000,000	224,101,197	3,901,399
KRG Capital Fund I	1999	50,000,000	43,261,578	91,634,458
KRG Capital Fund II	2001	100,000,000	79,539,180	115,172,562
KRG Capital Fund III, L.P.	2005	88,000,000	72,924,115	3,509,805
KRG Capital Fund IV L.P.	2007	300,000,000	53,654,303	565,654
Landmark Equity Partners III, L.P.	1993	27,085,010	27,085,010	75,045,740
Landmark Equity Partners IV, L.P.	1994	10,533,687	10,242,502	15,226,383
Landmark Equity Partners XIII, L.P.	2006	100,000,000	85,382,019	23,655,667
Landmark Equity Partners XIV, L.P.	2008	150,000,000	16,500,000	82,949
Landmark Mezzanine Partners	1995	75,000,000	59,315,512	106,599,975
Lehman Brothers Merchant Banking Part. II,LP	1997	158,552,133	158,552,133	200,483,752
Lexington Capital Partners I, L.P.	1996	50,000,000	49,613,120	62,102,505
Lindsay Goldberg & Bessemer L.P.	2002	300,000,000	307,640,096	434,160,016
Milestone Partners II, L.P.	2004	29,890,000	25,045,754	17,584,669
Milestone Partners III, L.P.	2008	60,000,000	28,911,800	-
Morgan Stanley Dean Witter Cap Part IV, L.P.	1998	300,000,000	227,851,338	434,385,493
Navis Asia Fund V, L.P.	2007	100,000,000	74,000,000	33,481
New Mountain Partners III L.P.	2007	300,000,000	86,550,079	14,990,090
New Mountain Partners. L.P.	2000	192,509,033	157,270,490	178,220,496
New York Life Capital Partners I, L.P.	1999	200,000,000	203,867,159	157,641,419
New York Life Capital Partners II, L.P.	2001	200,000,000	188,891,071	383,002,845
New York Life Capital Partners III-A, L.P.	2005	200,000,000	195,361,404	28,629,133
New York Life Capital Partners IV-A. L.P.	2008	100,000,000	43,182,786	13,925
Nordic Capital VII Beta L.P.	2008	214,965,000	58,116,888	(894,160)
PAI Europe III, L.P.	2001	429,930,000	328,966,935	800,590,942
PAI Europe IV-B2, L.P.	2005	143,310,000	114,613,621	26,906,406
PAI Europe V, L.P.	2007	143,310,000	48,199,003	(12,048)
PNC Equity Partners II, L.P.	2006	68,065,386	29,370,887	662,889
PNC Equity Partners, L.P.	2001	43,154,458	39,106,490	54,954,719
Palladium Equity Partners II-A, L.P.	2000	57,750,000	58,440,021	27,524,365
Partners Group Secondary 2008, L.P.	2007	214,965,000	55,254,792	303,396
Permira IV, L.P.	2006	179,137,500	114,719,610	-
Platinum Equity Capital Partners - A, L.P.	2004	125,000,000	98,722,596	184,368,505
Platinum Equity Capital Partners-A II, L.P.	2007	300,000,000	131,342,127	15,233,413

*Includes capital contributions for management fees, late interest, etc. that are not applied to the capital commitment.

**Summary of PSERS' Active Private Market Investments Committed,
Drawn, and Distributed (unaudited)**
(as of December 31, 2009)
(continued)

Partnership Name	Vintage	Capital	Capital	
Private Equity (cont'd):	<u>Year</u>	<u>Committed</u>	<u>Drawn</u>	<u>Distributions*</u>
Providence Equity Partners VI, L.P.	2006	\$ 300,000,000	\$ 161,665,713	\$ 9,353,704
Quadrangle Capital Partners II, L.P.	2005	250,000,000	200,901,481	45,588,156
Quadrangle Capital Partners, L.P.	2001	270,422,415	222,278,291	239,908,238
Sterling Capital Partners, L.P.	2002	75,000,000	84,229,630	82,413,136
Sunrise Capital Partners, L.P.	1998	57,388,755	56,607,546	16,736,372
TPG Partners II, L.P.	1997	50,000,000	53,854,393	90,586,297
TPG Partners V, L.P.	2006	250,000,000	221,215,697	41,674,765
TPG Partners VI, L.P.	2008	360,000,000	54,204,783	(2,725)
TPG Partners, L.P.	1993	24,194,356	24,375,251	89,210,590
Trilantic Capital Partners IV L.P.	2007	76,752,676	27,942,972	90,738
U.S. Equity Partners II	2001	300,000,000	213,669,862	167,429,008
U.S. Equity Partners, L.P.	1996	75,000,000	73,783,980	67,186,601
Wicks Communications and Media Part., L.P.	1999	87,500,000	87,943,776	104,929,461
Willis Stein & Partners, L.P.	1996	<u>25,000,000</u>	<u>25,000,000</u>	<u>53,573,595</u>
Private Equity Total		\$ 15,829,542,977	\$ 10,475,090,027	\$ 8,225,403,498
 Venture Capital :				
APA/Fostin Venture Fund I	1987	20,000,000	20,000,000	77,132,193
Adams Capital Management, L.P.	1997	12,500,000	12,500,000	22,671,838
Aisling Capital II L.P.	2006	50,000,000	37,738,547	1,087,960
Aisling Capital III, L.P.	2008	50,000,000	3,083,753	-
CEO Venture Fund I	1987	1,000,000	1,000,000	1,101,749
CEO Venture Fund II	1989	15,000,000	15,000,000	10,651,730
CS Strategic Partners IV VC, L.P.	2008	50,000,000	26,496,093	(396,537)
CSFB Strategic Partners III-VC, L.P.	2005	50,000,000	47,651,976	16,973,297
Co-Investment 2000 Fund, L.P.	2000	135,000,000	135,000,000	135,211,006
Co-Investment Fund II, L.P.	2006	135,000,000	70,875,000	-
Commonwealth Venture Partners I	1986	20,000,000	20,000,000	20,584,156
Commonwealth Venture Partners II	1992	10,000,000	10,000,000	15,214,766
Cross Atlantic Technology Fund II	2001	21,119,734	21,119,734	10,555,316
Cross Atlantic Technology Fund, L.P.	1999	30,141,666	30,141,667	28,345,782
Edison II-PA Venture Fund	1991	10,000,000	10,000,000	25,972,603
Edison Venture Fund III	1994	14,807,690	14,807,690	28,683,019
Franklin Capital Partners III	1995	15,000,000	15,000,000	9,626,580
Genesis Seed Fund	1987	2,000,000	2,000,000	815,687
Grotech Partners IV	1993	25,000,000	25,000,000	44,210,693
Jefferson Partners Fund IV (PA) L.P.	2003	27,898,843	23,487,929	(9)
KBL Healthcare Ventures	1999	13,593,334	13,593,333	6,563,009
Keystone Minority Capital Fund	1994	114,865	114,865	15,365
Keystone Venture Fund IV	1993	7,766,667	7,766,666	5,904,516
LLR Equity Partners II, L.P.	2004	75,000,000	71,250,000	16,345,332
LLR Equity Partners III, L.P.	2008	187,500,000	43,123,354	8,363,629
LLR Equity Partners, L.P.	1999	62,500,000	61,250,000	118,392,955
Landmark Equity Partners II, L.P.	1992	25,000,000	25,000,000	39,012,414
Landmark Equity Partners V, L.P.	1995	49,060,283	48,478,943	58,321,606

*Includes capital contributions for management fees, late interest, etc. that are not applied to the capital commitment.

Numbers may not add due to rounding.

**Summary of PSERS' Active Private Market Investments Committed,
Drawn, and Distributed (unaudited)
(as of December 31, 2009)
(continued)**

Partnership Name	Vintage	Capital	Capital	
Venture Capital (cont'd):	<u>Year</u>	<u>Committed</u>	<u>Drawn</u>	<u>Distributions*</u>
Lehman Bros. Communications Investors, L.P.	1999	\$ 12,500,000	\$ 11,442,260	\$ 5,164,360
Loyalhanna Venture Fund	1987	15,000,000	15,000,000	21,446,203
NEPA Venture Fund I	1985	1,000,000	1,000,000	6,080,528
NEPA Venture Fund II	1992	5,000,000	5,000,000	23,252,576
Novitas Capital , L.P.	1998	30,000,000	29,682,000	32,320,641
Novitas Capital II, L.P.	2000	75,000,000	74,100,000	7,464,424
P/A Fund	1993	30,000,000	30,000,000	66,195,394
Perseus-Soros BioPharmaceutical Fund	2001	112,206,666	98,691,823	136,042,226
Psilos Group Partners III, L.P.	2007	62,500,000	41,249,999	(5,475)
Quaker Bio-Ventures, L.P.	2003	69,350,000	66,576,000	13,712,630
Quaker BioVentures II, L.P.	2006	100,000,000	31,999,125	2,790,158
SCP Private Equity Partners I, L.P.	1996	62,500,000	62,500,000	39,486,003
SCP Private Equity Partners II, L.P.	2000	125,000,000	118,288,826	24,134,558
Spectrum Equity Investors, L.P.	1994	25,000,000	25,000,000	52,261,392
StarVest Partners , L.P.	1999	67,500,000	65,649,343	21,020,309
StarVest Partners II (Parallel), L.P.	2007	50,000,000	8,390,542	201,996
Sterling Venture Partners, L.P.	2000	33,986,000	35,554,923	26,242,116
TDH III, L.P.	1993	7,350,750	7,350,750	4,102,503
TL Ventures III, L.P.	1997	50,000,000	50,000,000	68,925,720
Technology Leaders, L.P.	1992	10,000,000	10,000,000	22,111,898
Tenaya Capital IV-P, L.P.	2003	75,000,000	70,733,693	14,796,205
Tenaya Capital V-P, L.P.	2007	75,000,000	28,508,745	-
Venture Capital Total		\$ 2,208,896,498	\$ 1,698,197,579	\$ 1,289,107,022
Private Debt:				
Avenue Asia Special Situations Fund II, L.P.	2001	220,000,000	220,000,000	370,823,700
Avenue Asia Special Situations Fund III, L.P.	2003	100,000,000	76,892,230	62,172,954
Avenue Asia Special Situations Fund IV, LP	2006	300,000,000	169,564,370	24,788,633
Avenue Europe Special Situations Fund, L.P.	2008	286,620,000	260,544,328	846,284
Avenue Special Situations Fund II, L.P.	2000	125,000,000	125,000,000	197,586,521
Avenue Special Situations Fund III, L.P.	2002	205,156,000	151,715,376	256,207,312
Avenue Special Situations Fund IV, L.P.	2005	115,000,000	144,782,669	49,090,478
Avenue Special Situations Fund V, L.P.	2007	300,000,000	300,000,000	(1,095,120)
Cerberus Institutional Partners, L.P. (Series 2)	2001	200,000,000	172,004,532	399,041,124
Cerberus Institutional Partners, L.P. (Series 3)	2003	100,000,000	81,000,000	57,120,746
Cerberus Institutional Partners, L.P. (Series 4)	2006	400,000,000	330,000,000	(284,722)
GSC Partners CDO Investors III, L.P.	2001	80,000,000	80,000,000	146,903,688
GSC Partners CDO Investors IV, L.P.	2003	80,000,000	80,000,000	70,302,000
GSC Recovery II, L.P.	2000	280,000,000	279,170,771	343,760,526

**Includes capital contributions for management fees, late interest, etc. that are not applied to the capital commitment.*

Numbers may not add due to rounding.

**Summary of PSERS' Active Private Market Investments Committed,
Drawn, and Distributed (unaudited)
(as of December 31, 2009)
(continued)**

Partnership Name	Vintage	Capital	Capital	
Private Debt (cont'd):	<u>Year</u>	<u>Committed</u>	<u>Drawn</u>	<u>Distributions*</u>
GSC Recovery III (Parallel Fund), L.P.	2005	\$ 200,000,000	\$ 189,826,824	\$ 33,613,294
Gleacher Mezzanine Fund II, L.P.	2006	100,000,000	25,569,434	2,026,967
Gleacher Mezzanine Fund, L.P.	2001	75,000,000	63,393,058	90,488,528
Gold Hill Venture Lending 03-A, L.P.	2004	50,000,000	50,000,000	19,581,782
NYLIM Mezzanine Part. (Parallel Fund) L.P.	2003	75,000,000	65,964,938	62,515,400
NYLIM Mezzanine Part. II (Parallel Fund) LP	2006	150,000,000	130,084,051	29,931,660
OCM Opportunities Fund VII L.P.	2007	75,000,000	75,000,000	-
OCM Opportunities Fund VII-b L.P.	2008	225,000,000	191,250,000	-
Versa Capital Fund I, L.P.	2005	75,000,000	74,250,000	34,635,082
Versa Capital Fund II, L.P.	2008	150,000,000	24,000,000	619,899
Windjammer Senior Equity Fund III, L.P.	2006	50,000,000	25,703,726	1,043,748
Private Debt Total		\$ 4,016,776,000	\$ 3,385,716,307	\$ 2,251,720,485
Grand Total		<u>\$ 22,055,215,475</u>	<u>\$ 15,559,003,913</u>	<u>\$ 11,766,231,004</u>

**Includes capital contributions for management fees, late interest, etc. that are not applied to the capital commitment.*

Numbers may not add due to rounding.

Summary of PSERS' Cash Investments **(unaudited, as of December 31, 2009)**

Cash represents one of eight major asset classes that PSERS uses to diversify the investments of the Fund. PSERS assigned one internal investment manager to management of the cash portfolio.

Policy

Cash investments are utilized by the Fund primarily to provide sufficient liquidity to meet its obligation to pay member benefits and capital commitments to private market and real estate investments. Cash investments are targeted to be 100% actively managed.

PSERS' Asset Allocation currently targets an allocation of 5.0% of assets to Cash investments.

Market Value as of December 31, 2009: \$2,891.7 million, or 6.2% of the Fund's total market value.

Number of External Investment Managers: None.

Number of Internal Investment Managers: PSERS had one employee managing a cash portfolio.

Investment Advisory Fees

Summary of Investment Advisory Fees
Fiscal Year Ended June 30, 2009
(Dollar Amounts in Thousands)

	<u>Fees</u>	<u>Basis Points</u>
External Management		
U.S. Equity	\$ 7,272	45
Non-U.S. Equity	38,786	33
Fixed Income	57,424	64
Commodities	12,576	68
Absolute Return	64,416	157
Real Estate	98,735	98
Alternative Investments	<u>185,432</u>	109
Total External Management	<u>464,641</u>	84
Total Internal Management	<u>8,998</u>	7
Total Investment Management	<u>\$ 473,639</u>	70
Custodian Fees	569	
Investment Consultant Fees	<u>3,357</u>	
Total Investment Expenses	<u>\$ 477,565</u>	70

Investment Advisory Fees
Fiscal Years Ended June 30, 2004 - 2008
(Dollar Amounts in Thousands)

<u>Fiscal Year</u>	<u>Fees</u>	<u>Basis Points</u>
2004	191,300	37
2005	192,677	36
2006	211,279	35
2007	313,758	41
2008	399,136	47

Investment Managers' Fees
Fiscal Year Ended June 30, 2009
(Dollar Amounts in Thousands)

External Management fees are treated as a reduction of the investment revenue of the Fund rather than as a budgeted administrative expense.

<u>Manager</u>	<u>Location</u>		<u>Amount</u>
U.S. Equity			
AH Lisanti Capital Growth, LLC	New York	NY	\$ 71
Ativo Capital Management, L.L.C.	Chicago	IL	80
Barclays Global Investors, N.A.	San Francisco	CA	240
Biondo Group, L.L.C. (The)	Milford	PA	52
Boston Company Asset Management, L.L.C.	Boston	MA	607
Conestoga Capital Advisors, Inc.	Radnor	PA	173
Connors Investor Services, Inc.	Wyomissing	PA	38
Denali Advisors, L.L.C.	San Diego	CA	55
Donald Smith & Co., Inc.	New York	NY	317
Emerald Advisors, Inc.	Lancaster	PA	326
First Pacific Advisors, Inc.	Los Angeles	CA	1,374
Great Companies, Inc.	Tampa	FL	124
Hanseatic Management Services, Inc.	Albuquerque	NM	144
Mellon Capital Management Corporation	San Francisco	CA	954
NorthPointe Capital, L.L.C.	Troy	MI	834
Oberweis Asset Management, Inc.	North Aurora	IL	457
Opus Capital Management, Inc.	Cincinnati	OH	126
Pacific Investment Management Company (PIMCO)	Newport Beach	CA	(704) *
Thomson Horstmann & Bryant, Inc.	Saddle Brook	NJ	485
Turner Investment Partners, Inc.	Berwyn	PA	561
Wellington Management Company, L.L.P.	Boston	MA	555
William Blair & Company, L.L.C.	Chicago	IL	<u>403</u>
Total-U.S. Equity			7,272
Non-U.S. Equity			
Acadian Asset Management	Boston	MA	777
Alliance Bernstein Institutional Investment Mgmt.	New York	NY	2,026
AXA Rosenberg Investment Management	Orinda	CA	1,239
Baillie Gifford Overseas Ltd.	Edinburgh	UK	2,186
Barclays Global Investors, N.A.	San Francisco	CA	3,808
Batterymarch Financial Management, Inc.	Boston	MA	2,282
Boston Company Asset Management, L.L.C.	Boston	MA	2,593
GlobeFlex Capital, L.P.	San Diego	CA	911
John Hsu Capital Group, Inc.	New York	NY	194
Marathon Asset Management Limited	London	UK	2,418

*Represents reversal of amount accrued in prior fiscal year.

Investment Managers' Fees
Fiscal Year Ended June 30, 2009
(Dollar Amounts in Thousands)
(continued)

<u>Manager</u>	<u>Location</u>		<u>Amount</u>
Non-U.S. Equity (continued)			
Martin Currie, Inc.	Edinburgh	UK	\$ 1,555
Mercator Asset Management, L.P.	Ft. Lauderdale	FL	2,668
Oberweis Asset Management, Inc.	North Aurora	IL	593
Pareto Investment Management, Ltd.	New York	NY	2,873
Pyramis Global Advisors	Boston	MA	478
Shah Capital Management, Inc.	Raleigh	NC	3,097
Templeton Investment Counsel, Inc.	Nassau	Bahamas	2,639
Victory Capital Management, Inc.	New York	NY	909
Wasatch Advisors, Inc.	Salt Lake City	UT	3,010
Wellington Management Company, L.L.P.	Boston	MA	1,602
William Blair & Company, L.L.C.	Chicago	IL	928
Total-Non-U.S. Equity			38,786
Fixed Income			
Aberdeen Asset Management, Inc.	Philadelphia	PA	1,164
Barclays Global Investors, N.A.	San Francisco	CA	3,609
BlackRock Financial Management, Inc.	New York	NY	829
BlackRock Mortgage (Offshore) Investors, L.P.	New York	NY	4,947
Bridgewater Associates, Inc.	Westport	CT	8,100
Brigade Capital Management, L.L.C.	New York	NY	15,475
Fischer Francis Trees & Watts, Inc.	New York	NY	754
Franklin Templeton Investments	Nassau	Bahamas	1,542
Hyperion Brookfield Asset Management, Inc.	New York	NY	3,159
LBC Credit Partners II, L.P.	Philadelphia	PA	4,464
Logan Circle Partners, L.P.	Philadelphia	PA	268
MacKay-Shields Financial Corporation	New York	NY	1,312
Oaktree Loan Fund, L.P.	Los Angeles	CA	3,261
Pacific Investment Management Company (PIMCO)	Newport Beach	CA	573
Piedmont Investment Advisors	Durham	NC	43
Pugh Capital Management, Inc.	Seattle	WA	44
Rogge Global Partners	London	UK	779
Sankaty Advisors LLC Bank Loans	Wilmington	DE	99
Sankaty Credit Opportunities IV, L.P.	Wilmington	DE	3,934
Stillwater Capital Partners, Inc.	New York	NY	613
TCW Mortgage	Dover	DE	5
TCW Credit Opportunities Fund, L.P.	Dover	DE	1,588
Western Asset Management Company	Pasadena	CA	862
Total-Fixed Income			57,424

Investment Managers' Fees
Fiscal Year Ended June 30, 2009
(Dollar Amounts in Thousands)
(continued)

<u>Manager</u>	<u>Location</u>		<u>Amount</u>
Commodities			
Credit Suisse Asset Management, L.L.C.	New York	NY	\$ 573
Deutsche Asset Management Americas, Inc.	New York	NY	3,511
Neuberger Berman Group, L.L.C.	New York	NY	1,090
Schroders Investment Management North America, Inc.	New York	NY	2,197
Wellington Management Company, L.L.P.	Boston	MA	<u>5,205</u>
Total-Commodities			12,576
Absolute Return			
Acorn Derivatives Management Corporation	White Plains	NY	600
AQR Capital Management, L.L.C.	Greenwich	CT	9,159
Barclays Global Investors, N.A.	San Francisco	CA	5,615
Boston Company Asset Management, L.L.C.	Boston	MA	1,835
Bridgewater Associates, Inc.	Westport	CT	16,876
First Quadrant, L.P.	Greenwich	CT	9,783
FX Concepts, Inc.	New York	NY	4,463
Goldman Sachs Asset Management International	London	UK	1,562
Harvest Fund Advisors, L.L.C.	Wayne	PA	253
Pacific Investment Management Company (PIMCO)	Newport Beach	CA	14,195
Zacks Investment Management	Chicago	IL	<u>75</u>
Total-Absolute Return			64,416
Real Estate-Publicly Traded			
Cohen & Steers Capital Management, Inc.	New York	NY	448
E.I.I. Realty Securities Corporation, Inc.	New York	NY	767
LaSalle Investment Management (Securities), L.P.	Baltimore	MD	298
Morgan Stanley Investment Management, Inc.	New York	NY	1,395
Security Capital Research & Management, Inc.	Chicago	IL	<u>426</u>
Subtotal-Real Estate-Publicly Traded			3,334
Real Estate-Direct Ownership			
Charter Oak Advisors, Inc.	King of Prussia	PA	864
GF Management, Inc.	Philadelphia	PA	131
Grandbridge Real Estate Capital, L.L.C.	Charlotte	NC	7
Grosvenor Investment Management U.S., Inc.	Philadelphia	PA	20
L & B Realty Advisors, L.L.P.	Dallas	TX	<u>23</u>
Subtotal-Real Estate-Direct Ownership			1,045

Investment Managers' Fees
Fiscal Year Ended June 30, 2009
(Dollar Amounts in Thousands)
(continued)

<u>Manager</u>	<u>Location</u>		<u>Amount</u>
Real Estate-Partnerships/Funds			
Apollo European Real Estate Fund III, L.P.	Purchase	NY	\$ 2,071
Apollo Real Estate Finance Corporation	New York	NY	1,800
AREFIN Co-Invest Corporation	New York	NY	52
AvalonBay Value Added Fund, L.P.	Alexandria	VA	837
AvalonBay Value Added Fund II, L.P.	Alexandria	VA	2,113
Avenue Real Estate Fund Parallel, L.P.	New York	NY	1,250
Beacon Capital Strategic Partners V, L.P.	Boston	MA	2,750
Berwind Investment Partnership IV, L.P.	Philadelphia	PA	(2) *
Berwind Investment Partnership V, L.P.	Philadelphia	PA	206
Berwind Investment Partnership VI, L.P.	Philadelphia	PA	343
BPG Co-Investment Partnership, L.P.	Philadelphia	PA	189
Blackstone Real Estate Partners Europe III, L.P.	New York	NY	3,449
Blackstone Real Estate Partners V.TE.1, L.P.	New York	NY	1,563
Blackstone Real Estate Partners VI.TE.1, L.P.	New York	NY	5,000
Broadway Partners Parallel Fund P II, L.P.	New York	NY	1,562
Broadway Partners Parallel Fund P III, L.P.	New York	NY	1,991
Cabot Industrial Value Fund III, L.P.	Boston	MA	1,318
Carlyle Europe Real Estate Partners III-A, L.P.	Washington	DC	2,765
Carlyle Realty Partners III, L.P.	Washington	DC	170
Carlyle Realty Partners IV, L.P.	Washington	DC	1,088
Carlyle Realty Partners V, L.P.	Washington	DC	3,000
Centerline Diversified Risk CMBS Fund II, L.L.C.	Irving	TX	771
Centerline High Yield CMBS Fund III, L.L.C.	Irving	TX	2,221
Centerline RE Special Situations Mortgage Fund, L.L.C.	Irving	TX	1,339
Cornerstone Patriot Fund, L.P.	Hartford	CT	800
CS Strategic Partners IV RE, L.P.	New York	NY	562
CSFB Strategic Partners II RE, L.P.	New York	NY	257
CSFB Strategic Partners III RE, L.P.	New York	NY	619
DLJ Real Estate Capital Partners II, L.P.	New York	NY	432
DLJ Real Estate Capital Partners III, L.P.	New York	NY	1,172
DLJ Real Estate Capital Partners IV, L.P.	New York	NY	3,125
DRA Growth and Income Fund VI, L.P.	New York	NY	2,054
Fillmore West Fund, L.P.	San Francisco	CA	1,248
Five Arrows Realty Securities V, L.P.	New York	NY	1,061
Fortress/PSERS Investment, L.P.	New York	NY	95
Fortress Investment Fund IV, L.P.	New York	NY	760
Fortress Investment Fund V (Fund A), L.P.	New York	NY	2,000
Hines U.S. Office Value Added Fund, L.P.	Houston	TX	557
JPMCB Strategic Property Fund	New York	NY	233
Legg Mason Real Estate Capital, Inc.	Los Angeles	CA	176
Legg Mason Real Estate Capital II, Inc.	Los Angeles	CA	1,244

Investment Managers' Fees
Fiscal Year Ended June 30, 2009
(Dollar Amounts in Thousands)
(continued)

<u>Manager</u>	<u>Location</u>	<u>Amount</u>
Real Estate-Partnerships/Funds (continued)		
Lehman Brothers/PSERS Real Estate, L.P.	New York NY	\$ 962
Lehman Brothers Real Estate Pension Partners II, L.P.	New York NY	723
Lehman Brothers Real Estate Pension Partners III, L.P.	New York NY	2,137
LEM Real Estate Mezzanine Fund II, L.P.	Philadelphia PA	937
LF Strategic Realty Investors II, L.L.C.	New York NY	841
Lubert-Adler Real Estate Fund II, L.P.	Philadelphia PA	18
MGPA Asia Fund III, L.P.	Hamilton Bermuda	6,542
MGPA Europe Fund III, L.P.	London UK	2,074
Madison Marquette Retail Enhancement Fund, L.P.	Washington DC	727
Morgan Stanley Real Estate Fund IV Special Domestic, L.P.	New York NY	258
Morgan Stanley Real Estate Fund IV Special Int'l, L.P.	New York NY	255
Morgan Stanley Real Estate Fund V Special Int'l, L.P.	New York NY	1,325
Morgan Stanley Real Estate Fund V Special U.S., L.P.	New York NY	1,174
Morgan Stanley Real Estate Fund VI Special Int'l, L.P.	New York NY	1,872
O' Connor North American Property Partners, L.P.	New York NY	1,238
O' Connor North American Property Partners II, L.P.	New York NY	2,447
Paladin Realty Latin America Investors III, L.P.	Los Angeles CA	424
Peabody Global Real Estate Partners, L.P.	New York NY	151
Prime Property Fund, L.L.C.	New York NY	545
PRISA	Parsippany NJ	776
ProLogis North American Industrial Fund, L.P.	Denver CO	1,257
RCG Longview Debt Fund IV, L.P.	New York NY	3,228
RCG Longview Equity Fund, L.P.	New York NY	1,059
RREEF America REIT II, Inc.	Chicago IL	(84) *
Stockbridge Real Estate Fund, L.P.	New York NY	1,449
Stockbridge Real Estate Fund II, L.P.	New York NY	1,185
Stockbridge Real Estate Fund III, L.P.	New York NY	4,428
Strategic Partners Value Enhancement Fund, L.P.	Los Angeles CA	825
UBS RESA	Hartford CT	619
Whitehall Street Real Estate L.P. VII & VIII	New York NY	11
William E. Simon & Sons Realty Partners, L.P.	Los Angeles CA	546
Subtotal-Real Estate-Partnerships/Funds		94,190
 Real Estate - Farmland		
Prudential Agricultural Group	Lisle IL	166
Subtotal-Real Estate-Farmland		166
Total Real Estate		98,735

*Represents reversal of amount accrued in prior fiscal year.

Investment Managers' Fees
Fiscal Year Ended June 30, 2009
(Dollar Amounts in Thousands)
(continued)

<u>Manager</u>	<u>Location</u>		<u>Amount</u>
Private Equity			
ABS Capital Partners II, L.P.	Baltimore	MD	\$ 16
Actis Emerging Markets 3, L.P.	London	UK	4,005
Allegheny New Mountain Partners, L.P.	New York	NY	278
Apax Europe VII-B, L.P.	St. Peter Port	Guernsey	2,095
Baring Asia Private Equity Fund III, L.P.	Hong Kong	China	1,987
Baring Asia Private Equity Fund IV, L.P.	Hong Kong	China	5,089
Blue Point Capital Partners II (B), LP	Cleveland	OH	326
Bridgepoint Europe IIA, L.P.	London	UK	1,084
Bridgepoint Europe IIIA, L.P.	London	UK	1,783
Bridgepoint Europe IV, L.P.	London	UK	8,430
Capital International Private Equity Fund V, L.P.	San Francisco	CA	3,000
Catterton Growth Partners, L.P.	Greenwich	CT	1,459
Catterton Partners V, L.P.	Greenwich	CT	829
Catterton Partners VI, L.P.	Greenwich	CT	2,032
Cinven Fund (Fourth), L.P. (The)	London	UK	2,839
Clarity Partners II, L.P.	Beverly Hills	CA	471
Clarity Partners, L.P.	Beverly Hills	CA	1,566
Credit Suisse First Boston Equity Partners, L.P.	New York	NY	159
Credit Suisse First Boston Int'l Equity Partners, L.P.	New York	NY	27
Crestview Capital Partners, L.P.	New York	NY	2,921
Crestview Partners II (PF), L.P.	New York	NY	5,743
CS Strategic Partners IV, L.P.	New York	NY	688
CSFB Strategic Partners II, L.P.	New York	NY	852
CSFB Strategic Partners III-B, L.P.	New York	NY	500
CVC Capital Partners Asia III Pacific, L.P.	George Town	Cayman	4,103
CVC European Equity Partners V (A), L.P.	George Town	Cayman	5,613
Deutsche European Partners IV, L.P.	London	UK	193
DLJ Merchant Banking Partners III, L.P.	New York	NY	774
DLJ Strategic Partners, L.P.	New York	NY	500
Edgewater Private Equity Fund III, L.P.	Chicago	IL	245
Evergreen Pacific Partners II, L.P.	Seattle	WA	508
Evergreen Pacific Partners, L.P.	Seattle	WA	608
First Reserve Fund XI, L.P.	Greenwich	CT	565
First Reserve Fund XII, L.P.	Greenwich	CT	1,035
Furman Selz Investors III, L.P.	New York	NY	(31) *
Graham Partners Investments (B), L.P.	Newtown Square	PA	140
Greenpark International Investors III, L.P.	London	UK	1,728
Greenwich Street Capital Partners II, L.P.	New York	NY	208
Halifax Capital Partners, L.P	Wilmington	DE	(17) *

*Represents reversal of amount accrued in prior fiscal year.

Investment Managers' Fees
Fiscal Year Ended June 30, 2009
(Dollar Amounts in Thousands)
(continued)

<u>Manager</u>	<u>Location</u>	<u>Amount</u>
Private Equity (continued)		
HSBC Private Equity Fund 6, L.P.	George Town Cayman	\$ 3,621
Irving Place Capital Partners III, L.P.	New York NY	2,627
Jefferies Capital Partners IV, L.P.	New York NY	1,644
KKR 2006 Fund, LP	New York NY	2,000
KRG Capital Fund IV (PA), L.P.	Denver CO	3,879
Landmark Equity Partners XIII, L.P.	Simsbury CT	875
Landmark Equity Partners XIV, L.P.	Wilmington DE	1,331
Landmark Mezzanine Partners, L.P.	Simsbury CT	27
Lehman Brothers Merchant Banking Partners II, L.P.	New York NY	60
Trilantic Capital Partners IV, L.P.	New York NY	1,485
Lindsay Goldberg & Bessemer, L.P.	New York NY	978
Milestone Partners II, L.P.	Rosemont PA	(40) *
Milestone Partners III, L.P.	Rosemont PA	631
Morgan Stanley Dean Witter Capital Partners IV, L.P.	New York NY	221
Navis Asia Fund V, L.P.	Kuala Lumpur Malaysia	1,645
New Mountain Partners III, L.P.	New York NY	4,194
New Mountain Partners, L.P.	New York NY	560
New York Life Capital Partners I, L.P.	New York NY	364
New York Life Capital Partners II, L.P.	New York NY	606
New York Life Capital Partners III, L.P.	New York NY	2,000
New York Life Capital Partners IV, L.P.	New York NY	2,000
Nordic Capital VII Beta L.P.	St. Helier Guernsey	4,482
PAI Europe III, L.P.	Paris France	704
PAI Europe IV, L.P.	Paris France	1,007
PAI Europe V, L.P.	St. Peter Port Guernsey	4,934
Palladium Equity Partners II-A, LLC	New York NY	322
Partners Group Secondary 2008, L.P.	St. Peter Port Guernsey	4,084
Permira IV, L.P. 2	London UK	1,929
Platinum Equity Capital Partners II, L.P.	Los Angeles CA	1,629
PNC Equity Partners II, L.P.	Pittsburgh PA	630
PNC Equity Partners, L.P.	Pittsburgh PA	30
Providence Equity Partners VI, L.P.	Providence RI	2,574
Quadrangle Capital Partners I, L.P.	New York NY	980
Quadrangle Capital Partners II, L.P.	New York NY	2,946
Sterling Capital Partners, L.P.	Northbrook IL	422
TPG Partners II, L.P.	Fort Worth TX	(4) *
TPG Partners V, L.P.	Fort Worth TX	831
TPG Partners VI, L.P.	Fort Worth TX	5,589
US Equity Partners II, L.P.	New York NY	882
Subtotal-Private Equity		129,030

*Represents reversal of amount accrued in prior fiscal year.

Investment Managers' Fees
Fiscal Year Ended June 30, 2009
(Dollar Amounts in Thousands)
(continued)

<u>Manager</u>	<u>Location</u>		<u>Amount</u>
Private Debt			
Avenue Asia Special Situations Fund III, L.P.	New York	NY	\$ 491
Avenue Asia Special Situations Fund IV, L.P.	New York	NY	4,500
Avenue Europe Special Situations Fund, L.P.	New York	NY	4,097
Avenue Special Situations Fund IV, L.P.	New York	NY	1,105
Avenue Special Situations Fund V, L.P.	New York	NY	3,750
Cerberus Institutional Partners, L.P. (Series Two)	New York	NY	237
Cerberus Institutional Partners, L.P. (Series Three)	New York	NY	500
Cerberus Institutional Partners, L.P. (Series Four)	New York	NY	6,000
Gleacher Mezzanine Fund, L.P.	New York	NY	33
Gleacher Mezzanine Fund II, L.P.	New York	NY	1,172
Gold Hill Venture Lending 03-A, L.P.	Santa Clara	CA	519
GSC Partners CDO Investors IV, L.P.	New York	NY	1,665
GSC Recovery III, L.P.	New York	NY	2,500
NYLIM Mezzanine Partners Parallel Fund, L.P.	New York	NY	334
NYLIM Mezzanine Partners Parallel Fund II, L.P.	New York	NY	1,875
OCM Opportunities Fund VII, L.P.	Los Angeles	CA	1,258
OCM Opportunities Fund VII-B, L.P.	Los Angeles	CA	3,510
Versa Capital Fund L.P.	Wayne	PA	96
Versa Capital Fund II, L.P.	Philadelphia	PA	3,020
Windjammer Senior Equity Fund III, L.P.	Newport Beach	CA	408
Subtotal-Private Debt			37,070
Venture Capital			
Aisling Capital II, L.P.	New York	NY	612
Aisling Capital III, L.P.	New York	NY	623
Co-Investment 2000 Fund, L.P. (The)	Radnor	PA	321
Co-Investment Fund II, L.P. (The)	Radnor	PA	1,860
Cross Atlantic Technology Fund, L.P.	Radnor	PA	103
Cross Atlantic Technology Fund II, L.P.	Radnor	PA	74
CS Strategic Partners IV VC, L.P.	New York	NY	375
CSFB Strategic Partners III-VC, L.P.	New York	NY	438
Franklin Capital Associates III, L.P.	Franklin	TN	84
Jefferson Partners Fund IV (PA), L.P.	Toronto	Canada	492
KBL Partnership, L.P.	New York	NY	286
Landmark Equity Partners V, L.P.	Simsbury	CT	16
Tenaya Capital IV-P, L.P.	New York	NY	740
Tenaya Capital V-P, L.P.	New York	NY	984
LLR Equity Partners, L.P.	Philadelphia	PA	232
LLR Equity Partners II, L.P.	Philadelphia	PA	845

Investment Managers' Fees
Fiscal Year Ended June 30, 2009
(Dollar Amounts in Thousands)
(continued)

<u>Manager</u>	<u>Location</u>	<u>Amount</u>
Venture Capital (continued)		
LLR Equity Partners III, L.P.	Philadelphia PA	\$ 2,517
Novitas Capital, L.P.	Wayne PA	114
Novitas Capital II, L.P.	Wayne PA	1,500
Perseus-Soros BioPharmaceutical Fund, L.P.	New York NY	657
Psilos Group Partners III, L.P.	New York NY	532
Quaker BioVentures, L.P.	Philadelphia PA	1,516
Quaker BioVentures II, L.P.	Philadelphia PA	2,583
SCP Private Equity Partners, L.P.	Wayne PA	249
SCP Private Equity Partners II, L.P.	Wayne PA	1,181
Starvest Partners II, L.P.	New York NY	278
Sterling Venture Partners, L.P.	Baltimore MD	117
TDH III, L.P.	Rosemont PA	<u>3</u>
Subtotal-Venture Capital		19,332
		<hr/>
Total-Alternative Investments		185,432
 Total External Management		 \$ 464,641
 Total Internal Management		 <u>8,998</u> **
 Total Investment Management		 <u>\$ 473,639</u>

**Internal Management fees include salaries and fringe benefits of \$4,329 and operating expenses of \$4,669.

Internal Equity Trading Desk

Internal Equity Trading Desk

One of the benefits of managing a significant amount of assets internally is that PSERS can have its own trading desk. A majority of the U.S. equity trades for the Fund are executed by PSERS' internal trading desk. Two of the internal U.S. equity managers as well as a number of the external U.S. equity managers utilize the trading desk to execute trades. The objectives of PSERS' internal trading desk include:

- to obtain best execution; and
- to pay the lowest possible commissions consistent with obtaining best execution

The trading desk provides PSERS with access to information on the markets from sell-side brokers which helps in the management of the investments of the Fund. The trading desk also provides portfolio transition management services to the System. When portfolio managers are terminated, the trading desk handles the liquidation of the portfolio or the transition from one portfolio manager to another, minimizing the costs of those transitions.

The order flow generated by the trading desk provides the System with access to initial public offerings (IPOs). IPOs can be a source of incremental returns since most generally trade higher after being issued. This IPO access generated approximately \$17 million in profits for PSERS since 1999.

PSERS' trading desk executed approximately 29,000 U.S. and Non-U.S. orders for the purchase and sale of stock, currency, futures, and options during the fiscal year ended June 30, 2009. The total dollar amount of U.S. and Non-U.S. orders traded during the fiscal year ended June 30, 2009, was approximately \$24.7 billion.

Public Market Emerging Investment Manager Program

Summary of PSERS' Public Market Emerging Investment Manager (PMEIM) Program (as of December 31, 2009)

The Public Market Emerging Investment Manager (PMEIM) Program is a sub-section of PSERS U.S. Equity, Non-U.S. Equity, Absolute Return, and Fixed Income investment classes.

Policy

Consistent with its fiduciary responsibilities, The Board has established the (PMEIM) Program to:

1. Locate and fund managers with successful histories of generating positive alpha with risk commensurate with the alpha generated (positive risk adjusted returns);
2. Provide a source of potential managers for the main fund; and
3. Assist public market emerging investment management firms with positive risk adjusted returns grow through the use of the System's name in the managers' marketing efforts.

The Board has allocated up to \$1.0 billion to the PMEIM Program. Funding for each investment manager will come from assets allocated within the main fund similar to or most closely related to the investment manager's mandate. The maximum number of investment managers in the program at any one time shall not exceed 25. The program may run with less than 25 investment managers.

Investment managers desiring to participate in the program must meet the following required criteria:

- Firms must be registered under the Investment Advisors Act of 1940 or be exempt therefrom (and will maintain such registration or exemption);
- Firms must provide transparency of positions and transactions;
- Firms must provide at least monthly liquidity;
- Firms, the portfolio manager, or any combination thereof must have a three-year historical, performance record verified by at least one consultant or accounting firm in accordance with the Global Investment Performance Standards (GIPS);
- Firms must have no more than \$1.5 billion of total assets under management when hired (existing investment managers will be terminated within a reasonable period of time from the PMEIM Program when the total assets under management exceeds \$3.0 billion); and
- For performance based fee accounts, the managers must have a hurdle rate and they must exceed this rate to earn the performance-based fee.

Preference will be given to investment managers deemed as able to meet the objectives, goals, and required criteria noted above plus having one or more of the following characteristics:

- Pennsylvania investment management firms headquartered or incorporated within the Commonwealth; and/or
- Minority and/or women-owned investment management firms approved by the Office of Minority and Women Business Enterprise in accordance with the criteria established by Executive Order No. 1987-18 and 4 Pennsylvania Code, Section 68.204


Market Value as of December 31, 2009: \$695.2 million or 1.5% of the total market value of the Fund.

Number of External Investment Managers: PSERS had contracts with 17 external investment managers in the PMEIM Program.

PSERS' PMEIM Investment Managers
(Dollar Amounts in Millions)
(as of December 31, 2009)
(unaudited)

<i>External Manager</i>	<i>Market Value</i>
AH Lisanti	\$ 26.2
Ativo Capital	19.0
Biondo Group	12.8
Conestoga Capital	48.0
Denali	37.6
EDMP	45.4
Hanseatic	46.1
Harvest Funds	59.3
Hellman Jordan	30.7
John Hsu	69.5
Opus Capital	33.4
Piedmont Investment Advisors	19.1
Pugh Capital	44.4
Shah Capital	62.2
Stillwater Capital	34.7
Westwood Global	58.2
Zacks	48.7
Total PSERS' PMEIM Portfolios	\$ 695.2

Numbers may not add due to rounding.

- *Pennsylvania-Based Investment Managers*
 - *Investments in Pennsylvania*
- 

Pennsylvania-Based Investment Managers

Commitment to Pennsylvania-Based Investment Managers (as of December 31, 2009)

As noted previously, the members of the Board and Staff are fiduciaries and must act solely in the interests of the members of the System and for the exclusive benefit of the System's members. In creating the investment program, the Board hires external investments managers and internal investment managers. The Board has determined that it is in the best interest of the System to manage assets internally when (1) the System's staff has the proven ability to internally manage portfolios at least as well as the external investment managers, and (2) the cost of investing those assets is no greater than the cost that would have been incurred to have those assets externally managed. The Board will also consider the diversification benefits that may be achieved by allocating assets to external portfolio managers even when conditions (1) and (2) are met.

The Board evaluates external managers based on a variety of factors, including, (1) their expected future performance; (2) their investment philosophy and style; (3) their investment process; (4) their personnel; (5) cost; and (6) how their philosophy and style fits in with the existing investment structure. In selecting external managers, PSERS will show preference to Pennsylvania-based potential managers that demonstrate similar strengths to alternative managers without a Pennsylvania nexus.

PSERS has shown a tremendous commitment to Pennsylvania's financial services industry by having assets managed by firms based in Pennsylvania or by firms with offices in Pennsylvania. The following is a list of both the assets managed internally by PSERS and externally from offices located in Pennsylvania, as of December 31, 2009:

<i>Pennsylvania-Based Manager</i>	<i>Market Value (in millions)</i>	<i>Percentage of the Fund</i>
Internal Management		
U.S. Equity:		
S&P 500 Index	\$ 4,317.5	9.3%
S&P 400 Index	441.0	0.9%
S&P 600 Index	413.1	0.9%
Non-U.S. Equity:		
ACW ex-U.S. Index	4,564.1	9.8%
Fixed Income:		
PSERS TIPS	1,330.6	2.8%
PSERS Active Aggregate	1,151.7	2.5%
Cash & Cash Equivalents:		
STIF	2,891.7	6.2%
Total Internal Management	\$ 15,109.7	32.4%
External Management		
U.S. Equity:		
Biondo Group	12.2	0.0%
Conestoga Capital Advisors	47.6	0.1%
Turner Investment Partners, Inc.	51.2	0.1%
Fixed Income:		
Aberdeen Asset Management, Inc.	522.1	1.1%

Commitment to Pennsylvania-Based Investment Managers
 (as of December 31, 2009)
 (continued)

Real Estate:			
BPG Co-Investment Partnership, LP	\$	20.5	0.0%
BPG Investment Partnership VI, LP		33.0	0.1%
Charter Oak Advisors, Inc.		88.8	0.2%
GF Management, Inc.		60.7	0.1%
Grandbridge Real Estate Capital, LLC		3.0	0.0%
LEM Real Estate Mezzanine Fund II, LP		37.3	0.1%
Lubert-Adler Real Estate Fund II, LP		3.1	0.0%
Lubert-Adler Real Estate Fund III, LP		12.3	0.0%
Lubert-Adler Real Estate Fund IV, LP		38.6	1.0%
Lubert-Adler Real Estate Fund V, LP		61.7	1.0%
Lubert-Adler Real Estate Fund VI, LP		57.3	0.1%
Private Equity and Debt:			
Graham Partners, LP		23.7	0.1%
Milestone Partners II, LP		21.7	0.0%
Milestone Partners III, LP		18.1	0.0%
PNC Equity Partners I, LP		24.3	0.1%
PNC Equity Partners II, LP		12.2	0.0%
Versa Capital Fund I, LP		68.8	0.1%
Versa Capital Fund II, LP		6.0	0.0%
Venture Capital:			0.0%
Adams Capital Management, LP		1.6	0.0%
Co-Investment Fund 2000, LP		66.1	0.1%
Co-Investment Fund II, LP		33.0	0.1%
Cross Atlantic Technology Fund, LP		12.0	0.0%
Cross Atlantic Technology Fund II, LP		14.2	0.0%
LLR Equity Partners, LP		15.7	0.0%
LLR Equity Partners II, LP		63.7	0.1%
LLR Equity Partners III, LP		40.0	0.1%
NEPA Venture Fund II, LP		1.2	0.0%
Novitas Capital, LP		1.2	0.0%
Novitas Capital II, LP		8.7	0.0%
P/A Fund, LP		0.6	0.0%
Quaker Bio-Ventures, LP		17.6	0.0%
Quaker Bio-Ventures II, LP		30.8	0.1%
SCP Private Equity Partners, LP		2.5	0.0%
SCP Private Equity Partners II, LP		69.5	0.1%
TDH III, LP		0.8	0.0%
Total External Management	\$	1,603.4	3.4%
Total Investment Portfolios Managed in PA	\$	16,713.1	35.8%

In FY 2009, investment manager fees paid to external firms managing PSERS' assets from offices located in Pennsylvania amounted to \$27.6 million, or 5.94% of the total external investment manager fees.

Investments in Pennsylvania

Summary of Investments in Pennsylvania (as of December 31, 2009)

Where investment characteristics including yield, risk, and liquidity are equivalent, the Board's policy favors investments that have a positive impact on the economy of Pennsylvania. The Board, in managing the investment portfolio, will also be cognizant of concentration risk to any one region, including Pennsylvania. The Fund will continue to seek investments in Pennsylvania-based companies when the investment characteristics are equivalent to other favorable investments subject to diversification considerations.

The following is a table of Pennsylvania-based investments and other statistics at December 31, 2009 (\$'s in millions):

<i>Asset Class</i>	<i>Total PA Market Value (PSERS' Portion)</i>	<i>Total PA Market Value (Total Invested)</i>	<i># of People Employed</i>	<i>Payroll</i>
U.S. Equities**	\$ 88.8	\$ 88.8	*	*
Fixed Income**	51.4	51.4	*	*
Private Real Estate	218.4	2,578.6	1,357	\$ 32.2
Private Markets:				
Venture Capital	145.3	1,380.5	5,556	\$ 285.6
Private Equity	1,898.2	12,813.5	28,579	\$ 1,110.9
Private Debt	265.3	3,646.1	14,295	\$ 705.7
Total	\$ 2,667.4	\$ 20,558.9	49,787	\$ 2,134.4

* Statistics for publicly traded companies not included due to the difficulty in obtaining the information.

** Market value is presented as of September 30, 2009.

U.S. Equities

PSERS invests in the stock of Pennsylvania-based companies through the various U.S. Equity portfolios managed by external and internal portfolio managers. PSERS has always had substantial investments in large national firms located in Pennsylvania, a list of which is included later in this section.

Fixed Income Securities

PSERS invests in the debt of Pennsylvania-based companies through the various Fixed Income portfolios managed by external and internal portfolio managers. PSERS has always had substantial investments in large national firms located in Pennsylvania, a list of which is included later in this section.

Summary of Investments in Pennsylvania
(as of December 31, 2009)
(continued)

Private Real Estate

PSERS has investments in limited partnerships that have invested in Pennsylvania real estate properties. PSERS has committed \$312.5 million in four funds (Fund IV, Fund V, Fund VI, and a Co-Investment Fund) managed by BPG Properties, Ltd., located in Philadelphia. PSERS has committed \$550 million in five funds (Lubert-Adler Funds II, III, IV, V and VI) managed by Lubert-Adler, another Pennsylvania-based real estate manager. Finally, PSERS has committed \$75 million in one fund (LEM Real Estate Mezzanine Fund II) managed by LEM Mezzanine Partners, located in Philadelphia.

As of December 31, 2009, PSERS' Pennsylvania real estate portfolio contained 22.7 million square feet of office, retail, and warehouse space and 177,585 apartment, hotel and condominium units. The gross market value of the Pennsylvania real estate portfolio investments totaled \$2.6 billion, of which PSERS' ownership share was \$218.4 million. The portfolio contains numerous notable Pennsylvania real estate investments, including:

- 5 North Fifth Street - PSERS owns a 100% interest in this major downtown Harrisburg, PA, office building that contains 71,080 square feet of office space. The building is PSERS' headquarters and is fully occupied by PSERS.
- King of Prussia Business Center – This office building is located in King of Prussia, PA. The King of Prussia Business Center contains approximately 175,000 square feet in 14 buildings on 12.5 acres. The King of Prussia Market is the largest suburban office market in the Philadelphia region and is in close proximity to most of the region's primary highways. This investment was made by BPG Investment Partnership V.
- The National at Old City – This condominium complex is located in Philadelphia, PA. The National at Old City consists of 153 units and contains 208,919 square feet of condominium space. This investment was made by Lehman Brothers Real Estate Pension Partners II.
- Kenmawr – This investment is a part of a long-term joint venture relationship between Lubert-Adler and Philadelphia Management and Companies (PMC) that specializes in adaptive re-use of vacant buildings into stable, high quality rental apartments within and outside of Pennsylvania. The Kenmawr investment is located in Pittsburgh, PA and consists of 206 apartment units and 44 commercial units. The Kenmawr investment was made in Lubert-Adler Real Estate Funds V and VI.
- Brandywine Office Portfolio – The Brandywine Office Portfolio consists of 29 properties totaling 1.6 million square feet and is located in the Lehigh Valley. This investment was made by DRA Growth and Income Fund VI.

Summary of Investments in Pennsylvania
(as of December 31, 2009)
(continued)

Venture Capital

PSERS' Venture Capital program has committed \$2,208.9 million to 50 partnerships since the inception of the program. An objective of this program is to target partnerships that demonstrate an ability to invest in Pennsylvania-based companies. Selected partnerships offer diversification according to geographic region and financing stage within Pennsylvania. From the inception of this program to December 31, 2009, 25 of the 50 partnerships were headquartered in Pennsylvania.

A key objective of PSERS' venture capital program is to attract both national and regional funds into the Pennsylvania small business community. Venture capital investments serve to accelerate economic growth in both the business sector and the community due to an increase in employment and revenues within the Commonwealth. Following are a sample of Pennsylvania companies invested in by PSERS through the Venture Capital program:

- Ciradiant Systems, Inc., Allentown, PA – Ciradiant provides optical component developers, network equipment manufacturers, and telecom service providers with award winning test systems. Circadiant's Optical Standards Testers generate real-world optical test signals that greatly improve network reliability and interoperability. This investment was made by Pennsylvania Early Stage Partners.
- E-Duction, Inc., Blue Bell, PA – E-Duction was launched to capitalize on a growing trend that has emerged in payment technology - payroll deduction. In 2002, E-Duction introduced the first payroll deduction card, CLEAR, that gives employees interest-free purchasing power, 365 days per year. CLEAR is an innovative employee program that allows employees to make purchases at over 33 million MasterCard acceptance locations worldwide and spread payments out over future paychecks. Pennsylvania Early Stage Partners made this investment.
- Neuronyx, Inc., Malvern, PA – Neuronyx is focused on neurological diseases and disorders. With a multi-faceted approach to address brain diseases, Neuronyx balances the significant but long-term promise of stem cell and gene-based therapies with the more conventional development time and risk of both scientific and regulatory nature of small molecule therapies. Rather than utilizing stem cells derived from embryonic and fetal sources, Neuronyx has developed a proprietary process for isolating and expanding adult bone marrow stem cells to provide extremely large, homogenous populations with desirable therapeutic characteristics. Pennsylvania Early Stage Partners made this investment.
- Neutronics, Inc., Malvern, PA - Neuronetics, Inc. is a privately held medical device company focused on developing non-invasive therapies for psychiatric and neurological disorders using MRI-strength magnetic field pulses. Neuronetics is the leader in the development of TMS Therapy, a non-invasive form of neuromodulation. KBL Healthcare Ventures made this investment.

Summary of Investments in Pennsylvania
(as of December 31, 2009)
(continued)

- ZOLL LIFECOR, Inc., Pittsburgh, PA – ZOLL LIFECOR, Inc., a subsidiary of ZOLL Medical Corporation, manufacturers and markets the LifeVest wearable defibrillator, which is worn by a patient at risk for sudden cardiac arrest. Sudden cardiac arrest leads to death within a few minutes if not treated by an electrical shock from a defibrillator. TheLifeVest device monitors the patient's heart continuously and, if the patient goes into a life threatening heart rhythm, delivers a shock treatment to restore the patient's heart to normal rhythm. TDH III, L.P. made this investment.

PSERS' is generally the lead investor in many of the venture capital funds in which PSERS invests. As a lead investor, PSERS provides Pennsylvania with capital from numerous out-of-state investors. As of December 31, 2009, PSERS' Venture Capital partnerships invested in 92 Pennsylvania locations employing approximately 5,556 employees with a combined payroll of \$185.6 million. The market value of these investments is \$1,380.5 million, of which PSERS' share is \$145.3 million.

Private Equity

PSERS' is generally the lead investor in many of the private equity funds in which PSERS invests. As a lead investor, PSERS provides Pennsylvania with capital from numerous out-of-state investors. As of December 31, 2009, PSERS' Private Equity partnerships invested in 1,034 Pennsylvania locations employing approximately 28,579 employees with a combined payroll of \$1,110.9 million. The market value of these investments is \$12.8 billion, of which PSERS' share is \$1,898.2 million.

The following companies are a sample of Pennsylvania investments funded through PSERS private equity partnerships:

- AirClic, Newtown, PA – AirClic is a leading provider of mobile business process solutions that offer organizations real-time visibility to the "who, what, where, when, and why" of their entire field operations. Using AirClic-enabled wireless devices, managers and workers can easily and economically capture, exchange, and access critical data that represent people, assets and activity. With its unsurpassed user-adoption rate, AirClic is driving new levels of accountability and improved customer service for many of the world's leading companies. Edgewater Private Equity Fund III made this investment.
- CODi, Inc., Harrisburg, PA – CODi, Inc. is a trusted provider of lightweight, high-quality notebook computer cases and accessories to millions of users. Since 1992, CODi has been a pioneer in the notebook and tablet case industry. CODi products use only premium materials that provide a lifetime of use, even in today's demanding business environment. CODi's accumulated knowledge dealing with the "corporate road warrior" allows the company to uniquely service corporate and consumer needs with precision. CODi provides the most comprehensive business solutions by delivering cost savings without sacrificing quality. The investment was brought about through Milestone Partners II.

Summary of Investments in Pennsylvania
(as of December 31, 2009)
(continued)

- EnerSys, Inc., Reading, PA – EnerSys, the world leader in stored energy solutions for industrial applications, manufactures and distributes reserve power and motive power batteries, chargers, power equipment, and battery accessories to customers worldwide. Motive power batteries are utilized in electric forklift trucks and other commercial electric powered vehicles. Reserve power batteries are used in the telecommunication and utility industries, uninterruptible power suppliers, and numerous applications requiring standby power. The company also provides aftermarket and customer support services to its customers in over 100 countries through its sales and manufacturing locations around the world. Morgan Stanley Dean Witter Capital Partners IV, L.P. made this investment.

- Gorell Enterprises, Indiana, PA - Gorell Enterprises is a manufacturer of specially engineered, custom-manufactured windows for replacement and new-construction applications, patio doors, aluminum storm windows and doors, sunrooms, and conservatories. Gorell is well known in the industry for placing strong emphasis on designing and manufacturing strong, durable high-quality products. Gorell was the national winner of the 2006 ENERGY STAR® “Sustained Excellence” Award, given for their new window models to make homes more energy efficient as well as secure. The windows feature three panes of glass, two of which sandwich a PVB interlayer to keep the glass intact. Thick, multi-chambered frame construction, double locks add structural strength and durability. AIP windows incorporate a SolarControl Plus® Low-E coating and argon gas fill for cost-saving energy efficiency year round—and qualify them for the ENERGY STAR® label. PNC Equity Partners L.P. made this investment.

- ICG Commerce, Inc., King of Prussia, PA - ICG Commerce is a leading Procurement Services Provider exclusively focused on helping companies achieve greater control and increased value from their procurement organization. The company offers sourcing and on-going operational buying services that enable companies to better manage spending, increase sourcing effectiveness, ensure compliance, and drive continual improvements. By working with dozens of leading procurement organizations, ICG Commerce brings its execution-based and continually growing compound experience to every customer contract negotiated and transaction processed. Graham Partners Investments made this investment.

- Interface Solutions, Inc., Lancaster, PA - Interface Solutions Inc. (ISI) is a leading manufacturer of sealing systems and engineered composite materials, including a unique line of specialty papers. The organization enjoys long-established cooperative partnerships with customers in an array of worldwide markets. Recent acquisitions, expansions, and capital investments in research facilities empower ISI to offer both OEM and aftermarket customers unmatched technical and design support and application testing. ISI has an extraordinary depth of experience and engineering knowledge, with roots to predecessor companies dating back over 90 years. ISI was created as an independent, private corporation in 1999; formed from the organization previously known as Armstrong Industrial Specialties Inc. (AIS). PNC Equity Partners L.P. made this investment.

Summary of Investments in Pennsylvania
(as of December 31, 2009)
(continued)

- Keystone Automotive Operations, Inc., Exeter, PA - Keystone Automotive Operations reigns as the largest distributor and marketer of specialty automotive parts in the world with more than a quarter of a million accessories and performance parts representing over 700 product lines. Keystone Automotive's main warehouse, the largest automotive aftermarket warehouse in the industry, consisting of 800,000 square-foot is located in northeastern Pennsylvania. Keystone prides itself on products and delivery capabilities. Keystone makes this evident by constantly expanding with a 185,000 square-foot hub in Kansas City, an 80,000 square-foot hub in Corona, California, and satellites in Alabama, Colorado, Florida, Georgia, Illinois, Indiana, Maryland, Massachusetts, New York, New Mexico, North Carolina, Ohio, Pennsylvania, Tennessee, Texas and Canada. In today's ever changing and expanding marketplace, Keystone Automotive Operations is shaping its future and the future of the automotive aftermarket industry through careful planning, continued growth, and ongoing expansion. Irving Place Capital Partners II, LP made this investment.

- Tangent Rail Corporation, Pittsburgh, PA – Tangent Rail Corporation serves the railroad industry with quality treated wood products and preservatives, rail grinding, switching and track maintenance services, and environmentally friendly railroad tie pickup and disposal solutions. PNC Equity Partners L.P. made this investment.

Private Debt

PSERS' is generally the lead investor in many of the private debt funds in which PSERS invests. PSERS has committed \$225.0 million to Versa Capital Partners, LP (formerly known as Chrysalis Capital Partners L.P.) managed by Versa Capital Management, located in Wayne, Pennsylvania. As of December 31, 2009, PSERS' Private Debt partnerships invested in 216 Pennsylvania locations employing approximately 14,295 employees with a combined payroll of \$705.7 million. The market value of these investments is \$3.6 billion, of which PSERS' share is \$265.3 million.

The following companies are a sample of Pennsylvania investments made through PSERS' Private Debt program:

- PQ Corporation, Berwyn, PA – PQ Corporation is a leading producer of silicate, zeolite, and other performance materials serving the detergent, pulp and paper, chemical, petroleum, catalyst, water treatment, construction, and beverage markets. It is a global enterprise, operating in 19 countries on five continents. Potters Industries, a wholly owned subsidiary, is a leading producer of engineered glass materials serving the highway safety, polymer additive, metal finishing, and conductive particle markets. OCM Opportunities Fund VII, LP made this investment.

- Philadelphia Newspapers LLC, Philadelphia, PA – Philadelphia Newspapers LLC publishes newspapers, offering readers services; publication services, such as regional publications, weeklies, and magazines; marketing services, such as data base marketing and commercial printing; and advertising services, including automotive, recruitment, real estate, general, retail, national, and online. It also publishes real estate magazines and other periodicals, and operates an on-line listing service. Cerberus Institutional Partners (Series Four) made this investment.

Pennsylvania-Based Publicly Traded Stocks
(as of September 30, 2009)

<i>Security</i>	<i>Shares Outstanding</i>	<i>Market Value</i>
Air Products & Chemicals, Inc.	108,461	\$ 8,414,404
Airgas, Inc.	21,215	1,026,170
Alcoa, Inc.	231,946	3,043,132
Allegheny Energy, Inc.	34,587	917,247
Allegheny Technologies, Inc.	20,014	700,290
Amerigas Partners	14,200	511,768
Amerisourcebergen Corp.	69,663	1,559,058
Ansys, Inc.	37,276	1,394,868
Armstrong World Industries, Inc.	1,900	65,474
Atlas Energy, Inc.	4,751	128,619
Atlas Pipeline Partners	2,200	16,082
Black Box Corp.	16,550	415,240
Brandywine Realty Trust	49,563	547,176
Buckeye Partners	25,350	1,227,194
Calgon Carbon Corp.	41,280	612,182
Cephalon, Inc.	25,304	1,473,705
Charming Shoppes, Inc.	2,052,830	10,120,452
CIGNA Corp.	70,553	1,981,834
CNX Gas Corp.	50,300	1,544,210
Comcast Corp. Class A	2,222	37,507
Consolidated Energy, Inc.	95,777	4,320,500
Crown Holdings, Inc.	67,193	1,827,650
Dentsply International, Inc.	30,324	1,047,391
Dollar Financial Corp.	4,030	64,561
Endo Pharmaceuticals Holdings, Inc.	20,500	463,915
EQT Corp.	78,514	3,344,696
eResearch Technology, Inc.	127,191	890,337
Federated Investors, Inc. Class B	18,055	476,110
FMC Corp.	14,794	832,163
GSI Commerce, Inc.	38,680	746,911
H.J. Heinz Company	64,322	2,556,800
Herley Industries, Inc.	37,300	486,765
Hershey Company	33,842	1,315,100
Horsehead Holding Corp.	287,365	3,367,918
Interdigital, Inc.	11,210	259,624
Internet Capital Group, Inc.	25,641	214,359
Kensley Nash Corp.	33,970	983,432
Koppers Holdings, Inc.	4,790	142,024
Kulicke & Soffa Industries, Inc.	98,708	595,209
Lannett Company, Inc.	39,900	298,452
Liberty Property Trust	72,014	2,342,615
Michael Baker Corp.	21,550	783,127

Pennsylvania-Based Publicly Traded Stocks
 (as of September 30, 2009)
 (continued)

<i>Security</i>	<i>Shares Outstanding</i>	<i>Market Value</i>
Mylan Labs, Inc.	62,311	\$ 997,599
Parkvale Financial Corp.	38,846	357,383
Penn Virginia Corp.	13,790	315,929
Penn Virginia Resource Partners	9,900	169,686
Pep Boys – Manny Moe & Jack	144,300	1,409,811
P H Glatfelter Company	10,870	124,788
PMA Capital Corp. Class A	153,164	871,503
PNC Financial Services Group, Inc.	98,361	4,779,361
Portec Rail Products, Inc.	49,900	473,551
PPG Industries, Inc.	33,654	1,958,999
PPL Corp.	76,851	2,331,659
Quaker Chemical Corp.	17,400	381,582
RAIT Financial Trust	36,530	107,398
Rex Energy Corp.	92,090	768,952
Spectrum Control, Inc.	73,308	622,385
Sunoco, Inc.	23,857	678,732
Sunoco Logistics Partners	59,800	3,543,150
TF Financial Corp.	15,400	290,675
Triumph Group, Inc.	6,200	297,538
II-VI, Inc.	39,075	994,068
United States Steel Corp.	69,398	3,079,189
Universal Stainless & Alloy Products, Inc.	17,833	325,452
Univest Corp. of Pennsylvania	20,900	452,903
Urban Outfitters, Inc.	7,200	217,224
Wabtec Corp.	3,870	145,241
Total		\$ 88,791,029

Pennsylvania-Based Corporate Bonds
(as of September 30, 2009)

<i>Security</i>	<i>Interest Rate (%)</i>	<i>Maturity Date</i>	<i>Par Value</i>	<i>Market Value</i>
Airgas, Inc.	7.125	10/01/2018	130,000	\$ 134,063
Alcoa, Inc.	5.900	02/01/2027	5,000,000	4,252,100
Allegheny County Hospital	5.000	09/01/2018	2,000,000	2,214,860
Allegheny Ludlum Corp.	6.950	12/15/2025	300,000	270,378
Allegheny Technologies, Inc.	8.375	12/15/2011	80,000	84,717
Allegheny Technologies, Inc.	9.375	06/01/2019	1,015,000	1,149,153
Allentown PA Taxable	0.000	10/01/2022	1,800,000	679,716
Allentown PA Taxable	0.000	10/01/2023	3,170,000	1,092,794
Allentown PA Taxable	0.000	10/01/2024	2,605,000	820,262
Allentown PA Taxable	0.000	10/01/2025	3,660,000	1,055,507
Allentown PA Taxable	0.000	10/01/2026	3,655,000	968,867
Bell Telephone Co. of PA	8.350	12/15/2030	125,000	145,025
Comcast Corp.	10.625	07/15/2012	5,000,000	5,960,350
Comcast Corp.	6.500	01/15/2015	1,240,000	1,381,720
Comcast Corp.	5.900	03/15/2016	1,025,000	1,101,568
Comcast Corp.	6.500	01/15/2017	330,000	362,198
Comcast Corp.	5.875	02/15/2018	200,000	213,106
Comcast Corp.	7.050	03/15/2033	470,000	533,008
Comcast Corp.	6.450	03/15/2037	50,000	52,945
Comcast Corp.	6.950	08/15/2037	520,000	580,403
Consolidated Natural Gas Co.	6.850	04/15/2011	2,500,000	2,665,500
Consolidated Natural Gas Co.	6.250	11/01/2011	4,815,000	5,191,533
Consolidated Natural Gas Co.	5.000	03/01/2014	475,000	500,465
Duquesne Light Company	6.700	04/15/2012	5,000,000	5,267,900
Harrisburg PA Taxable	0.000	04/01/2012	750,000	701,573
Harrisburg PA Taxable	0.000	04/01/2014	440,000	372,024
Hershey Company	8.800	02/15/2021	1,000,000	1,274,980
Penn National Gaming, Inc.	6.875	12/01/2011	1,270,000	1,263,650
Penn National Gaming, Inc.	6.750	03/01/2015	2,215,000	2,120,863
Pennsylvania Electric Company	5.200	04/01/2020	990,000	986,911
PNC Funding Corp.	4.250	09/21/2015	1,072,000	1,076,213
PPL Capital Funding, Inc.	6.700	03/30/2067	1,295,000	1,081,325
Rite Aid Corp.	8.625	03/01/2015	1,207,000	982,196
Rite Aid Corp.	9.375	12/15/2015	840,000	682,500
Rite Aid Corp.	9.750	06/12/2016	70,000	75,600
Rite Aid Corp.	7.500	03/01/2017	200,000	176,000
Rite Aid Corp.	9.500	06/15/2017	290,000	234,900
Sungard Data Systems, Inc.	4.875	01/12/2014	240,000	216,000
Sungard Data Systems, Inc.	10.625	05/15/2015	1,080,000	1,144,800
Verizon Pennsylvania Inc.	5.650	11/15/2011	2,220,000	2,364,766
Total				\$ 51,432,439

Real Estate Separate Account Pennsylvania Properties
(as of December 31, 2009)

<i>Real Estate Separate Account Pennsylvania Properties</i>			
<u>Property</u>	<u>Location</u>	<u>Description</u>	<u>Manager</u>
5 North Fifth Street	Harrisburg	5-story office building (PSERS headquarters)	Grosvenor
Total market value (unaudited) of Pennsylvania-based properties was \$8.0 million as of December 31, 2009.			

Pennsylvania-Based Private Equity/Venture Capital/Private Debt General Partners

(Dollar Amounts in Millions)

(Since the inception of the program as of December 31, 2009)

<u>Partnership</u>	<u>Location</u>	<u>PSERS Maximum Capital Commitment</u>
Adams Capital Management, L.P.	Sewickley	\$ 12.5
APA/Fostin Venture Fund I (closed)	King of Prussia	20.0
CEO Venture Fund I (closed)	Pittsburgh	1.0
CEO Venture Fund II (closed)	Pittsburgh	15.0
Co-Investment 2000 Fund, L.P.	Wayne	135.0
Co-Investment Fund II, L.P.	Wayne	135.0
Commonwealth Venture Partners I (closed)	Philadelphia	20.0
Commonwealth Venture Partners II (closed)	Philadelphia	10.0
Cross Atlantic Technology Fund, L.P.	Radnor	30.1
Cross Atlantic Technology Fund II, L.P.	Radnor	21.1
Graham Partners Investments, L.P.	Newtown Square	56.7
Keystone Minority Capital Fund (closed)	Philadelphia	0.1
Keystone Venture Fund IV (closed)	Philadelphia	7.8
LLR Equity Partners, L.P.	Wayne	62.5
LLR Equity Partners II, L.P.	Wayne	75.0
LLR Equity Partners III, L.P.	Wayne	187.5
Loyalhanna Venture Fund (closed)	Pittsburgh	15.0
Milestone Partners II, L.P.	Rosemont	29.9
Milestone Partners III, L.P.	Rosemont	60.0
NEPA Venture Fund I (closed)	Bethlehem	1.0
NEPA Venture Fund II	Bethlehem	5.0
Novitas Capital I, L.P.	Wayne	30.0
Novitas Capital II, L.P.	Wayne	75.0
P/A Fund	King of Prussia	30.0
PNC Equity Partners, L.P.	Pittsburgh	43.2
PNC Equity Partners II, L.P.	Pittsburgh	68.1
Quaker Bio-Ventures, L.P.	Wayne	69.4
Quaker Bio-Ventures II, L.P.	Wayne	100.0
SCP Private Equity Partners I, L.P.	Wayne	62.5
SCP Private Equity Partners II, L.P.	Wayne	125.0
TDH III, L.P.	Rosemont	7.4

**Pennsylvania-Based Private Equity/Venture Capital/Private Debt
General Partners**

(Dollar Amounts in Millions)

(Since the inception of the program as of December 31, 2009)

(continued)

<u><i>Partnership</i></u>	<u><i>Location</i></u>	<u><i>PSERS Maximum Capital Commitment</i></u>
Technology Leaders, L.P. (closed)	Wayne	\$ 10.0
TL Ventures III, L.P.	Wayne	50.0
Versa Capital Partners, L.P. (f/k/a Chrysalis)	Wayne	75.0
Versa Capital Partners III, L.P.	Wayne	<u>150.0</u>
<i>Total</i>		<u>\$ 1,795.8</u>

PSERS' PMEIM Program
Minority/Women Investment Managers
(Dollar Amounts in Millions)
(unaudited)

The following ten minority-owned or women-owned firms were under contract with PSERS to provide investment management services as of December 31, 2009:

<i>External Manager</i>	<i>Status</i>	<i>Market Value</i>
AH Lisanti	Women-owned	\$ 26.2
Ativo Capital	Minority-owned	19.0
Denali	Minority-owned	37.6
EDMP	Women-owned	45.4
Hanseatic	Women-owned	46.1
John Hsu	Minority-owned	69.5
Opus Capital	Minority-owned	33.4
Piedmont Investment Advisors	Minority-owned	19.1
Pugh Capital	Minority-owned	44.4
Shah Capital	Minority-owned	62.2
Total PSERS' PMEIM Minority/Women Owned Portfolios		\$ 402.9

Numbers may not add due to rounding

- *Health Options
Program*

- *Premium Assistance
Program*



Health Options Program

Health Options Program

Pursuant to Sec. 8502.1, PSERS sponsors a group health insurance program called the Health Options Program (HOP) for individuals who are annuitants or survivor annuitants or the spouse or dependents of an annuitant or survivor annuitant. The HOP is funded by and for eligible participants. The following is a summary of HOP initiatives during the period July 1, 2008 through June 30, 2009.

- The Retirement Board added a physical fitness benefit to its Medicare supplement plan covering 45,000 retirees and their dependents effective January 1, 2009. The benefit is a two-year pilot project to determine if a physical fitness program can be cost effective in a Medicare supplement environment. After evaluating the group's participation in the fitness classes and the impact on claims cost, the Retirement Board will decide whether to continue the benefit past the two-year period.
- The Retirement Board expanded the capabilities of the HOPbenefits.com website. The previous website provided general information about HOP and permitted users to download plan documents. The expanded website gives HOP Medical Plan participants access to personal health information and provide them with the ability to inquire and receive updates on the status of their claims. The updated website went online in November 2009.
- The Segal Company completed its 2008 claims audit of HOP's self-funded medical benefit plans administered by CoreSource, Inc. The claims audit concluded that not only did CoreSource provide excellent service, but that the financial accuracy, payment accuracy, procedural accuracy, and timeliness were exceptional and considerably exceeded industry standards.

Plans Available Through HOP

HOP offers participants a choice among a supplement to Medicare, various Medicare prescription drug plans, and a Medicare Advantage plan. Participants under age 65 and not eligible for Medicare may elect to enroll in a high deductible health insurance plan without prescription drug coverage or a managed care plan. These options are available to new enrollees or HOP participants electing to change coverage during the 2009 option selection period. HOP participants enrolled in a legacy Medicare Advantage plan or companion managed care plan, for individuals not eligible for Medicare, during 2008 may continue to participate in that plan for 2009. The following is a list of HOP plans:

For Individuals Eligible for Medicare:	For Individuals Not Eligible for Medicare
HOP Medical Plan (Medicare supplement)	HOP Pre-65 Medical Plan
Basic Medicare Rx Option (Medicare Part D)	HOP Pre-65 Medical Plan w/ Rx coverage
Enhanced Medicare Rx Option (Medicare Part D)	
HOP Managed Care Plan by Highmark	HOP Pre-65 Managed Care Plan by Highmark
Legacy Medicare Advantage Plans	Legacy Pre-65 Managed Care Plans
Aetna Golden Medicare	Aetna Patriot Plan
Aetna Medicare Value	Aetna Choice
Aetna Golden Choice	Keystone Health Plan East
Keystone 65	Keystone Health Plan East
Keystone 65 Direct	Keystone Health Plan East

Health Options Program
(continued)

IBC Personal Choice 65	IBC Personal Choice
Keystone Central Senior Blue	Keystone Central
UPMC for Life Medicare	UPMC
(PacifiCare) Secure Horizons	PacifiCare
Humana	Humana

HOP Premiums

Paid By Individuals ELIGIBLE for Medicare

The premiums paid by participants eligible for Medicare generally vary by geographical area. The exceptions are the premiums for the HOP Medicare Rx Options. The following is a summary of the monthly premium costs during 2009 and 2010 in Pennsylvania for single coverage:

Southeastern Region: Bucks, Chester, Delaware, Montgomery, and Philadelphia Counties	2009	2010	Increase
HOP Medical Plan	\$197	\$199	1%
<i>Age 65 Rate</i>	<i>\$188</i>	<i>\$190</i>	<i>1%</i>
HOP Managed Care Plan by Highmark†	\$244	\$257	5%
Legacy Medicare Advantage Plans	2009	2010	Increase
Aetna Golden Medicare HMO Value Plan (\$252 in Philadelphia County)	\$201	\$266	32-36%
Aetna Golden Medicare HMO (\$369 in Philadelphia County)	\$332	\$375	13-14%
Aetna Golden Choice PPO (\$370 in Philadelphia County)	\$365	\$411	11-13%
IBC's Personal Choice 65	\$564	\$591	5%
Keystone East HMO	\$301	\$350	16%
Keystone East POS	\$321	\$375	17%

Southwestern Region: Allegheny, Fayette, Greene, Indiana, Washington, and Westmoreland Counties	2009	2010	Increase
HOP Medical Plan	\$185	\$187	1%
<i>Age 65 Rates</i>	<i>\$176</i>	<i>\$178</i>	<i>1%</i>
HOP Managed Care Plan by Highmark†	\$232	\$245	6%
Legacy Medicare Advantage Plans	2009	2010	Increase
Aetna Golden Medicare HMO Value Plan	\$176	\$206	17%
Aetna Golden Choice PPO	\$388	\$255	-34%
Highmark Security Blue HMO	\$224	\$238	6%
UPMC HMO	\$157	\$207	32%

† Formerly called Highmark FreedomBlue PPO

Health Options Program
(continued)

Northern & Central Region: (All other counties in Pennsylvania)	2009	2010	Increase
HOP Medical Plan	\$155	\$157	1%
<i>Age 65 Rates</i>	<i>\$148</i>	<i>\$150</i>	<i>1%</i>
HOP Managed Care Plan by Highmark [†]	\$220	\$225	2%

Legacy Medicare Advantage Plans	2009	2010	Increase
Aetna HMO	\$209-\$291	\$203-\$284	-2 to -3%
Aetna Golden Choice PPO	\$312-\$388	\$227 to \$379	-27 to -2%
Highmark Security Blue HMO	\$224	\$238	6%
Keystone Central HMO	\$189	\$205	8%
Keystone Central PPO	\$197	\$213	8%
UPMC HMO	\$157	\$207	32%

[†] Formerly called Highmark FreedomBlue PPO

Medicare Rx Option: <i>All Counties in Pennsylvania</i>	2009	2010	Increase
Basic Medicare Rx Option	\$25	\$26	1%
Enhanced Medicare Rx Option	\$83	\$87	5%

HOP Premiums Paid By Individuals NOT ELIGIBLE for Medicare

The premiums paid by participants not eligible for Medicare generally do not vary by geographical area. The exceptions are the regional managed care plans. The following is a summary of the 2009 and 2010 premium costs in Pennsylvania for single coverage:

All Counties in Pennsylvania.	2009	2010	Increase
Pre-65 Medical Plan	\$566	\$569	0.5%
Pre-65 Medical Plan w/ Prescription Drugs	\$682	\$686	0.6%
HOP Pre-65 Managed Care Plan by Highmark [†]	\$852	\$918	8%

[†] Formerly called Highmark PPOBlue

Southeastern Region: (Bucks, Chester, Delaware, Montgomery, and Philadelphia Counties)

Legacy Pre-65 Managed Care Plans	2009	2010	Increase
Aetna HMO	\$743	\$917	23%
Aetna Choice POS	\$984	\$1,204	22%
IBC's Personal Choice 65	\$771	\$907	18%
Keystone East HMO	\$778	\$839	8%
Keystone East POS	\$774	\$835	8%

Health Options Program (continued)

Southwestern Region: (Allegheny, Fayette, Greene, Indiana, Washington, and Westmoreland Counties)

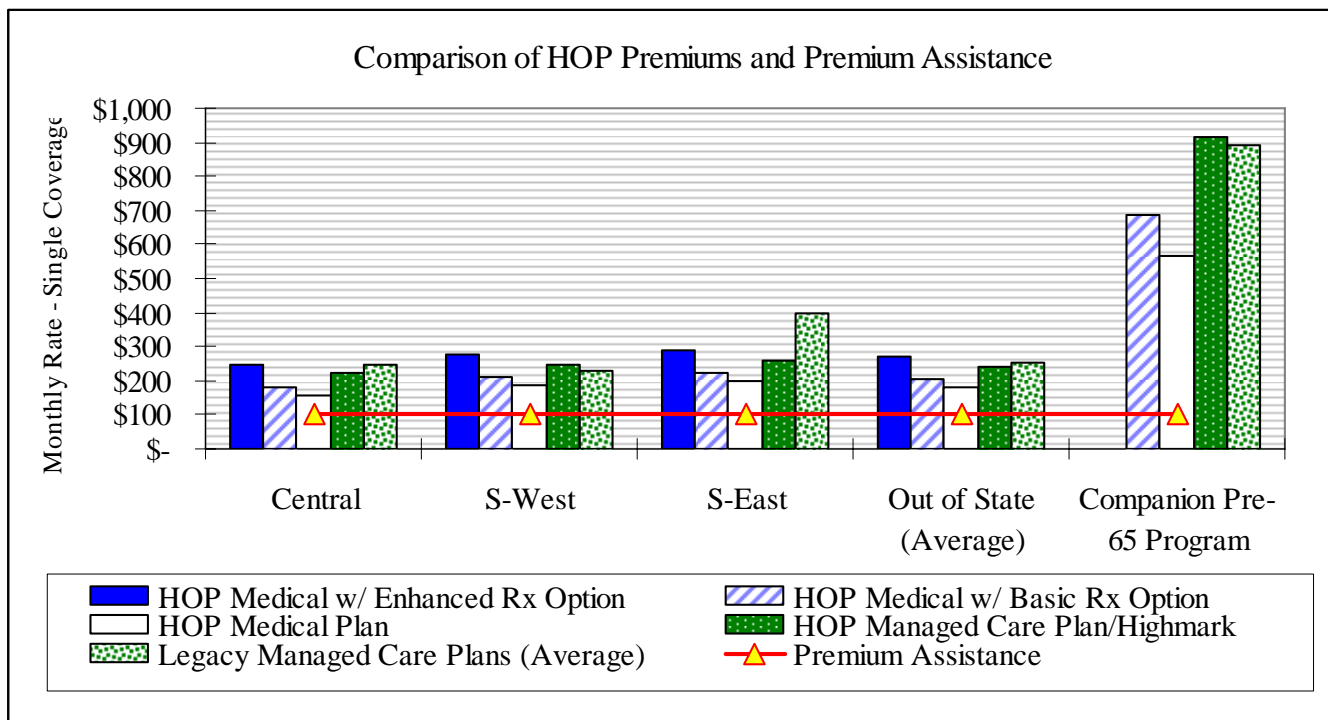
Legacy Pre-65 Managed Care Plans	2009	2010	Increase
Aetna HMO	\$710	\$903	27%
Aetna POS	\$846	N/A	
Highmark Keystone HMO	\$1,251	\$1,793	43%
Highmark PPO Blue	\$973	\$1,250	28%
UPMC HMO	\$1,045	N/A	

Northern & Central Region: (All Counties Not in Southeastern or Southwestern Regions)

Legacy Pre-65 Managed Care Plans	2009	2010	Increase
Aetna Patriot Plan HMO (Pittsburgh Only)	\$710	\$903	27%
Aetna POS	\$881	\$990	12%
Highmark PPO	\$973	\$1,250	28%
Keystone Central HMO	\$624	\$766	23%
Keystone Central PPO	\$774	\$968	25%
UPMC EPO	\$1,045	NA	NA

HOP Premiums Compared to the PSERS Premium Assistance Benefit

The following charts illustrate the HOP premiums paid by PSERS retirees for single coverage compared with the PSERS Premium Assistance benefit. The premiums for 2-person and family coverage would be at least twice the cost of single coverage. Premium Assistance is an offset for the PSERS retiree's premium, only.



Health Options Program
(continued)

	Central Region	Southwest Region	Southeast Region	Out of State (Average)	Companion Pre-65 Program
HOP Medical w/ Enhanced Rx Option	\$ 245.00	\$ 275.00	\$ 287.00	\$ 269.00	
HOP Medical w/ Basic Rx Option	\$ 183.00	\$ 213.00	\$ 225.00	\$ 207.00	\$ 686.00
HOP Medical Plan	\$ 157.00	\$ 187.00	\$ 199.00	\$ 181.00	\$ 569.00
HOP Managed Care Plan/Highmark	\$ 225.00	\$ 245.00	\$ 257.00	\$ 242.33	\$ 918.00
Legacy Managed Care Plans (Average)	\$ 244.00	\$ 227.00	\$ 395.00	\$ 252.00	\$ 891.00
Premium Assistance	\$ 100.00	\$ 100.00	\$ 100.00	\$ 100.00	\$ 100.00

The current Premium Assistance benefit will cover, on average, 38% of the fee-for-service premium (with the enhanced prescription drug coverage) and 41% of the managed care premium for retirees eligible for Medicare. The Premium Assistance benefit covers, on average, 13% of the premium for retirees not eligible for Medicare.

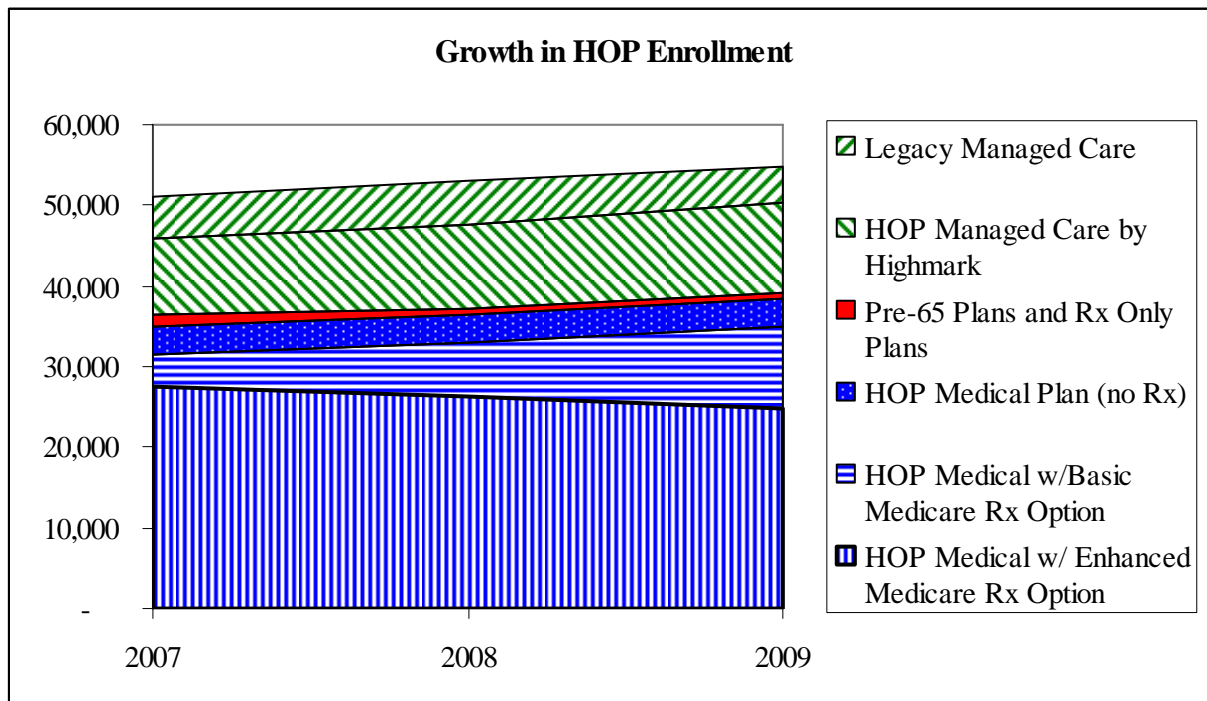
HOP Enrollment

As of October 1, 2009 there are 66,520 participants (54,790 retirees plus their dependents) in the HOP. The majority of the HOP participants were enrolled in the HOP Medical Plan with Enhanced Medicare Rx Option. The total numbers of retirees by Option are:

Eligible for Medicare	Participants
Self Funded Plans	
HOP Medical w/ Enhanced Medicare Rx Option	29,187
HOP Medical w/Basic Medicare Rx Option	12,345
HOP Medical Plan (no Rx)	3,931
Enhanced or Basic Medicare Rx Option (Rx only)	257
Managed Care Plans	
HMO Option	12,806
PPO Option	6,900
POS Option	212
Total Eligible for Medicare	65,638
Not Eligible for Medicare	
Fee-For-Service Plans	
HOP Pre-65 Medical Plan w/Rx (High Option)	194
HOP Pre-65 Medical Plan (Standard Option)	173
Managed Care Plans	
HMO Option	212
POS Option	82
PPO Option	221
Total Not Eligible for Medicare	882
Total Participants	66,520

Health Options Program (continued)

The following graph illustrates the number of retirees (not counting dependents) in the various options from October 2007 to October 2009:



Funding

A majority of the premium income is deducted from the retiree's monthly retirement benefit and transferred to the plans (claims administrator for the self-funded Options). Approximately 5,000 retirees submit monthly premium payments to the HOP Administration Unit, as their monthly retirement benefits, if any, are insufficient to cover the premium cost. In addition, individuals enrolled in a Medicare Rx Option without HOP Medical Plan coverage must submit monthly premium payments.

HOP income will total approximately \$225 million during the 2010 Plan Year. A majority of this income comes from premium payments from participants. Other sources of funding are Medicare prescription drug payments (for participants enrolled in a Medicare prescription drug plan) from the Center for Medicare and Medicaid Services (CMS) and investment income. The following is a breakdown of these sources of income:

Income	2010 (in millions \$)
Participant Contributions	\$194
CMS - Medicare Prescription Drug Payments	30
Interest Income	1
Total	\$225

Health Options Program
(continued)

PSERS retirees enrolled in HOP, who meet the eligibility requirements for Premium Assistance, receive \$100 per month as a partial reimbursement for the out-of-pocket premium expense. Approximately 46,500 of the 66,900 HOP participants receive Premium Assistance. This accounts for about \$56 million of the \$83 million annual expenses for the Premium Assistance Program. The following Premium Assistance Program section provides additional information.

Contributions and interest income pay for the benefits provided to HOP participants plus administrative expenses. The following is a breakdown of the benefit expenses:

Benefit Expenses	2010 (in millions \$)
Self-funded Hospital, Medical & Major Medical Benefits	\$ 90
Self-funded Prescription Drug Benefits	64
Managed Care Contributions	66
Total	\$ 220

In addition to the benefit expenses identified above, the HOP will pay \$5.5 million in enrollment and administrative expenses including reimbursing PSERS for its expenses.

As of June 30, 2009, HOP had net assets of \$106 million held in trust to pay the expenses of HOP for the exclusive benefit of participants

Premium Assistance Program

Premium Assistance Program

In accordance with Sec. 8509, PSERS provides up to \$100 per month in Premium Assistance to eligible retirees to help cover the cost of their health insurance. The eligibility requirements for premium assistance are as follows:

- 24.5 years of credited service, or
 - 15 years of credited service if termination of employment and retirement occurred after age 62, or
 - Receiving a Disability annuity from PSERS;
- and
- Have an out-of-pocket premium expense from their former school employer's health plan or the PSERS sponsored Health Options Program (HOP).

The Retirement Board is charged with the responsibility of determining what plans are approved for Premium Assistance. The policy established in 1993, was intended to provide Premium Assistance to retirees who continued their active employee coverage until age 65 or who enrolled in a group health insurance plan for Medicare eligible retirees managed by their former school employer. The approval policy was reviewed in consideration of changes in the retiree health insurance market place since 1993 and the Retirement Board amended the policy effective January 1, 2010. The new policy sets forth basic requirements a school employer must meet to be approved for Premium Assistance. The restated policy is not intended to interfere with a Public School's compliance with Act 110, collective bargaining process, the selection of insurance carriers, funding methods, or establishing the level of basic hospital, medical and major medical benefits provided by the plans. The operative section of the Plan Approval Policy is Section III, D of the Policy which states:

If a School Entity offers the same group health benefit plans to its retirees that it offers to active employees, then the School Entity can be considered to be in compliance with the Approved Plan criteria with regard to those plans.

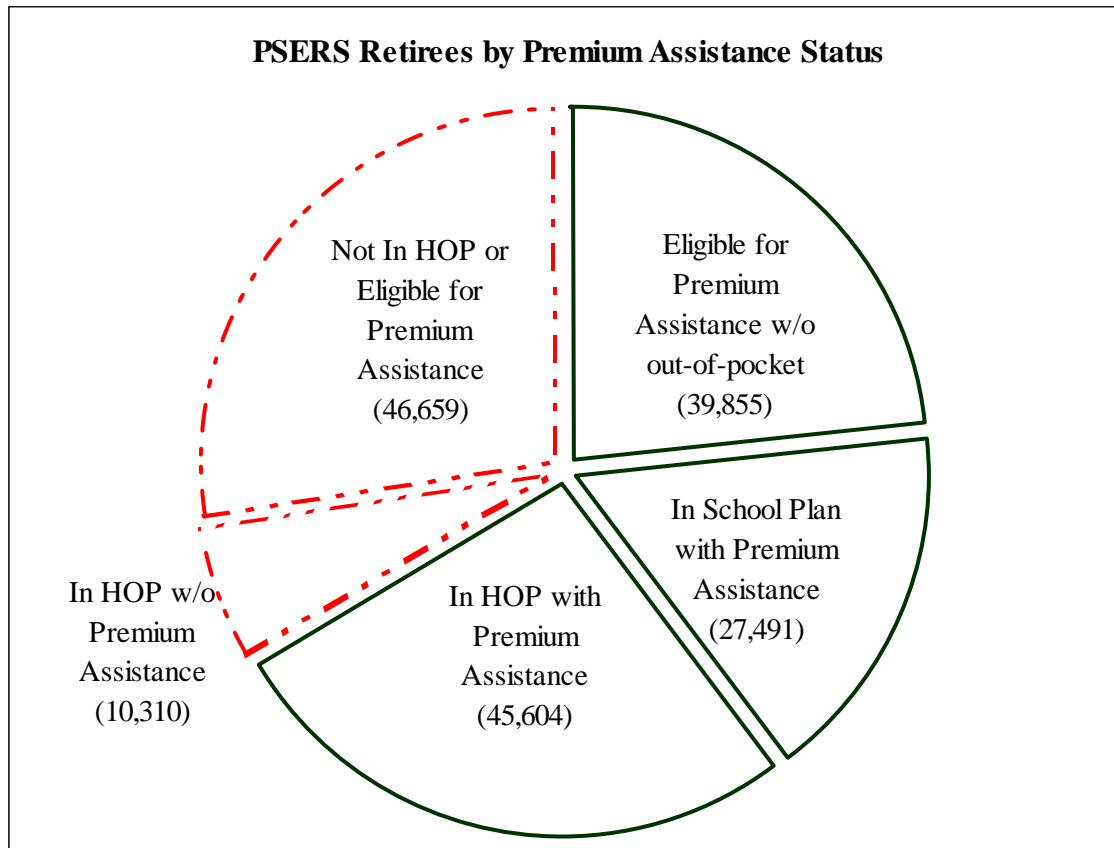
School employers that offer a plan that is not the same group health benefit plan offered to active employees, such as a Medicare Advantage or Medicare supplement plan, must meet certain criteria to be approved for Premium Assistance. For example, if a public school endorses or recommends an individual health insurance policy sold through an independent commissioned agent and is not a party to the contract or pays a portion of the premium, that "plan" will not be approved for Premium Assistance. This policy modification protects PSERS ability to offer retirees and their dependents group health insurance and minimizes premium costs associated with adverse selection.

Enrollment

As of June 30, 2009, PSERS had 169,919 retirees (excluding survivor annuitants and beneficiaries) receiving a monthly benefit. Of these retirees 112,950 meet the service, service and age at termination of school service, or retirement type (disability) eligibility requirements for the premium assistance program. Of the retirees meeting these requirements, 39,855 are not receiving premium assistance payments because they do not have an out-of-pocket premium expense from an approved plan. Of the 73,095 retirees receiving premium assistance benefits, 45,604 are enrolled in HOP and 27,491 are participating in their former school employer's health plan and have an out-of-pocket premium expense.

Premium Assistance Program (continued)

A breakdown of retirees by their premium assistance status is as follows:



June 30, 2009	Number	Percentage
Eligible for Premium Assistance without an Out-of-Pocket Expense from an Approved Plan	39,855	23%
Receiving Premium Assistance In School Plan	27,491	16%
Receiving Premium Assistance In HOP	45,604	27%
In HOP without Premium Assistance	10,310	6%
Not In HOP or Eligible for Premium Assistance	46,659	27%
Total Retiree Population ¹	169,919	100%
Eligible ² For Premium Assistance	112,950	

¹ As of June 30, 2009 Actuarial Valuation (Excludes Survivor Annuitants and Beneficiaries)

² Meeting the service, service and age at termination of school employment or retirement type requirements.

Funding

The Premium Assistance Program is funded by employer contributions. The PSERS Actuary determined that the contribution needed during the 2010/2011 fiscal year was 0.64% of payroll. For the year ended June 30, 2009, employer contributions equaled \$92.5 million and net investment income equaled \$1.9 million. During this period, PSERS paid Premium Assistance benefits equaling \$83.2 million and incurred administrative expenses of \$1.8 million. As of June 30, 2009, the Premium Assistance Program had net assets of \$105.1 million.

